Charitable Alliance

Friday 8 June 2012

Charitable Alliance
c/- Community Council for Australia
Level 1, The Realm, 18 National Circuit
Barton, ACT, 2600

The Hon. Wayne Swan MP, **Deputy Prime Minister and Treasurer**
The Hon. David Bradbury MP, **Assistant Treasurer**
The Hon. Bill Shorten MP, **Minister for Financial Services and Superannuation**
The Hon. Mark Butler MP, **Minister for Social Inclusion**

P.O. Box 6022
House of Representatives
Parliament House
Canberra ACT 2600

Dear Ministers,

Professional Trustee Company (PTC) Issues
Excessive fees & governance issues cost Australian community millions annually

We write as an '*Alliance*' of concerned trustees, advisors to and stakeholders of Charitable Trusts and Foundations (**Charitable Alliance**) that continue to provide significant financial and other support to communities across Australia, to request:

1. A formal review of the Corporations Amendment *(Financial Services Modernisation)* Act 2009 (**CAFSMA**), in line with the explanatory memorandum (**EM**) of the CAFSMA that states "the Government is committed to a review of the fee arrangements in relation to charitable trusts after two years of operation". We note that May 2012 is two years since the CAFSMA came into effect in May 2010.

   We also note that Charitable Alliance representatives have been unable to access details of the committed two year review. From phone calls and meetings in March and April 2012, it appears no review is currently underway or planned. Calls and or meetings were held with:
   - Treasury Department Liaison Officer;
   - Treasury Corporations & Capital Markets Division;
   - Office of the Minister for Financial Services & Superannuation; and
   - Management of the Retail Investor Division of Treasury.

2. Where the Charitable Alliance's concerns are not captured in the CAFSMA Review (*item 1*), that the Federal Government undertakes a broader review and implement necessary legislative changes to address serious issues relating to the role of PTCs in the governance and administration of Charitable Trusts and Foundations in Australia – refer **Briefing Note B** *(attached)*.

To support this formal request, attached to this letter are some preliminary briefing notes on issues relating to PTCs and their role in the governance and administration of Charitable Trusts & Foundations in Australia:

A. Role of, fees charged by & changed nature of PTCs (**Briefing Note A**)
B. Issues requiring review (**Briefing Note B**)

Absent a court application to remove a PTC, there is no mechanism to change from one PTC to another. Where the PTC is the sole trustee, any such court application would be novel. Therefore PTCs are not exposed to competition and lack accountability. Charitable Trusts & Foundations may not obtain services at the lowest possible price. Unfortunately, this leads to significant decreases in financial and other support to disadvantaged communities across Australia, the ultimate beneficiaries of the Charitable Trusts & Foundations.

Lack of portability is very rare in the financial services sector. For example, Australian consumers have the freedom to move their superannuation benefits from one fund to another and consequently benefit from increased competition. The Federal Government has also recently made it both less burdensome, administratively and financially, for Australian consumers to transfer their mortgages to another bank. The desirability of introducing portability of PTCs to the Charitable Trusts & Foundations sector is compelling.

Please note this letter seeks to bring this matter to the Federal Government's attention and seek pro-active review and changes. However is not intended to be a comprehensive submission.

This matter is of extreme importance to our many community organisations that are adversely impacted significantly by the existing legislation.

The Charitable Alliance requests that The Federal Government:

1. Confirm that a formal review of the CAFSMA will occur in line with the explanatory memorandum;
2. Notify the Charitable Alliance of the CAFSMA review details when finalised, to allow a formal submission(s) to be made; and
3. Ministers meet with Charitable Alliance representatives to discuss these important issues for Charitable Trusts & Foundations – organisations that are committed to supporting those in need in our community.

Kind Regards,

Graeme Danks
Honorary Trustee
Danks Trust

Sandy Clark
Chairman
William Buckland Foundation

Tim Costello AO
Chairman
Community Council for Australia (CCA)

This letter is sent on behalf and with the endorsement of an '*Alliance*' of the following concerned trustees of, advisors to and stakeholders of Charitable Trusts and Foundations:

Peter Yates AM, **Chairman Designate, Royal Children's Hospital Foundation, Melbourne**
Simon McKeon, **Chairman, Global Poverty Project Australia & Business for Millennium Dev't**
Ian Smith, **Director, Baker IDI Heart & Diabetes Institute Holdings Ltd** *(Partner, Bespoke Approach)*
David Crosbie, **CEO, CCA & Member, Not-for-Profit Sector Reform Council**
Richard Leder, **Deputy Chairman, Royal Children's Hospital Foundation, Melbourne**
Sue Hunt, **Executive Director, Royal Children's Hospital Foundation, Melbourne**
Graeme Sinclair, **Trustee, William Buckland Foundation**
Jane Gilmour OAM, **Trustee, William Buckland Foundation**
Martyn Myer AO, **President, The Myer Foundation**
Leonard Vary, **CEO, The Myer Foundation & Sidney Myer Fund**
Peter Winneke, **Head of Philanthropic Services, The Myer Family Company**
Dr John Baxter, **Chairman, Percy Baxter Charitable Trust**
Denis Tricks AM, **Chairman, Hugh Williamson Foundation**
Martin Carlson OAM, **Trustee, Hugh Williamson Foundation**
Elizabeth Cham, **IPCS** *(Former CEO, Philanthropy Australia)*
Jill Reichstein OAM, **Chair, Reichstein Foundation**
Esther Abram, **Chief Executive Officer, Changemakers**
Alan Froud, **Deputy Director, National Gallery of Australia**
Andrew Danks, **Honorary Trustee, Danks Trust**
Mike Danks, **Honorary Trustee, Danks Trust**

Copied to: Robert Fitzgerald (Chair) & Susan Pascoe (CEO), ACNC
Sue Vroombout / Irene Sim & Simon Milnes, Retail Investor Division, The Treasury

Charitable Alliance

Professional Trustee Company (PTC) Issues
Briefing Note A: Role of, fees charged by & the changing nature of PTCs

The issues identified below result in the **reduction of tens of millions of dollars every year** to the funds available to be distributed in grants to not-for-profit organisations who support important needs in the Australian community.

1. Australian trustee companies administer circa 2,000 Charitable Trusts and Foundations with assets of approx. $3.3 billion, usually as sole trustee. During 2008/09 these trusts are understood to have distributed circa $180 million in grants to the Australian community.

2. When many of the trusts were formed (many in the late 1800's and early 1900's), PTCs were 'pure' Trustee Companies. Today they are often subsidiaries of mainstream commercial financial service providers, with 'trusts' forming a minor part of their business (circa $3.3bn against a total assets managed of over $500bn).

3. The Corporations Legislation Amendment Act 2009 - Financial Services Modernisation (**CAFSMA**), inserted Chapter 5D into the Corporations Act 2001 (Cth) (Corps Act), resulted in changes to the Act that captured 'Trustee Companies' including their role as 'professional' trustees. The CAFSMA refers to an annual fee of 'up to' 1.056% of *capital*. Such a change to the fee structure results in a significant increase in the fees payable to Trustee Companies by many Charitable Trusts & Foundations, thereby reducing substantially the funds available to support those in need in the community.

4. The CAFSMA does not deal with, or limit, the range of other additional fees that are often charged by PTCs over and above the fee structure outlined in the CAFSMA, including, but not limited to, Investment Management or Advisory fees – fees which are not regulated and in many cases are not independent and or competitively tendered. These additional fees further reduce the funds available to support the Australian community.

5. The CAFSMA took effect on 6 May 2010. The explanatory memorandum of the CAFSMA states that "the Government is committed to a review of the fee arrangements in relation to charitable trusts after two years of operation" (paragraphs 2.66 & 7.162 of the EM). This is in relation to the fee arrangements for both existing and new charitable trusts (paragraph 2.93). Two years is May 2012. As at May 2012, it appears no review is currently underway.

6. A large portion of the fees charged by PTCs are paid by Charitable Trusts & Foundations established with monies left by deceased individuals and families on the understanding that the trust/foundation would be maintained in perpetuity for the benefit of the most disadvantaged in the community. In the majority of cases:
   A. The founders, nor any descendants, are no longer there to advocate on their behalf; and
   B. There are no independent trustees to:
      - Ensure independence between the governance role of a trustee and the provision of a range of paid services; and or
      - Challenge additional fees charged over and above the substantial CAFSMA fees under.

   So, in practice, a PTC's 'profit' arm, can tell itself, as the sole trustee of Charitable Trusts & Foundations, that certain fees will be charged and increased at its discretion.

NOW is the time to address the loss to the Australian community of tens of millions of dollars every year. The substantial reduction in funds Charitable Trusts & Foundations are able to distribute to those in need in the community is being reduced at a time when the structure of the Australian economy is changing at a rapid rate, resulting in:

- Ever increasing demands on governments and not-for-profit organisations; and
- A reduction in available funding to not-for-profit organisations from other non-government sources, compounded by many larger not-for-profit organisations' own investments being impacted by the flow on effects of the current uncertainty in global economies

Charitable Alliance

Professional Trustee Company (PTC) Issues
Briefing Note B: Issues Requiring Review

1. Fee Calculation

Recent amendments to legislation (**CAFSMA**) resulted in the method of calculating PTC's fees changing to be a % of *capital*. In many cases that we are aware of, this has resulted in a significant increase in fees being charged to Charitable Trusts & Foundations by PTCs, often with no increase in services provided. Historically, most Charitable Trusts & Foundations have been charged a small percentage of annual *income*. To demonstrate the significant impact of this change, a number of '**Case Studies**' will be provided to the CAFSMA review. In the meantime, two current examples follow showing the significant fee increases being demanded by two PTCs:

A. **Example A**: Trust assets = $17.5m. 'Will' prescribes the fee at 2.5% of income (~$20,000 to $30,000/year). Post-CAFSMA this PTC is now demanding its '*statutory fee entitlement*', which equates to ~$170,000/year. Increase = $140,000 (550% to 650%).
B. **Example B**: Trust assets = $57.2m. Pre-CAFSMA PTC fee = ~$179,000/year. Subject to the interpretation of the 'grandfathering provision', the post-CAFSMA fee could be either $328,000 or $604,000/year. Increase = either $149,000 (83%) or $425,000 (237%).

2. 'Grandfathering'

Recent amendments (CAFSMA) were 'intended' to 'grandfather' prior arrangements. Due to a lack of clarity in the legislation and 'heavy handed' approach applied by the PTCs, this intention has not been achieved.

3. 'Portability'

Australia is unusual in that in many cases individual (honorary) trustees must take court action (at significant risk, time & expense) in order to seek removal of a PTC as a co-trustee (e.g. due to poor service or excessive fees). This results in an inefficient trustee company sector, inflated fees and significantly less funding available for distribution to the Australian community through not-for-profit entities. The introduction of 'portability' of the 'Professional Trustee' role, exercised through a regular competitive tender process for co-trustees and sole trustees would address many of these issues, allowing market forces to bring efficiency to the sector.

4. Transparent Reporting

PTCs manage about 2,000 Charitable Trusts & Foundations, only a handful of which report publicly. Accordingly there is no transparency of these trusts at all. Transparency is required particularly for those Charitable Trusts & Foundations where a PTC is the sole trustee. Issues that can arise in such situations include the inability to ensure fees charged are equitable given the level of services provided. A regulator, such as the Australian Charities and Not-For-Profit Commission (**ACNC**), could monitor this field and have the ability to dismiss a sole trustee due to poor service or excessive fees. Reporting could be a simple process. A return could:

- Be completed for each trust each year;
- Include financial statements, list of grants made and detailed expenses including PTC fees;
- Allow a regulator to review these trusts' activities (currently not monitored by any external body) and be alert for abnormal activities, including excessive fees; and
- Allow for aggregate information to be released on the size & scope of the philanthropic sector.

5. Governance Independence

An inherent conflict exists across Charitable Trusts & Foundations, where PTCs fulfil roles as both:

A. Trustee - 'governance', for which fees can be charged under the CAFSMA; and
B. Paid Service Provider roles (e.g. investment advisory, compliance, administration and or grant making), for which additional unregulated fees are charged, on top of CAFSMA fees.

This issue is heightened where a PTC is the sole trustee of a Charitable Trust, where founders are no longer alive and there is no independent trustee(s). Independence would open the sector to additional service providers and competition. Independent governance could be achieved by regulating the obligation to separate:

- The 'governance' function as legal 'trustee'; and
- Fee charging service provision.

That is, a paid Trustee may not also be a paid service provider to the same / related trust to which they are a trustee. Beyond independence this will allow efficiency through market forces.

Charitable Alliance

Charitable Alliance
c/- Community Council for Australia
Level 1, The Realm, 18 National Circuit,
Barton, ACT, 2600

Friday 21 December 2012

Corporations and Markets Advisory Committee
Level 16, 60 Margaret Street
SYDNEY NSW 2000

Attention: Mr John Kluver, Executive Director
By email: camac@camac.gov.au

Dear John,

The introduction of the *Corporations Amendment (Financial Services Modernisation) Act 2009* (**CAFSMA**) changed the regulation of fees charged by licensed Trustee Companies (**TCs**) to charitable trusts.

The Charitable Alliance wishes to thank the federal government for recognising the need to undertake a review of the activities of TCs and the portability of their services and the Corporations and Markets Advisory Committee (**CAMAC**) for agreeing to undertake the review.

Please find attached the Charitable Alliance submission to the CAMAC Review.

The Charitable Alliance is an alliance of very concerned trustees, advisors to and stakeholders of Charitable Trusts and Foundations (*refer Annexure 1 of the submission*) that:

- ✓ Have a corpus that in aggregate exceeds $1 billion;
- ✓ Provide support to the community exceeding $1 billion annually; and
- ✓ Engage with, and are focussed on the support of, those in need in communities across Australia

The flow on effects of the CAFSMA has highlighted issues that extend beyond the regulated fees to a range of issues that are impacting on the core 'charitable purposes of trusts'. Our submission seeks to highlight these issues and present a range of solutions or recommendations.

The issues impacting on charitable trusts are not just about fees or portability or ASX listed TC's excessive profits at the expense of the communities - at the heart of all these issues is the strength of our communities.

In the interests of those most in need in our communities, for generations to come, the Charitable Alliance asks CAMAC to ensure the fundamental goal of changes to charitable trust regulations or operations is to strengthen their capacity to fulfil their *charitable purpose*.

Please confirm to Graeme Danks (gdanks@danks.com.au) that CAMAC received this submission.

Kind regards

Graeme Danks
Honorary Trustee
Danks Trust

Sandy Clark
Chairman
William Buckland Foundation

Tim Costello AO
Chairman
Community Council for Australia (CCA)

Charitable Alliance Submission to CAMAC Review of Charitable Trusts and Foundations

The introduction of the *Corporations Amendment (Financial Services Modernisation) Act 2009* (**CAFSMA**) changed the regulation of fees charged by licensed Trustee Companies (**TCs**) to charitable trusts.

The Charitable Alliance thanks the federal government for recognising the need to undertake a review and the Corporations and Markets Advisory Committee (**CAMAC**) for agreeing to undertake the review.

1. Charitable Alliance

The Charitable Alliance is an Alliance of concerned trustees, advisors to and stakeholders of Charitable Trusts and Foundations (**Charitable Trusts**) that provide significant financial and other support to communities across Australia.

The Charitable Alliance includes stakeholders of a range of charities, grant making trusts and foundations, including Private Ancillary Funds (PAFs) that:

- ✓ Have an corpus that in aggregate exceeds $1 billion
- ✓ Provide support to the community exceeding $1 billion annually
- ✓ Engage with, and are focussed on the support of, those in need in communities across Australia

A list of the Charitable Alliance members is included as **Annexure 1.**

The Charitable Alliance letter to the federal government on 8 June 2012 forms **Annexure 2**.

A background to Charitable Trusts in Australia forms **Annexure 3**.

Provides support to the community ***exceeding $1 billion annually***

In line with CAMAC's terms of reference, the Charitable Alliance submission will address:

- An overview of charitable trusts in Australia and the problems associated with their relationship with TCs
- Case studies illustrating the quantum of fees that are or could be charged to Trusts by TCs, and what fee arrangements would be available on the open market
- Case studies illustrating what fees may be charged by TCs that are not regulated by CAFSMA
- The regulation of "new" fee arrangements and provide recommended proposals for reform
- The effectiveness of the "grandfathering" regime, and some proposals for reform
- A discussion of issues regarding the removal and replacement of trustees of charitable trusts, and proposals for reforms that may assist with portability
- Other issues that impact on the objectives of CAFSMA or the charitable purposes of trusts

The Charitable Alliance proposes that CAMAC recommend to government:

Recommendation 1: Pricing Reform

- ✓ Ensure the fee in the Corporations Act is a 'maximum' rather than an 'entitlement' and the calculation of a 'maximum' fee not be linked to a % of capital, rather the 'maximum' fee be:
  - Capped at 5.5% of income annually (incl. GST); and
  - A one off establishment fee in the first year only (again as a % of income) – aimed at recognising the additional work involved for the TC in the first year)
- ✓ Ensure TCs are obliged to set "just and reasonable" fees that reflect the time and effort involved in the service provided (*allowing for the benefits of 'centralised' management*)
- ✓ In respect of "grandfathering", clarify the legislation to preserve the actual quantum of fees charged prior to CAFSMA
- ✓ Set a transparent mechanism for setting and reviewing total fees charged to charitable trusts to ensure that TCs are acting fairly
- ✓ Reduce the cost of the fee review mechanism by removing the need to go to a Court at first instance to resolve a dispute about fees
- ✓ Make 'failure to comply with pricing requirements' a trigger for a TC to be replaced as the manager of a charitable trust

Recommendation 2: Governance Reform

2A: Transparency

- ✓ Improve competition between TCs through transparent reporting obligations from which valid comparisons can be made on pricing in the market
- ✓ Ensure the person empowered to decide which TC should manage the charitable trust has sufficient information to make an informed decision

2B: 'Independent' Advice

- ✓ TCs be required to seek independent advice before investing the funds of charitable trusts in the financial instruments of companies related to the TC

2C: Orphan trusts

- ✓ Prevent orphan trusts from being created by legislating that TCs receiving fees from a charitable trust must constitute a minority of the trustees of that charitable trust
- ✓ Protect existing orphan trusts by requiring the appointment of new trustees and independent "responsible persons"

2D: Portability & Effective Competition

- ✓ Promote portability by ensuring someone has the power to decide which TC should manage a charitable trust (*this could be a peer review body modelled on ASIC 'Takeovers Panel'*)
- ✓ Adopt a cost effective mechanism for choice about which TC should manage a charitable trust
- ✓ Remove barriers to entry into the market of managing charitable trusts by creating a new class of AFSL licence dedicated to the management of charitable trusts (only)

2E: Dispute Resolution

- ✓ Implement a cost effective dispute resolution system to manage disputes between TCs and other co-trustees (i.e. *the same peer review body modelled on ASIC 'Takeovers Panel'*)

2. Background

A. Third Pillar of Economy, but First Pillar of Society

The recent issues impacting on charitable trusts are not just about fees or portability or ASX listed trustee company's excessive profits at the expense of the communities. At the heart of all these issues is the strength of our communities.

Charitable trusts play a vital role in building community resilience, inter-connectedness and citizenship across Australia. They are a long established vehicle to enable people to contribute to the groups and causes that matter to them, a way of establishing on on-going gift to the community. So significant is this act of giving that the government rightly provides tax concessions and other benefits to charitable trusts, provided they direct their distributions to charitable purposes. Governments give concessions to this sector in recognition of the fact that it is the third pillar of the economy and the first of society.

*This issue **affects most Australians** – whether through their hospital, school, life saving club, community group, welfare services, medical research or many others – **impacting directly on the strength of our communities***

Charitable trust funding supports thousands of charities across Australia, enabling them to extend and sustain their invaluable work. The real benefit of charitable trusts cannot be measured in financial terms, but we know that many organisations would have to reduce their services to the community, or even close if it were not for the trust funding they receive.

The fundamental goal of any change to charitable trust regulations or operations must be to strengthen their capacity to fulfil their *charitable purpose*. This goal should be the touchstone for governments, regulators, trustee companies, trustees, beneficiaries, and the broader community in considering how best to address emerging concerns about reduced distributions and mission drift away from the core purpose of charitable trusts.

B. Ever Increasing Demands on Government

This CAMAC Review is occurring at a time when state and federal governments (*of all political parties*) are struggling to keep up with demands on them from the community for basic services and many would argue human rights. For example, is CAMAC aware that:

- In 2009 government reported a shortage of over 170,000 affordable houses, a shortage that is projected to rise to over 600,000 houses by 2030. To put this in context, the $5.6 billion spent on the National Homelessness Partnership built just 20,000 houses (<11.7% of 'gap')
- By 2050 projections show that in Australia:
    - The number of Australians > 65 years old will have doubled
    - Australia's workforce < 65 years old will have halved (*i.e. tax payers*)
    - Cost to government of core service delivery is expected to have increased by >300%

*Australian governments and Australians needs an efficient competitive and pro-active charitable sector supported by 'trusted guardians' **if Australia is to maintain the style of society we have enjoyed and future generations deserve**.*

C. Australia has lost its 'trusted guardians'

Charitable Trusts are generally established by monies left by generous (deceased) individuals and families on the desire to benefit the most disadvantaged in the community. On establishing a Charitable Trust, the founder often elected to appoint a '*licensed* Trustee Company' (**TC**) as a trustee of the charitable Trust - as 'guardian' of the 'charitable purpose' of their community 'gift'.

Unfortunately, since many TCs were appointed as a '*trusted guardian*' in the 1900's, the 'core purpose' of TCs has changed significantly:

- When appointed TCs were 'pure' trustee companies – in essence '*trusted guardians*' on behalf of the beneficiaries ... the Australian community. TCs were essentially publicly owned bodies whose sole function was to manage trusts and other traditional services ... to prudently guard the assets of Charitable Trusts on behalf of those in need
- Today most TCs are divisions of ASX listed profit driven financial services companies, with gross profit expectations of 30 to 50%. Directors of TCs have a direct conflict between their fiduciary duties to shareholders as a Director and to the community as 'trusted guardian' of Charitable Trusts

Trustee companies that were 'trusted guardians' are today an 'arm' of ASX listed profit driven financial services companies

The Charitable Alliance argues to CAMAC that CAFSMA:

- Does not protect and or support the 'charitable purpose' of Charitable Trusts
- Results directly in tens of millions of dollars intended to benefit the community, being paid directly to listed financial services companies
- Highlights some serious macro-issues that surround the governance and operation of TCs in their roles as trustees of Charitable Trusts in Australia

Nothing illustrates this more starkly than the extensive pro-active lobbying undertaken by the Trustee Corporations Association of Australia (**TCA**) - now part of the Financial Services Council (**FSC**) - in 2008 to introduce the federal **CAFSMA** legislation.

It is interesting to note that in TCA's July 2008 submission, the TCA stated as follows:

- Page 7 under 'Fees' - "*We believe that competitive forces, as in other industries, should be allowed to determine a reasonable level of fees commensurate with the work and responsibilities involved in providing estate and trustee services*."
- Page 5 under 'Removal of Trustees' – "*We believe that the ability of beneficiaries to remove a trustee should remain restricted to circumstances of breach of trust or gross negligence, and continue to be a matter for the relevant supreme court*"

Note: trustees in the Charitable Alliance have been advised that to remove a trustee in the supreme court could cost $0.5m and if the 'independent' trustee were to loose the court could rule the individual is liable for the costs of both parties.

The Charitable Alliance asks CAMAC to consider - how does CAFSMA:

- Develop a competitive national market for TCs?
- Encourage new entrants

CAFSMA legislation ***compromises the core 'charitable purpose'*** *of charitable trusts at the expense of ASX listed licensed Trustee Companies … reducing funds available to* ***support those in need in our community by tens of millions of dollars per annum***

Background (continued ...)

D. Policy mandate: Transparency + Competition = Stronger Communities

The introduction of competition in the market for TC services by providing Charitable Trusts with this option would be consistent with principles of transparency and accountability, and is particularly relevant in a deregulated, market driven economy.

The introduction of true competition will improve consumer protection by forcing TCs to provide a high quality, cost effective service to Charitable Trusts ... but only if legislation allows that if they fail they can and will lose the business.

Early in 2012 Min Bill Shorten wrote to Senator Bob Brown advising that *"... An important objective of the new regime (CAFSMA) was to encourage the development of a competitive national market for trustee companies and to encourage new entrants.*"

Again, the Charitable Alliance asks CAMAC to consider - how does CAFSMA:

- Develop a competitive national market for TCs?
- Encourage new entrants?

E. Policy Consistency

It is essential that the Commonwealth Government gets these reforms right and aligns where possible with the valuable objectives recently endorsed by:

- Recent reforms introducing 'portability' (competition) to key segments of the Australian market including **superannuation, insurance, home loans and banking**

  Ensuring **competition through portability** will deliver better contribution to the 'charitable purpose' of Charitable Trusts. Consumer choice in perpetual trusts can only ever be considered at a point in time. This ought not be limited to the time the trust was created, having regard to the changing nature of TCs, the competitive market, and contemporary governance. Any reforms must better protect those who are no longer able to oversee trusts they established.

- Passage of the *Australian Charities and Not-For-Profits Commission Bill 2012* (**ACNC Bill**):
  - Maintaining, protecting & enhancing public trust and confidence in the charitable sector as essential to its ongoing sustainability, including the ability to provide services to the public
  - A national regulatory system that promotes good governance, accountability and transparency for charitable entities, including charitable trusts, to also enhance public trust and confidence that underpins the sector.

Guiding policy principles for assessment of reforms must remain true to the original aims of CAFSMA:

- *Increased consumer protection and transparency*
- *Introducing market competition*
- *Reducing regulatory burden on TCs in respect of interstate regulatory requirements*

Ultimately the recommendations of CAMAC concerning the **impact of quantum of fees for both existing and new trusts on net distributions** must be aimed at maximising community benefit after fair reward for TCs governed by fair payment for work done based on the services provided.

Good policy dictates that fees should not be driven by expected profit margins for TCs – for whom philanthropy management is now often a business 'arm' of a large commercial financial service provider with managing trusts only a small part of their business which has fiduciary duties to its shareholders.

3. The Impact of CAFSMA

CAFSMA allows TCs, for matters commencing after 10 May 2010, being able to charge 1.056% of capital, which presents a range of issues:

- A fee based on a % of capital has no connection to the cost of providing the services
- It creates an additional conflict as it has the potential to incentivise TCs to keep funds in the corpus of the trust when it may be more appropriate to make distributions
- There is real potential that investment strategies and decisions will be influenced inappropriately by the potential to generate (in many cases significantly) larger fees.

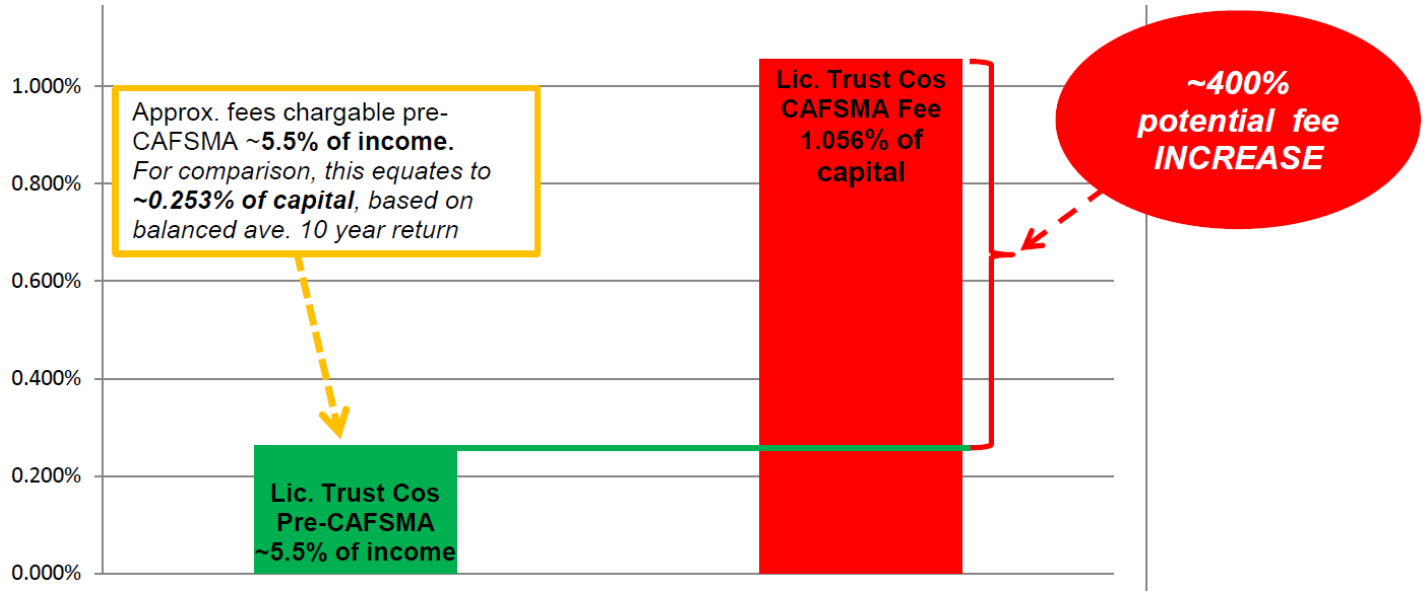
A fee based on a % of capital has no connection to the cost of providing the services

To illustrate the impact of CAFSMA, examples have been shown below and case studies included in **Annexure 8**, however it is difficult to state these figures definitively due to the lack of transparency that exists on the actual data (meaning assumptions have had to be made).

CAMAC should also note that:

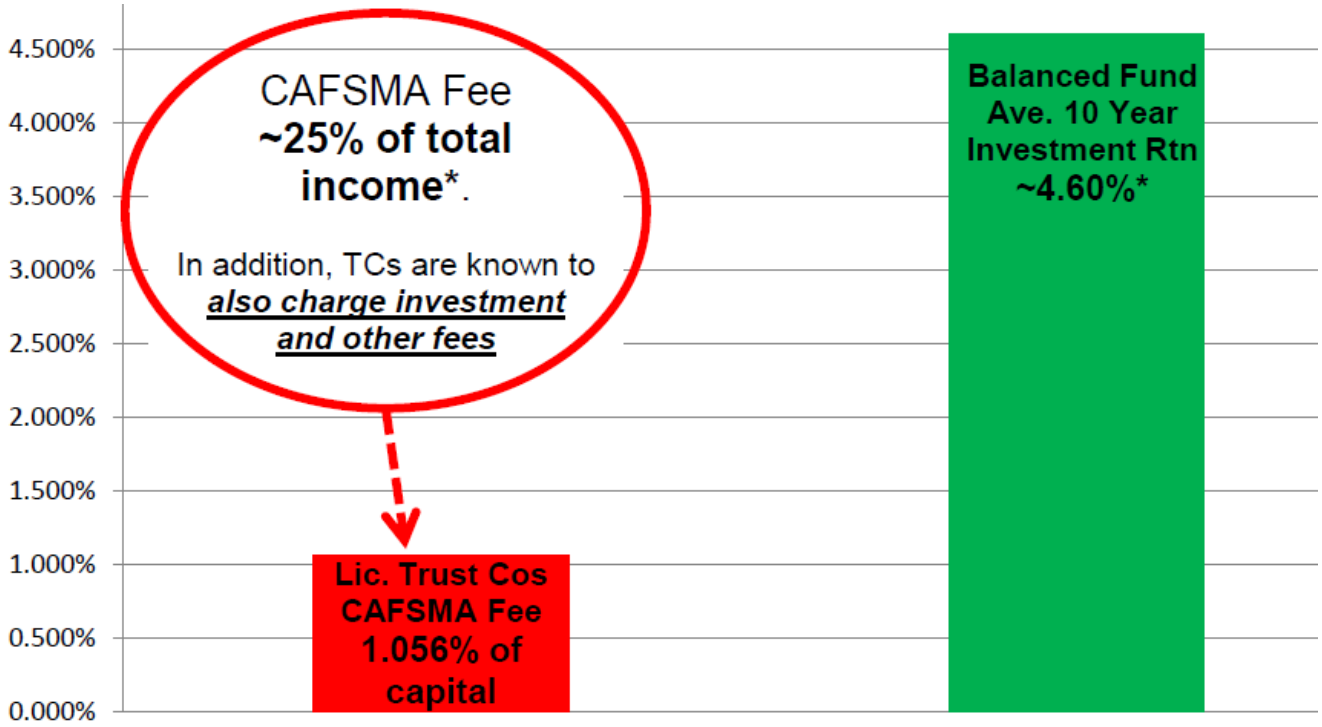
- All figures below EXCLUDE at times significant 'investment, common fund and other fees' charged by TCs; and
- '*grandfathering*' was intended to prevent TCs from increasing the fees charged to existing trusts. The Charitable Alliance's direct experience suggests TCs are demanding their 'entitlement' (CAFSMA fees) to trusts which have multiple trustees, and as a result it is highly likely they are being charged to all 'Orphan Trusts' where there are no independent trustees to monitor the fees that TCs are indeed charging.

Example A: Based on a ten year market average 4.6% investment return from a balanced investment fund (refer Annexure 9), the chart below illustrates the massive impact of a shift from charging 5.5% of income (equating to circa 0.253% of capital) to charging 1.056% of capital (incl. GST).



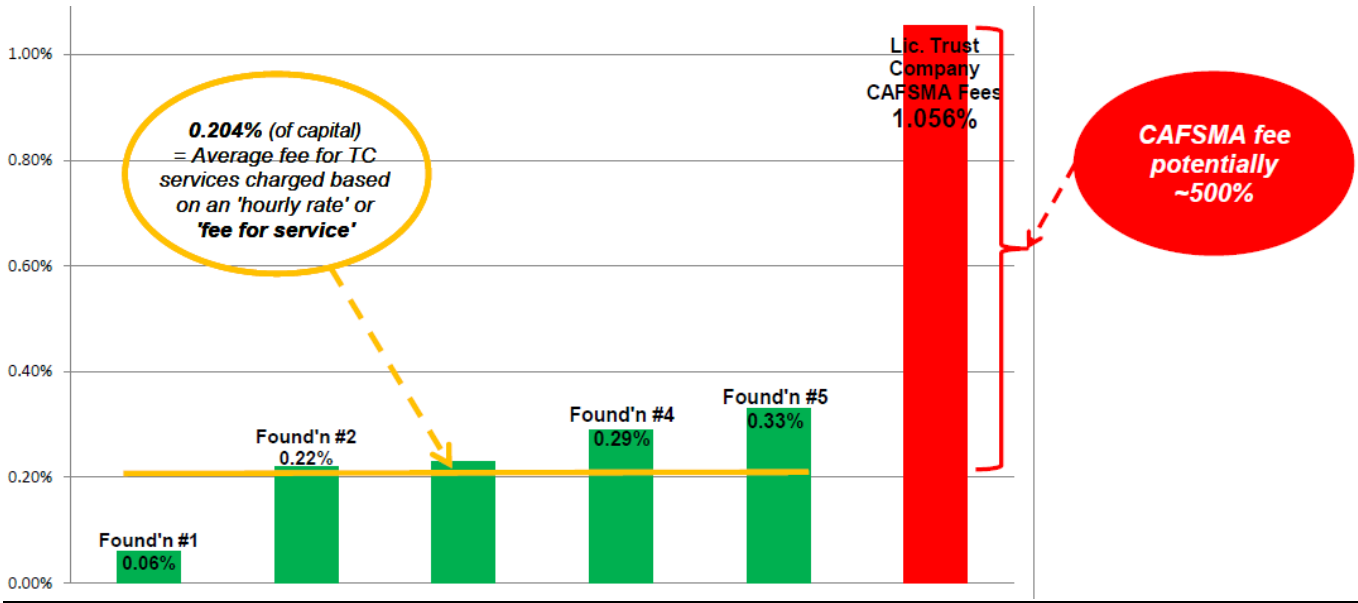
Impact of CAFSMA (continued ...)

*<u>Example B</u>: Based on a ten year market average 4.6% investment return from a balanced investment fund (refer Annexure 9), the chart below illustrates the massive portion of Charitable Trust income the CAFSMA Fee represents (~25%). CAMAC should note that this **<u>excludes</u>** the at times significant 'investment, common fund and other fees' charged by TCs.*



<u>Example C</u>:

*The table below shows professional trust administration fees charged by a non ASX listed TC for comparable TC services provided charged based on an hourly fee for service (not a % of income or % of capital). CAMAC should note that <u>for comparison purposes only</u>, the fees have been expressed as a % of capital - refer Case Study 1 in **Annexure 8** – and that the 'cost to serve' on this basis equates to a similar (but lower) level to the 'pre-CAFSMA legislation' % of income fee above.*

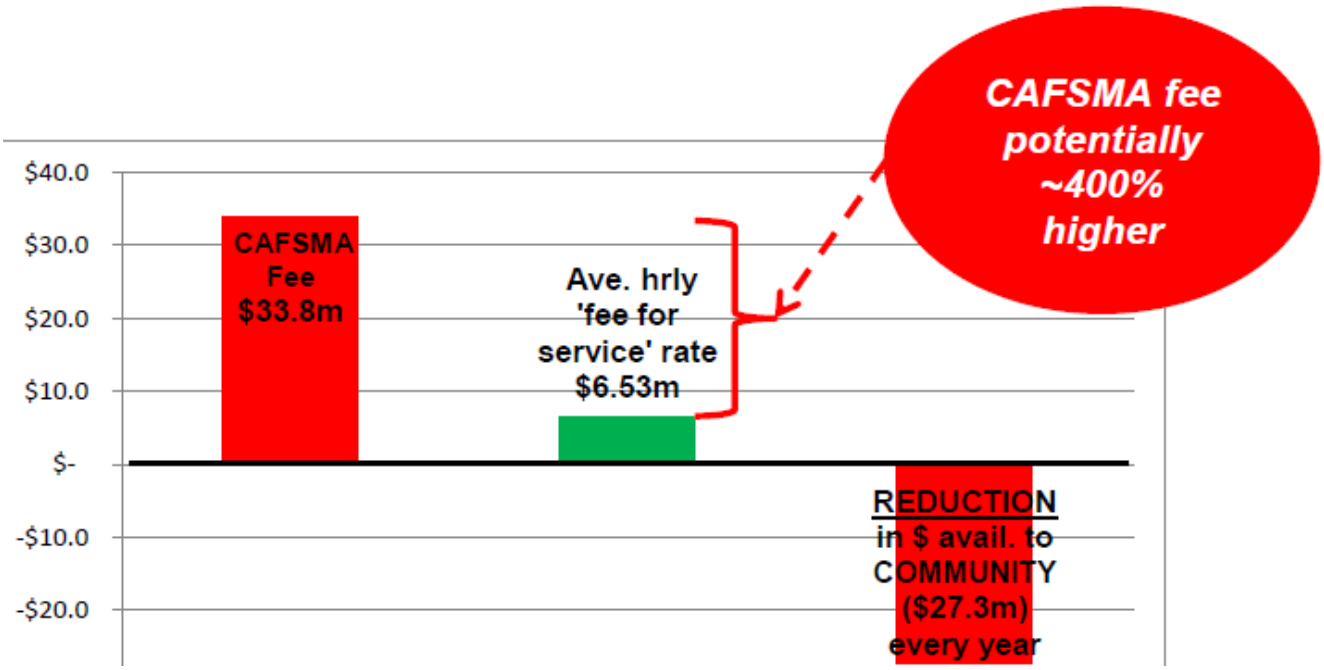


Impact of CAFSMA (continued ...)

Example D:

Applying the average 'fee for service' from Case Study 1 (Annexure 8) to the total corpus of Charitable Trust funds indicates the CAFSMA fees (as a % of capital) could be more than 400% higher than charging on the basis of 'fee for service'.

CAMAC should note that this could result in the reduction of over $25m per year every year of funds available to those in need in the community.



The table below illustrates the inputs to the summary above:

Illustration of potential impact of CAFSMA fees		$m	Notes
Corpus	$	3,200.0	#1
Investment Income	$	147.2	#2
CAFSMA Fee 'entitlement'	$	33.8	#3
Ave. fees based on a 'fee for service' rate	$	6.5	#4
Reduction in funds available for distribution	**-$**	**27.3**	**lost to COMMUNITY every year**
		-418%	

Note #1: as CAMAC was advised by Financial Services Council (FSC) across 2,100 Charitable trusts & foundations
Note #2: average income on 'Corpus' applying average returns over last 10 years for a balanced managed fund
Note #3: CAFSMA fee 'entitlement' of 1.056% of capital, which excludes other investment management and other fees
Note #4: hourly fee for service examples, expressed as a % of capital

4. Recommended Solutions

Aimed at strengthening Australian communities, the Charitable Alliance solutions are designed to:

- ✓ Support Charitable Trusts, which play a crucial role in creating a strong civil society at large
- ✓ Reflect modern regulatory principles including competition and consumer choice
- ✓ Align with the policy objectives of ACNC

The ACNC approach accepts Charitable Trusts need to be regulated differently to other trusts - their perpetuity and their varied and on-going stakeholders require special regulation and ongoing oversight which are unlikely to come from the reforms introduced by CAFSMA.

It is timely that Australia takes this opportunity to consolidate changes in TC regulation to embrace the potential to combine what community beneficiaries could reasonably expect would be achieved by CAFSMA, with the strengths and rationale of ACNC reforms.

The Charitable Alliance submits the Commonwealth Parliament should modify the operation of CAFSMA to ensure that charitable trusts are managed fairly and equitably by TCs, allowing Charitable Trusts to assist the community to the fullest extent.

CAMAC should recommend the reforms outlined under item 1 of this submission – which are outlined under two key areas:

- ✓ **Recommendation 1: Pricing Reform**
- ✓ **Recommendation 2: Governance Reform**

To follow is more detailed information on the recommended reforms, along with discussion on the associated factors to be considered.

5. Other Considerations

Recognising the limitations of this review of the CAFSMA legislation by CAMAC the Charitable Alliance also encourages CAMAC to bring to the government's attention two broader reforms:

A. Governance Independence

An inherent conflict exists across Charitable Trusts, where TCs fulfil roles as both:

i. Trustee – 'governance', for which fees can be charged under the CAFSMA; and
ii. Paid Service Provider roles, for which additional unregulated fees are charged, on top of CAFSMA fees.

This issue is heightened where a TC is the sole trustee of a Charitable Trust, where founders are deceased and there is no independent trustee(s). Independence would open the sector to additional service providers and competition.

In an ideal market independent governance would be achieved by regulating separation of:

- ✓ The 'governance' function as legal 'trustee'; and
- ✓ Fee charging service provision

That is, a paid Trustee may not also be a paid service provider to the same / related trust to which they are a trustee. Beyond independence, combined with some of the Recommendations in this submission, this will allow efficiency through market forces.

B. Winding Up & Consolidating Assets of Smaller 'economically unviable' Trusts

Due to the challenges of managing smaller trusts (many of which it is expected are likely Orphan Trusts), subject to the conditions in the relevant trust deeds / founding Will, consideration may be given to the consolidation of the assets of smaller trusts into either:

- ✓ A consolidated fund managed by a not-for-profit TC; or perhaps
- ✓ A sub-fund(s) of a Community Foundation

Recommendation 1: Proper Regulation of Setting & Reviewing Fees Charged by TCs

1A: Ensure fees set out in *Corporations Act* is a maximum rather than an 'entitlement', and that TCs have an obligation to set fees that are "just and reasonable" reflecting the pains and trouble of managing them

We recommend that under the Corporations Act it be mandatory for a TC to apply a list of relevant factors to determine "reasonableness" when initially setting fees or on review of those fees by a regulator. The legislation should adopt factors already identified the Corporations Act section 601TEA(3) as those which the Court may take into account in deciding whether fees are excessive. These are:

- *the extent to which the work is 'reasonably necessary';*
- *the quality of the work performed;*
- *the complexity (or otherwise) of the work performed;*
- *the extent to which the trustee company would have to deal with 'extraordinary issues';*
- *the extent to which the trustee company had to accept a higher level of risk or responsibility than is usually the case;*
- *the value and nature of the property dealt with; and*
- *any other relevant matters.*

In addition, a provision should be added requiring that fees be "just and reasonable" or "must not exceed what is reasonable in the circumstances for the provision by that person of the services in question".

The combination of these two legislative changes will ensure the reversal of onus onto the TC to set equitable fees. Setting a maximum fee along with a requirement to set reasonable fees will best protect charitable trusts.

The Legislation must be clear that:

- *the sections of the Act setting maximum fees are not entitlements but rather limits, and only in extraordinary circumstances would a TC be able to charge fees at the maximum level.*
- *Fees associated with 'centralised' management of multiple Charitable Trusts (including particularly 'Orphan Trusts') be set and assessed in total across all trusts managed in a 'centralised' manner (i.e. not on an individual basis unless that is how it is managed).*

The calculation of a 'maximum' fee not be linked to a % of capital, rather the 'maximum' fee be:

- *Capped at 5.5% of income annually (incl. GST); and*
- *A one off establishment fee in the first year only (as a % of income), aimed at recognising the additional work involved for the TC in the first year)*

1B: Ensure the "grandfathering" of fee arrangements works

Amend the Corporations Act to preserve the actual quantum of fees that were actually charged prior to the introduction of CAFSMA, not the maximum permissible quantum of fees.

The grandfathering provision should be repealed and replaced by a provision requiring trustee companies to charge charitable trusts at the same rate as they were actually charged prior to the introduction of CAFSMA.

If the actual quantum of fees is above the statutory maximum, the TC should be required to set new fees in accordance with the reforms suggested above to reflect the work required to manage the trust.

Recommendation 1 (continued ...)

1C: Set up a proper mechanism for the setting & reviewing of fees

Setting reasonable fees should also be included in the "governance standards" which will be set out in the regulations to the ACNC Act.

The Corporations Act should be amended to provide for the systematic review of TCs fees for the management of charitable trusts for fairness and competitiveness in the market. The regulator should have to review the fees charged by a TC to a particular charitable trust every five years, comparing the fees to other trusts of the same size and complexity.

If a TC wishes to increase fees it charges up to 'the maximum', it should be required to:

- *Go through the same process set out above with regard to increasing fees charged to new charitable trusts.*
- *Apply to the ACNC to increase the fees with supporting evidence to ensure that any increase will be reasonable and justified according to the particular charitable trust.*
- *Disclose the reason for the increase in fees to ASIC and the ACNC Commissioner, which should then be made openly available, to allow for public scrutiny of the increase.*

Recommendation 1 Discussion

Fees charged to charitable trusts: sometimes fair, often not

The Charitable Alliance acknowledges that TCs should receive a fair fee for the service actually provided. However, it is essential that the fee charged is tethered to the amount it actually costs to provide the service, including a certain baseline to reflect the cost of maintaining the systems used by TCs to manage the trusts. Any profit margin should be transparent and meet community expectations within the charitable sector – that is a prudent margin to allow a stable environment.

The difficulties in the interpretation of the relevant section of the *Corporations Act* and how this is used by the TCs to justify large increases in fees is detailed in **Annexure 3** to this submission.

Other jurisdictions - offer some guidance as to how an equitable fee regime could be achieved.

In New Zealand the Court may allow a trustee to charge a fee or commission charged as long as it is "just & reasonable". In determining whether the fee or commission is "just & reasonable", the Court must have regard to circumstances similar to that set out in section 601TEA(3) of the *Corporations Act* (Cth), incl. the amount and difficulty of the service provided and the skill and success of the trustee in administering the trust. This approach places the onus on the trustee to show that the fees are "just & reasonable", rather than on the trust or co-trustees to show fees are "excessive".

In the United Kingdom a trustee is only entitled to receive remuneration out of the funds of the charity if a number of conditions are met. The conditions are:

- The amount or maximum amount of remuneration must be set out in writing between the charity or its trustees, and the relevant person who is to provide the services in question;
- The amount must not exceed what is reasonable in the circumstances for the provision by that person of the services in question;
- Before entering into the agreement, the charity trustees must have decided they were satisfied it was in the best interests of the charity for the services to be provided by the relevant person for the amount of remuneration set out;
- The trustees receiving remuneration from the charity must constitute a minority of the persons for the time being holding office as charity trustees of the charity; and
- There must be no express provision in the Trust Deed prohibiting the relevant person from receiving remuneration.

These conditions protect charitable trusts from becoming orphaned and completely under the control of trustees receiving remuneration and the unchecked conflicts of interest that accompany it. Moreover, instead of having a statutory maximum, the amount cannot exceed "what is reasonable in the circumstances", which ensures all remuneration agreements reflect the specific needs of the trust.

Recommendation 1 Discussion (continued ...)

What factors should be used to determine reasonableness of fees charged in Australia?

TCs should be required to show that proposed fees are "reasonable in all the circumstances" standard before being permitted to charge a charitable trust for services provided. The factors set out in section 601TEA(3) of the *Corporations Act,* which are the factors which a Court can currently consider in deciding whether fees are excessive are a good starting point. The factors identified in the Act are:

- the extent to which the work is 'reasonably necessary';
- the quality of the work performed;
- the complexity (or otherwise) of the work performed;
- the extent to which the trustee company would have to deal with 'extraordinary issues';
- the extent to which the trustee company had to accept a higher level of risk or responsibility than is usually the case;
- the value and nature of the property dealt with; and
- any other relevant matters.

In addition to these factors, in assessing reasonableness, regard should be had to what is reasonable in the sector. This should be done by reference to other service providers who could provide the service.

This proposed list of relevant factors makes it clear that TC fee arrangements should reflect the complexity and difficulty of administering the trust. A consideration of the level of fees charged against this list of factors would give a good indication of whether fees charged were reasonable.

A philanthropic adviser member of the Charitable Alliance is aware of numerous cases of philanthropic advisers (non traditional TCs) charging for trustee, secretariat and grant research services on a fee-for-service basis. Similar to other professional service providers (e.g. lawyers and accountants) these philanthropic advisers maintain timesheets and charge clients based upon the actual services provided, based upon hourly rates.

Whilst the fees vary dependent upon the level and number of services provided, including number of grants made, meetings per year and program-related activity (e.g. site visits), and are charged based on hourly rates - ***the fees tend to vary between 0.1% to 0.3% of the foundations' corpus*** *– compared with a fixed 1.056% of capital regardless of the level of service provided.*

Some examples are included below (excluding investment management fees):

1. *Foundation 1: corpus $24m with fees for all services equating to 0.23% of corpus*
2. *Foundation 2: corpus $16.5m with fees for all services equating to 0.33% of corpus*
3. *Foundation 3: corpus $10m with fees for all services equating to 0.22% of corpus*
4. *Foundation 4: corpus $28m with fees for all services equating to 0.06% of corpus*
5. *Foundation 5: corpus $11m with fees for all services equating to 0.29% of corpus*

A philanthropic adviser member of the Charitable Alliance is also aware of a high profile family who established a $5m foundation with a TC as a co-trustee in recent years.

Instead of being inspired to significantly increase the corpus size (which they have the capacity to do) for the benefit of the community, the family is ***so upset by the high fees and lack of ability to remove the TC*** *that it is likely to* ***simply walk away*** *from creating a significant foundation for the benefit of the Australian community.*

Recommendation 1 Discussion (continued ...)

Role of the ACNC and the ACNC Commissioner

The ACNC Commissioner should be empowered to investigate and act if a TC was charging fees that are not reasonable in the circumstances.

The Governance Standards should also require fees to be set and continually assessed by TCs according to the list of factors already set out in the *Corporations Act* and mentioned above. While it would not solve the portability issue (as it would remain difficult for trusts to change TCs for reasons other than excessive fees), it would go some of the way to addressing the problems raised.

In the alternative, the setting of reasonable fees charged to charitable trusts should be included as a licence condition for the holding of a financial services licence. This would give ASIC and power to assess whether the TC was meeting this requirement. A failure by a TC to charge reasonable fees, or justify why the fees charged were reasonable, should result in their position as licensed trustee being opened up for competition.

What trustee responsibilities should fees cover?

The requirement to set reasonable fees should cover all fees for all services provided by TCs to Charitable Trusts. They should not be permitted to charge any fees outside this framework. Currently the services provided by TCs and included within the Trustee Fee include:

- Assisting with the establishment of the Trust:
- General administration of the Trust
- Administration of assets and investments
- Administration of distributions

The Charitable Alliance acknowledges that TCs need appropriate remuneration for managing smaller trusts and component pricing may make the management of these trusts unprofitable. The Public Trustees may provide a safety net in such circumstances.

In addition to allowing TCs to increase their fees by >400%, CAFSMA does not consider the full range of (at times significant) investment and other additional fees charged by TCs over and above the CAFSMA legislated fees)*

Additional services and therefore fees, that are, or could be, charged to Trusts by TCs, but are **NOT** included within the fees regulated under CAFSMA, include:

- Investment Management or Advisory Fee – fees which are not regulated and in many cases are not independent and or competitively tendered
- Common / managed fund fees charged by a related party (of the TC) for managing a fund in which trust funds are invested (i.e. separate to the Investment fees above charged by the TC)
- Providing investment research and proposals
- Ongoing monitoring of the trust investments to ensure they are in line with expectations
- Providing legal opinions (relating particularly to taxation, but also otherwise) for specific issues related to the trust

When determining whether fees are reasonable, the TC and regulator must have regard to:

- What other fees are charged to charitable trusts over and above the regulated CAFSMA fee, including investment management and 'common / managed fund' fees (by a related party)
- Benefits of 'centralised' management of multiple trusts (including in particular 'Orphan Trusts'), with recognition the community should be the beneficiary of any synergies / cost efficiencies

*The **community should be the beneficiary** of any synergies / cost efficiencies available from the 'centralised' (pooled) management of multiple trusts (in particular 'Orphan Trusts')*

Recommendation 1 Discussion (continued ...)

Ensuring the grandfathering of "existing" fee arrangements

The grandfathering of 'existing' fee arrangements (actual fees charged) between TCs and charitable trusts prior to CAFSMA has **NOT** been effective. This is due to a lack of clarity in the drafting of the statute combined with the opportunistic interpretation preferred by TCs. Prior to the introduction of this regime on 6 May 2010, the amount which TCs were able to charge under State legislation (set out in **Annexure 6**) was not necessarily relied upon by TCs. As can be seen from the case studies in **Annexure 8**, many charitable trusts were not, for example, being charged in accordance with the Victorian *Trustee Companies Act*.

*'grandfathering' provisions under CAFSMA have **NOT protected the community***

Instead of protecting charitable trusts by keeping in place old fee arrangements, TCs have taken the commencement of the CAFSMA as an opportunity to charge what they see was a statutory "entitlement" under the old State legislation. This runs contrary to the apparent purpose of the reforms. In situations where the TC has not raised any concerns about the fees being too low this change is particularly egregious.

Case Study 4 (of 8): Charitable Trust** - refer **Annexure 8

- *Trust assets = $57.2m*
- *Pre-CAFSMA 'actual' TC fee charged = ~$179,000/year*
- *Subject to the interpretation of 'grandfathering provision', post-CAFSMA fee could be either $328,000 or $604,000/year*
- *Increase = either $149,000 (83%) or $425,000 (237%) per annum*

Case Study 6 (of 8): Charitable Trust** - refer **Annexure 8

- *Assets = circa $17.5m*
- *'Will' prescribes the fee at 2.5% of income which has been charged for 43 years (~$20,000 to $30,000/year +GST in recent years)*
- *Post-CAFSMA the TC is demanding its 'statutory fee entitlement', which equates to ~$150,000 to $170,000/year (varies based on valuation of assets)*
- *CAFSMA Increase = $140,000 (550% to 650%) per annum*

The relevant provision in the Corporations Act states that where a trustee company provides a service as trustee of a charitable trust, and the provision of the service commenced prior to 6 May 2010, the trustee company must not charge fees in excess of the fees that it could have charged in relation to the charitable trust immediately before that date. The grandfathering provision was put in place to keep prior fee arrangements between charitable trusts and trustee companies in place, protecting the trusts from a costly increase in fees.

In the second reading speech introducing CAFSMA to Parliament, Minister Chris Bowen explained:

> *"The government is aware of the need to protect charitable trusts by regulating the fees they may be charged by trustee companies. It is proposed to 'grandfather' the fees charged to existing charitable trusts and foundations. Thus, if the fees of the charitable trust would be increased due to the introduction of a new fee regime, the grandfathering provision would require that client to be charged as if they were still covered under the old rules."*

Recommendation 1 Discussion (continued ...)

As it stands, the effect of the provision is not to protect the actual fee arrangements that existed between trusts and trustee companies, but rather only the old State and Territory limits on fees. Some of these limits on fees are more onerous on charitable trusts than the CAFSMA. This has lead to a unnecessarily complex legal position where the total fees which may be charged by trustee companies are difficult to ascertain. This is particularly evident when considering the diversity of fee regimes in the States and Territories that existed prior to the CAFSMA.

The failure of this provision to operate as intended has the potential to cost charitable trusts significant amounts of money in increased fees, with no substantial change in the service provided by the TC. This is a substantial failure in the aim of the legislation to improve consumer protection. Instead, the Act should be amended to preserve the actual quantum of fees the TCs were charging prior to the enactment of CAFSMA rather than the maximum the TCs could have charged.

Regular review of fees charged every five years

An automatic review mechanism should be introduced to ensure protection of charitable trusts, particularly orphaned trusts.

As it stands it is only the States' Attorneys-General or co-trustees who can bring an action to get a review of fees. The paucity of cases of fees being challenged shows either:

- that this is beyond the resources of the Attorneys, and therefore the oversight they provide is not sufficient; or
- the default practice is that the stakeholders in the trust just accept that there can be no effective review.

The ACNC Commissioner could play an important role in this regard.

The Commissioner will have the expertise and resources to properly assess whether a TC is charging reasonable fees, making a determination that fees are note "just and reasonable". The Commissioner should be given standing to either carry out an assessment of fees or initiate a court review. If the TC disagrees with the assessment of the Commissioner it could appeal the assessment to a Court. However, as the TC stands to gain from any increase in fees they should bear the cost of review, not the public or the charitable trust. Failing to justify why the fees are reasonable would trigger an option on behalf of the charitable trust or the ACNC to transfer trustees, subject to certain other preconditions being met prior to the option being exercised.

The ACNC Commissioner should automatically review fees charged to trusts by TCs every five years. The review process would involve the TC making submissions showing that the fees they charged were reasonable in the context of the charitable sector. It is essential that there is a regular review to make sure money which should be devoted to charitable purposes is not unfairly diverted to TCs.

If CAMAC considers that this role for the ACNC Commissioner is not appropriate, it should recommend that the jurisdiction of FOS be extended to deal with complaints or referrals. The only other alternative would appear to be for ASIC or the offices of the Attorneys-General to review fees.

Recommendation 2: Governance Reform for Charitable Trusts

2A: Transparency

TCs should be required to provide financial reports to ACNC Commissioner or another appropriate regulator to ensure access and oversight to the information by stakeholders including Attorneys General, TCs, and co-trustees. This would allow for:

- *The regulator to be able to ascertain whether the fees charged by TCs are in an appropriate range and that funds are being managed properly*
- *Information to be collected about the health of charitable trusts and how better to improve their effectiveness*

Recommendation 2A Discussion

Transparent reporting obligations

As charitable trusts exist for the public benefit, their financial reports and disclosures should be provided on a confidential basis to the appropriate regulator. This would not mean that all the financial information of the trust would be provided, but it should be possible for the regulator to review key aspects of the trust on an annual basis (e.g. determine the 'total' fees being charged and how the trust monies were being invested).

This transparency is justified by the fact that charitable trusts are meant to exist for the public benefit. The regulator on behalf of the public should be able to assess whether those responsible for managing funds set up for their benefit are doing so properly. Reporting obligations should differ depending on the size of the trust. A division could be made between small (those trusts with corpus of less than $250,000), medium (between $250,000 and $1,000,000) and large ($1,000,000) to determine the extent of the disclosure obligations.

Charitable Trusts exist for the public / community benefit, so financial reports, including details of 'total' fees charged should be reported confidentially and monitored annually by a regulator.

Existing obligations

The vast majority of charitable trusts managed by TCs do not make any reports financial or otherwise to regulators. This makes it very difficult for TCs to be held to account for their management of the trust and the fees they charge.

This was noted in the Explanatory Memorandum to the ACNC Bill at page 292.

> *Charitable trusts do not report to stakeholders, however, for internal purposes are required to maintain up-to-date financial information. Information needed to meet reporting obligations under this option would already be collected by charitable trusts. Therefore, regular reporting to the NFP regulator would have minor compliance costs for these entities and would amount to inserting already collected information into a standard form. A conservative estimate would be that it cost half of one working day in staff time for these entities to meet reporting obligations under this option.*

There is a complete lack of transparency relating to the operation of these trusts, which is of particular concern in the case of orphan trusts. Without this basic information it is impossible to make a judgment about distribution levels and whether the fees charged are equitable given the level of service that is being provided.

Recommendation 2A: Discussion (continued ....)

While ASIC does have some oversight and particular beneficiaries may elect to seek an Annual Information Return, it is mainly through TCs self-reporting breaches that ASIC will discover irregularities in trust management. The oversight is limited to high-level surveillance to meet licensing requirements rather than a more intensive APRA-style regulation.

The ACNC will introduce transparency into management of charitable trusts. Registered entities under the ACNC Bill will be subject to reporting obligations. All registered entities will have to provide the Commissioner with an annual information statement, and medium and large entities will have to provide a financial report. This will enable the Commissioner to have the information necessary to assess the activities of trusts, including fees charged by TCs.

The importance of transparency

It is essential that the regulator responsible for acting in the trusts' best interests have sufficient information to make a decision. The reporting obligations in the ACNC Bill are a positive development. If it applies to all charitable trusts, it will ensure that there is oversight of the fees charged and financial decisions made by TCs. In addition to this reform, a provision should be added into the *Corporations Act 2001* requiring all TCs that charge fees to charitable trusts to report to the ACNC the fees they have charged and the services they have provided in each year.

Disclosure of component pricing to the appropriate regulator, setting out the work completed by TCs justifying the charged fees, would allow for a better assessment of whether the fees were reasonable. The Charitable Alliance believes this kind of transparency will encourage TCs to apply fees fairly and reasonable.

Reporting could be in a form similar to a PAF Return which PAFs are required to lodge with the ATO each year. As set out in **Annexure 7**, the PAF Return includes a summary of:

- Director/trustee details
- Income and expenses
- Assets and liabilities
- Gifts made
- Confirmation that a financial audit has occurred; and
- Confirmation by the independent auditor of compliance by the PAF and the trustee with the PAF Guidelines

In addition, the reporting obligations to consumers of TCs, as holders of Financial Services Licences, should be widened to include disclosure to the ACNC, and thereby being available to the States' Attorneys-General, actual or potential beneficiaries and any co-trustees. This would enable the ACNC and Attorneys-General to properly fulfil their role as protectors of the trust (like a beneficiary would in relation to a fixed trust) and also empower co-trustees to use the dispute resolution mechanism to change trustees. This would require the role of the FOS to be widened to allow for disputes over the fees of charitable trusts to be considered or replaced in this respect by the Commissioner. This is discussed further in Part 7 of this submission.

Alternatively, disclosure could be required to the ATO. While the ATO does not have specific expertise over the charitable sector, the information gathered would allow for identification of trusts that were being charged in a way which was substantially more than trusts of their class. This could be a trigger for review by the regulator of the management of the trust by the TC.

Lack of effective review by beneficiaries

Another reason why increased transparency is crucially important is because of the lack of oversight by beneficiaries into the management of the trust.

As stated above, charitable trusts differ from ordinary fixed trusts in a fundamental respect: many trusts, instead of having defined beneficiaries, are devoted to a particular charitable object or purpose with discretion vested in the trustee for distributions. This means that unlike other kinds of trusts, there are no beneficiaries with a legal interest capable of supporting a court challenge to the trustees' administration of the trust. Instead, the States' Attorneys-General has standing to bring an action in Court on behalf of the object and purpose of the trust, and it is this mechanism is meant to protect charitable trusts from being mismanaged.

The States' Attorneys-General do not have the resources to properly exercise their responsibilities in this regard. The reality is that many charitable trusts, particularly orphan trusts, have had no appropriate oversight of their management. The CAFSMA has not overcome this problem for charitable trusts as the consumer protection measures which it introduced are largely ineffective for charitable trusts.

While procedure provided for by CAFSMA does provide a means of gaining information about the working of a charitable trust (as set out in **Annexure 5**), the utility of the provisions are limited. While members of the public within the "class that the trust is intended to benefit" can request an account of the trust, for the reasons mentioned above this is unlikely to offer sufficient oversight. However, even if the people who received grants from a particular trust did get access to this financial information, this would be unlikely to achieve the aim of holding TCs accountable for their management of the trust. It is difficult to envisage a person who had received a grant from a charitable trust then complaining about the management of that trust, management which had just conferred upon them a grant of money. Additionally, a body who has missed out on a grant will have limited redress if any, to challenge the use of a trustee's discretion.

Moreover, this process does not involve any form of specific dispute resolution, meaning that once information is requested, the requesting person is left with the existing and unsatisfactory procedures for exercising oversight on the operation of the trust. A new mechanism is needed to ensure that there is some person – whether a co-trustee or new regulator – capable of acting as an advocate for the interests of the charitable trust when those interests clash with the TCs. As it stands there is no one to ensure that the balance is always tipped in favour of the best interests of the charitable purposes for which the trust was originally established.

Additionally, there may be no person with sufficient legal interest in the operation of the orphan trust who would request the Annual Information Return. Where settlors or identified beneficiaries are not present, it is likely to fall to the state Attorneys-General as responsible Ministers or ASIC to request, receive and review the information in the Annual Information Return.

Recommendation 2: Governance Reform for Charitable Trusts

2B: Require TCs to seek 'independent' advice

- ✓ ***TCs be required to seek independent advice before investing the funds of charitable trusts in the financial instruments of companies related to the TC***

Recommendation 2B Discussion

TCs and Investment Advice: A Clear Conflict of Interest

A conflict of interest exists where a TC decides to invest the funds of a trust in the financial instrument of a related company (for which the related party may charge fees over and above the TC fee and or Investment Management fees). It appears this is a relatively common activity: the funds of trusts devoted to charitable purposes are kept "in house" without sufficient thought given to whether this is the most appropriate investment in the circumstances.

The Charitable Alliance understands that when TCs are making investment decisions for charitable trusts they often seek advice from corporate entities which are related to the TC, usually being owned by the same financial services company. While, strictly speaking, this is not the TC investing funds in an investment product which will make itself money, it is still sufficiently related to make investment without first getting independent oversight or advice inappropriate.

CAMAC should recommend that provisions be added to the Corporations Act banning this activity unless the TC has sought truly independent advice as to whether the investment is appropriate for the charitable trust.

Such a provision would be a reflection of the current state of the law relating to the duties and responsibilities of trustees. Central to the role of trustee is the trustee's duty not to misuse his or her position for personal gain. It is essential that a trustee have loyalty to the trust. This is not a new concept: the English case of Keech v Sandford (1726) Cas temp King 61 is the foundational case for the principle that trustee owes a strict duty of loyalty to the trust, and that and any possibility of a conflict of interest must be avoided. The reason why this obligation and duty is construed very strictly is because of the power and control that the trustee has over the trust, and the ease at which an unscrupulous trustee could take advantage of his or her position. This is no different to the position of TC: as they are empowered to make investment decision, they should be forced to do so in a way which puts the interests of the trust before the interests of a related company.

Having this enshrined in legislation would give the situation clarity, and stop TCs from undertaking such a course of action without fear of being challenged in a Court due to the trust being "orphaned" or the co-trustees not understanding the implications of such an investment. As discussed above, the current lack of accountability and transparency makes oversight by any interested party very difficult. TCs must act in the best interests of the trusts they manage; and implementing this recommendation would do much to ensure that this occurred.

2C: Implement Governance reform to protect "orphan" charitable trusts

- ✓ ***Prevent the creation of Orphan Trusts***

  The creation of new orphan trusts should be prevented by introducing a legal presumption that where trust deeds have appointed independent trustees alongside TCs, the settlor intended for an independent trustee in perpetuity. This would mean a Court would presume a settlor intended for a mechanism in the Trust Deed that allows for the appointment of new independent trustees.

  As part of this, there should be a presumption that the Trust Deed permits the appointment of alternate trustees to allow for transfer of knowledge and proper succession.

- ✓ ***Protect existing orphan trusts by requiring the appointment of new trustees and independent "responsible persons"***

  TCs should be prohibited from charging any fees to charitable trusts unless the fees have been assessed by an independent observer. The nature and extent of the involvement of the independent observer should differ depending on the size of the orphan trust.

  The legislation should be amended to provide that trusts exceeding particular corpus value are no longer orphaned by requiring the appointment of an independent trustee. This person would have all the powers and responsibilities of an ordinary trustee.

  For smaller trusts, an independent "responsible person" should be appointed. The independent observer would not have a responsibility to manage the trust, but have access to financial documents and information about the fees charged by the TC. This person could then make a complaint to the ACNC or appropriate regulator if they considered the fees charged were not reasonable in the circumstances.

*A large portion of Charitable Trusts are '**Orphan Trusts**', where TCs are now the sole trustee. These trusts usually exist as a result of:*

- *the death of the original trustees*
- *having been established with a sole trustee*

Orphan Trusts have no one to effectively stand up for the interests of the community, against the commercial imperatives of TCs

Recommendation 2C Discussion

Management of "Orphan" trusts - *Orphan trusts: the current situation*

TCs are now the sole trustees for a large number of charitable trusts. These trusts, which have been orphaned by the death of the original trustees, or which were established with a sole trustee, do not have anyone to effectively stand up for their interests against the commercial imperatives of the TCs. While these trusts are meant to be protected by the cap on fees provided in the *Corporations Act*, the cap has proven to be ineffective in a number of instances.

The management of these trusts must be made much more transparent to ensure that the benefit to the community is protected. Perpetuity is a long time, and inevitably involves changing stakeholders and changing market forces.

*Case Study 8 demonstrates the **stark investment performance difference** between a 'community focussed' investment committee and an Orphan Trust managed by a 'profit driven' TC*

Recommendation 2C Discussion (continued ...)

One of the policy principles which motivated the CAFSMA reforms was to improve transparency for the consumers of financial products; in this regard, the reforms have failed to understand how the orphan trusts are isolated from effective review.

The regulation by ACNC may increase this transparency. It is noted from the Explanatory Memorandum to the Bill at page 18 that the ACNC Commissioner will have regard to issues of regulatory necessity, risk and proportionality to ensure that his or her actions are suitable and relative to individual circumstances. These concepts involve ensuring that regulatory responses give consideration to the different circumstances of different entities, including entity size, revenue and donations received from the public.

Management of "Orphan" trusts - *Preventing the existence of orphan trusts*

An ideal solution would be to prevent the existence of orphan trusts altogether for trusts with a corpus greater than $1 million or more. This would be achieved by mandating that all charitable trusts must have a majority of independent trustees who do not charge TC fees. Other jurisdictions have taken this route to protect charitable trusts: in the United Kingdom all charitable trust must have a majority of trustees who do not receive any fees from the trust monies.

This also reflects the governance requirements for PAFs in Australia. As set out in **Annexure 7**, PAFs must have at least one independent director or trustee, known as a Responsible Person. It is also interesting to note that for Public Ancillary Funds the majority of directors/trustees must hold a position of responsibility within the community.

Consultation with all stakeholders should assist in setting the appropriate limits to ensure that there would not be unnecessary or over regulation for those smaller trusts which may not have the impact for greater community benefit or for those trusts which have named beneficiaries. These, of course, will still be impacted in any case by the new reporting arrangements for ACNC. The threshold criteria amount should be consistent with the size categories in the ACNC Bill.

In order to ensure proper governance of smaller trusts, CAMAC should recommend that a "responsible person" be appointed to oversee the management of the trust. This should be modelled on the governance requirements for PAFs. . In the case of PAFs, the responsible person must be an active director or trustee of the fund. However, for smaller funds this may not be appropriate and be too cumbersome for effective management. In these circumstances the "Responsible Person" would only have the right to observe the management of the trust and notify the ACNC if they consider that the fees being charged by the TC are excessive or the trust is not being managed appropriately.

New or replacement trustees

Such reforms would obviously necessitate the appointment of new trustees. Such persons – which could be appointed by the Court, the ACNC, or the relevant Attorney General – could be drawn from a list of upstanding members of the community willing to serve as trustees. While this may be a large undertaking at the beginning of the reform, it will ensure that there are people who are able to act as an advocate for the interest of the charitable trust when those interests conflict with TCs.

Such a reform would level the playing field, enabling TCs to continue providing a useful service to charitable trusts, but allowing for oversight of their actions without the need for an expensive government regulator. However, if an appropriate disclosure regime ensuring transparency and a mechanism for fairly setting fees for consumer protection are introduced, this may not be necessary. If this does not occur then radical change is the only solution which adequately protects the interests of the community.

Reform is required to ensure the ***creation of new 'Orphan Trusts' is avoided***

2D: Introduce Portability to the Charitable Sector

- ✓ **Ensure someone – whether an independent "responsible person" or regulator – has the power to decide which TC should manage the charitable trust.**

  The role of selecting a TC should be allocated to a sub-committee led by the ACNC commissioner, as they will have the resources and expertise to make an appropriate decision. This could be a peer review body modelled on ASIC 'Takeovers Panel'.

  In the alternative, unpaid volunteer co-trustees of the medium and large charitable trusts could make the decision. This would enable for there to be portability and competition between TCs without the involvement of Government, either through ACNC, Attorneys-General or the Courts.

- ✓ **Empower the ACNC to initiate a review of appointments of TCs every five years, with a competitive tendering process to allow for other players to enter the market.**

  Each trust would have autonomy in arranging how the tendering process would occur, with oversight from the ACNC. TCs would have to show they went through a process of independent testing against market fees.

- ✓ **Amend the Corporations Act to remove barriers and provide greater competition in the charitable trusts sector by allowing specialist trustee corporations (including not-for-profits) to be licensed to provide charitable trust services.**

Recommendation 2D Discussion

The current legal position

The court has an inherent jurisdiction to appoint and remove trustees. In all jurisdictions except the Australian Capital Territory and South Australia, the court is also conferred a separate statutory jurisdiction which allows it to appoint a new trustee whenever it is expedient and appropriate, either in substitution for or in addition to any existing trustees.

Removal of a trustee by a Court will not take place unless there has been some wrongdoing on the part of that trustee: the mere fact that the Court would not have made the appointment itself is not enough. It would most likely require a breach of trust on behalf of the TC, not just a dispute about the appropriate fees to charge.

The current legal position - *Impact of the ACNC Bill*

The ACNC Bill gives the ACNC Commissioner the power to suspend or remove the trustees of "registered entities." At this stage it is unclear whether all charitable trusts will be required to register under the new regulation as it depends on State legislation. However it can be assumed that registration will occur as it is a prerequisite for a trust to access certain Commonwealth tax concessions. In the future it may also be a prerequisite for other exemptions, benefits and concessions provided for under other Australian laws.

The ACNC Bill refers to the "responsible entities" of "registered entities". In the case of charitable trusts, the "responsible entities" are the trustees. Under the proposed legislation, the Commissioner will be able to remove or suspend the trustees if the Commissioner reasonably believes:

- The registered entity has contravened a provision of the ACNC Act, or it is more likely than not the registered entity will contravene a provision of the Act;
- The registered entity has not complied with a "governance standard", or it is more likely than not that the registered entity will not comply with a "governance standard"; or
- The registered entity has not complied with an "external conduct standard".

Recommendation 2D Discussion (continued ...)

Whether this will permit the ACNC Commissioner to remove TCs as trustees in the event they charge excessive fees will depend on how the ACNC Regulations define "governance standards." The regulations are yet to be released.

If the ACNC Commissioner removes a trustee it may appoint an acting trustee to take its place while a new trustee is found. The acting trustee can exercise all the rights, titles and powers and must perform all the functions of the removed trustee. The Commissioner, however, retains control: he or she can give a written direction to the acting trustee instructed them to act in a particular way.

The Explanatory Memorandum (**EM**) of the ACNC Bill usefully identifies the benefits of the Commissioner holding the power to suspend or remove trustees:

- Unlike State Attorneys-General the ACNC has both supervisory and investigatory powers in relation to registered entities (which includes charitable trusts). These powers allow the ACNC Commissioner the means to investigate claims of misconduct and to gather evidence.
- A regulator can ensure the actions are proportional in the circumstances and act in a timely manner, without needing to enter into a lengthy court process.
- The decisions of regulators are subject to an review and appeal in the Courts.
- A regulator can provide cost-effective and accessible redress, ensuring that the beneficiaries of charitable trusts, the wider public, have improved access to justice.

As the EM notes, this movement of the oversight of trustees from a judicial to regulatory function is similar to reforms that have occurred overseas (notably in the UK with the Charity Commission). Similar Australian examples include the power of APRA to suspend or remove trustees of most superannuation funds, and the power of the Commissioner of Taxation to suspend and remove the trustees of self-managed super funds and charitable ancillary funds.

The current approach: failing to protect Charitable Trusts

The status quo is clearly unsatisfactory from a consumer protection perspective. Only allowing Courts to remove and replace trustees is a significant barrier to allowing for the efficient removal and replacement of trustees. Court action necessarily means significant risk, time and expense for the co-trustees seeking to have the TC removed; and in the case of orphan trust, it is up to the Attorney-General to act. This lack of portability makes it very difficult to allow for competition in setting prices. This could potentially result in an inefficient TC sector, inflated fees and significantly less funding available for distribution to the Australian community through not-for profit entities.

The introduction of competitiveness in the market for trustee company services by providing charitable trusts with this option would be consistent with principles of transparency and accountability, and is particularly relevant in a deregulated, market driven economy. It will also improve consumer protection by forcing TCs to continue to provide a high quality, cost effective service to charitable trusts as if they fail they will lose the business.

Recommendation 2D Discussion (continued ...)

Adopting a mechanism for charitable trusts to exercise choice

It is important to have a simple and cost-effective mechanism by which the election change TCs should occur. Rather than it being through the unilateral act of the Commissioner, one option is to allow the co-trustees to elect to have the TC role put out to tender. This would make TCs compete with each other and offer fees which actually reflect the service they provide. It would also ensure that TCs are accountable by allowing co-trustees to remove and replace them if necessary. This mechanism would be particularly useful if the UK requirement that licensed trustees receiving fees be in the minority of trustees was adopted. In many ways, it presents the ideal reform: there would be no need for an expansive role by a regulator as this could be done by the co-trustees.

For smaller trusts, the independent "responsible person" would manage the process of allowing other TCs to inspect the financial reports of the charitable trust. If the responsible person was convinced that another TC could provide the service for less money, they could to apply to the ACNC have the TC replaced.

If CAMAC was of the view that it was necessary to have an government regulator assess whether a trustee should be removed, it should recommend that either the ACNC or the relevant Attorney-General have the power to remove a TC from its position as trustee and appoint a new trustee. The TC could appeal this decision to a Court, but any appeal should be entirely at the TC's cost given the charitable nature of the trust. The ACNC, Ombudsman or Attorney-General should be able to act either on its own motion, or by the application of one of the co-trustees or responsible person.

If orphan trusts are allowed to continue to exist, CAMAC should recommend that the ACNC Commissioner, States' Attorney-General or a Court be given power to order the appointment of a new TC could be appointed according to a tender process. If setting reasonable fees is included as a "governance standard" in the ACNC regulations this would allow trustees to be removed and then the acting trustee directed to manage the tender process in the best interests of the charitable trust.

Instituting a new AFSL licence for specialist managers of charitable trusts

ASIC licensing requires for TCs

The licence from ASIC to be a TC requires the company be able to:

- Apply for probate of a will, apply for a grant of letters of administration, or election to administer a deceased estate; and
- Act as executor or administrator of a deceased estate, plus one other "estate management function".

However, the expertise necessary for being a licensed trustee of a charitable trust is limited to:

- Performing trustee functions; and could include
- Establishing and operating common funds.

This current licensing requirements place a considerable barrier on new companies entering the TC market. This barrier is particular harmful to the competition for the management of charitable trusts, as these functions are not necessary for the effective and proper management of a charitable trust. CAMAC should recommend that this requirement be altered to allow for specialised companies to be set up to manage charitable trusts.

The ACNC Bill requirements for reporting, supervision and the Commissioner's powers in respect of their operation would make this alternative feasible.

An existing alternative of private trustees does exist, however private trustees do not generally charge for their work and many do not seek reimbursement of expenses. A not for profit trustee corporation would be entitled to be reimbursed for the costs only of managing trusts.

2E: Implementing better dispute resolution mechanisms for TC disputes

- ✓ ***Put in place appropriate dispute resolution mechanisms to assist resolve disagreements between TCs and co-trustees and beneficiaries by allowing the ACNC power to set up a body which can hear and resolve disputes without the need to go to Court (which could be modelled in a similar manner to the Takeovers Panel)***

Impact of the changes to ASIC licensing and Options for Dispute Resolution

CAFSMA introduced ASIC licensing for TCs incorporating disclosure requirements and mandatory dispute resolution structures for TCs. These reforms are set out in **Annexure 5**. The changes have failed to properly support policy principles of transparency & consumer protection for charitable trusts.

Dispute resolution procedures

The dispute resolution procedures provided for by CAFSMA substantially rely on the Financial Ombudsman Service (**FOS**). As it stands, a person with a dispute about the management of a charitable trust is entitled to lodge a dispute with the FOS if the applicant is "entitled to request an annual information return from the trustee and the dispute is otherwise within the jurisdiction of FOS.

The only persons entitled to request an annual information return from a TC are:

1. a settlor, or one of the settlors, of a trust;
2. a person who, under the terms of the trust, has power to appoint or remove a trustee of the trust or to vary (or cause to be varied) any of the terms of the trust; or
3. a person, or person's appointed successor, who is named in the instrument establishing a trust is a person who must, or may, be consulted by the trustee or trustees before distributing or applying money or other property for the purposes of the trust.

This does not include people "class that the trust is intended to benefit" and therefore only provides very limited oversight and is of no assistance to orphan trusts. Furthermore, the FOS Scheme cannot consider a dispute that relates to "the level of a fee, premium, charge or interest rate". This means that in any disputes about fees the FOS Scheme does not allow for a co-trustee to question or to seek review of the fees that may be charged by a trustee company without going to a Court, even though a co-trustee may have a legitimate reason in the interests of consumer protection to complain about the conduct or the financial service provided by the trustee company.

Broadening the FOS Scheme

Given that the FOS Scheme is a free scheme designed to uphold the rights of clients of financial services, minor reform broadening the scope of the FOS terms of reference may allow for some oversight of the fees charged by TCs. This dispute resolution method recognises the imbalance between the financial service provider and the consumer and remedies them. However, at present, the fact that fees are excluded means that the FOS Scheme does not currently provide a meaningful check on the fees charged by TCs acting in the charitable trust sphere.

Allowing other parties standing to make a complaint outside the Court system

As many charitable trusts have discretionary beneficiaries, one party who can challenge the fees charged by TCs are the co-trustees of the trust. The dispute resolution mechanism as envisaged by ASIC licensing should be extended to apply to disputes between co-trustees and TCs about fees. This would avoid the need (at first instance) for the co-trustees to apply to the ACNC or a Court to have matter resolved as the FOS would be able to give a determination binding on the TC.

Alternatively, a better solution is to offer the new ACNC commissioner oversight of disputes between charitable trusts and TCs. The ACNC commissioner would be able to offer better solutions taking account of all the relevant issues, and would have experience in the philanthropic sector.

Annexure 1: Charitable Alliance

The Charitable Alliance is an '*alliance*' of concerned trustees, advisors to and stakeholders (listed below) of Charitable Trusts and Foundations that provide significant financial and other support to communities across Australia. The Charitable Alliance are stakeholders in a wide range of charities, grant making trusts and foundations, including Private Ancillary Funds (PAFs) that:

1. Have a corpus that in aggregate exceeds $1 billion
2. Provide support to the community exceeding $1 billion annually
3. Engage with, and are focussed on supporting, those in need in communities across Australia

Charitable Alliance:

- ✓ Tim Costello AO, **Chairman, Community Council for Australia (CCA)**
- ✓ Sandy Clark, **Chairman, William Buckland Foundation**
- ✓ Graeme Danks, **Honorary Trustee, Danks Trust**
- ✓ Peter Yates AM, **Chairman Designate, Royal Children's Hospital Foundation, Melbourne**
- ✓ Simon McKeon, **2011 Australian of the Year**
- ✓ Ian Smith, **Director, Baker IDI Heart & Diabetes Institute Holdings Ltd** *(Partner, Bespoke Approach)*
- ✓ David Crosbie, **CEO, CCA & Member, Not-for-Profit Sector Reform Council**
- ✓ Richard Leder, **Deputy Chairman, Royal Children's Hospital Foundation, Melbourne**
- ✓ Sue Hunt, **Executive Director, Royal Children's Hospital Foundation, Melbourne**
- ✓ Graeme Sinclair, **Trustee, William Buckland Foundation**
- ✓ Jane Gilmour OAM, **Trustee, William Buckland Foundation**
- ✓ Martyn Myer AO, **President, The Myer Foundation**
- ✓ Leonard Vary, **CEO, The Myer Foundation & Sidney Myer Fund**
- ✓ Peter Winneke, **Head of Philanthropic Services, The Myer Family Company**
- ✓ Peter Whitehead, **Director, Traditional Trustee Company Services, Myer Family Company** *(formerly* **NSW Public Trustee, Nat'l President TCA & Nat'l Mgr Fiduciary Solutions, Perpetual**)
- ✓ Dr John Baxter, **Chairman, Percy Baxter Charitable Trust**
- ✓ Denis Tricks AM, **Chairman, Hugh Williamson Foundation**
- ✓ Martin Carlson OAM, **Trustee, Hugh Williamson Foundation**
- ✓ Steve Killelea, **Chairman & Founder, The Charitable Foundation & Global Peace Index**
- ✓ Clyde McConaghy, Trustee, **The Charitable Foundation & Global Peace Index**
- ✓ Martin Armstrong, **Director** *(of Corp. Trustee of)***, Jack Brockoff Foundation**
- ✓ Barry Capp, **Former Chairman, William Buckland Foundation & Philanthropy Australia**
- ✓ Elizabeth Cham, **IPCS & Former CEO, Philanthropy Australia**
- ✓ Jill Reichstein OAM, **Chair, Reichstein Foundation**
- ✓ Esther Abram, **Chief Executive Officer, Changemakers**
- ✓ Alan Froud, **Deputy Director, National Gallery of Australia**
- ✓ Andrew Danks and Mike Danks, **Honorary Trustees, Danks Trust**
- ✓ Alan Froud, **Trustee, Ord Poynton Dequest**
- ✓ Sylvia Admans, **CEO, RE Ross Trust**
- ✓ Darvell Hutchinson, **Chairman, Helen Macpherson Smith Trust**
- ✓ Andrew Brookes, **Chief Executive, Helen Macpherson Smith Trust**
- ✓ David Leeton, **Director, Victor Smorgon Charitable Fund & CFO, The Victor Smorgon Group**
- ✓ Gerard O'Neill, **CEO, Bush Heritage**

Annexure 1: Charitable Alliance (continued ...)

Community Council for Australia (CCA) 'members'

The Community Council for Australia (**CCA**) forms part of the Charitable Alliance.

The CCA is an independent, non-political member-based organisation dedicated to building flourishing communities primarily by enhancing the extraordinary work and effort undertaken within the not-for profit sector in Australia.

CCA seeks to change the way governments, communities and the not-for-profit (**NFP**) sector relate to one another. This includes establishing a regulatory environment that works for community organisations and not against them.

The mission of CCA is to lead the sector by being an effective voice on common and shared issues affecting the contribution, performance and viability of NFP organisations in Australia, through:

- ✓ Promoting the values of the sector and the need for reform
- ✓ Influencing and shaping relevant policy agendas
- ✓ Informing, educating, and assisting organisations in the sector to deal with change and build sustainable futures
- ✓ Working in partnership with government, business and the broader Australian community to achieve positive change

The CCA board includes:

- ✓ Tim Costello, CCA Chair and CEO World Vision Australia
- ✓ Stephen Judd, CEO, HammondCare
- ✓ Brett Williamson, CEO, Surf LIfe Saving Australia
- ✓ Mary Jo Capps, CEO, Musica Viva
- ✓ David Crosbie, CEO, CCA
- ✓ Jayne Meyer-Tucker, CEO, Good Beginnings
- ✓ Lisa O'Brien, CEO, The Smith Family.
- ✓ Toby Hall, CEO, Mission Australia
- ✓ Steve Persson, CEO, The Big Issue In Australia
- ✓ Dennis Young, CEO, Drug Arm
- ✓ Heather Neil, CEO, RSPCA
- ✓ Anne Hollonds, CEO, The Benevolent Society
- ✓ Keith Garner, CEO, Wesley Mission

Membership as at August 2012:

1. Aboriginal Employment Strategy Ltd – Danny Lester
2. Access Community Group – Samantha Hill
3. Alcohol and other Drugs Council of Australia – David Templeman
4. Alcohol Tobacco and Other Drugs Association ACT – Carrie Fowlie
5. Associations Forum Pty Ltd – John Peacock
6. Australian Charities Fund – Edward Kerr
7. Australian Council For International Development – Marc Purcell
8. Australian Indigenous Leadership Centre – Rachelle Towart

... continued over

Annexure 1: Charitable Alliance - Community Council for Australia (CCA) 'members' (continued ...)

9. Australian Institute of Superannuation Trustees – Fiona Reynolds
10. Australian Major Performing Arts Group – Bethwyn Serow
11. Catholic Social Services Australia – Paul O'Callaghan
12. Church Communities Australia – Chris Voll
13. Connecting Up Australia – Doug Jacquier
14. Consumers Health Forum of Australia – Carol Bennett
15. Drug-Arm Australia – Dr Dennis Young (CCA Board Director)
16. Foundation for Alcohol Research and Education – Michael Thorn
17. Fundraising Institute of Australia – Rob Edwards
18. Good Start Childcare – Julia Davison
19. Good Beginnings Australia – Jayne Meyer Tucker (CCA Board Director)
20. HammondCare – Stephen Judd (CCA Board Director)
21. HETA Incorporated – Sue Lea
22. Hillsong Church – George Aghajanian
23. Illawarra Retirement Trust – Nieves Murray
24. Lifeline Australia – Dr Maggie Jamieson
25. Maroba Lodge Ltd – Viv Allanson
26. Melbourne City Mission – Rev Ric Holland
27. Mental Health Council of Australia – Frank Quinlan
28. Mission Australia – Toby Hall (CCA Board Director)
29. Musica Viva Australia – Mary Jo Capps (CCA Board Director)
30. Opportunity International Australia – Rob Dunn
31. Philanthropy Australia – Deborah Seifert
32. Principals Australia – Jim Davies
33. ProBono Australia – Karen Mahlab
34. RSPCA Australia – Heather Neil (CCA Board Director)
35. St John Ambulance Australia – Peter Lecornu
36. Social Ventures Australia – Michael Traill
37. Surf Life Saving Australia – Brett Williamson (CCA Board Director)
38. The ANZCA Foundation – Ian Higgins
39. The Benevolent Society – Anne Hollonds (CCA Board Director)
40. The Big Issue – Steven Persson (CCA Board Director)
41. The Centre for Social Impact – Peter Shergold
42. The Smith Family – Dr Lisa O'Brien (CCA Board Director)
43. The Ted Noffs Foundation – Wesley Noffs
44. Volunteering Australia Inc. – Cary Pedicini
45. Wesley Mission – Rev. Keith Garner (CCA Board Director)
46. WorkVentures Ltd – Arsenio Alegre
47. World Vision Australia – Rev. Tim Costello (CCA Chair of Board)
48. YMCA Australia – Ron Mell
49. Youth Off The Streets – Fr Chris Riley
50. YWCA Australia - Dr Caroline Lambert

Annexure 2: Charitable Alliance June 2012 Letter to Government

Charitable Alliance

Friday 8 June 2012

Charitable Alliance
c/- Community Council for Australia
Level 1, The Realm, 18 National Circuit
Barton, ACT, 2600

The Hon. Wayne Swan MP, **Deputy Prime Minister and Treasurer**
The Hon. David Bradbury MP, **Assistant Treasurer**
The Hon. Bill Shorten MP, **Minister for Financial Services and Superannuation**
The Hon. Mark Butler MP, **Minister for Social Inclusion**

P.O. Box 6022
House of Representatives
Parliament House
Canberra ACT 2600

Dear Ministers,

Professional Trustee Company (PTC) Issues
Excessive fees & governance issues cost Australian community millions annually

We write as an '*Alliance*' of concerned trustees, advisors to and stakeholders of Charitable Trusts and Foundations (**Charitable Alliance**) that continue to provide significant financial and other support to communities across Australia, to request:

1. A formal review of the Corporations Amendment *(Financial Services Modernisation)* Act 2009 (**CAFSMA**), in line with the explanatory memorandum (**EM**) of the CAFSMA that states "the Government is committed to a review of the fee arrangements in relation to charitable trusts after two years of operation". We note that May 2012 is two years since the CAFSMA came into effect in May 2010.

   We also note that Charitable Alliance representatives have been unable to access details of the committed two year review. From phone calls and meetings in March and April 2012, it appears no review is currently underway or planned. Calls and or meetings were held with:
   - Treasury Department Liaison Officer;
   - Treasury Corporations & Capital Markets Division;
   - Office of the Minister for Financial Services & Superannuation; and
   - Management of the Retail Investor Division of Treasury.

2. Where the Charitable Alliance's concerns are not captured in the CAFSMA Review (*item 1*), that the Federal Government undertakes a broader review and implement necessary legislative changes to address serious issues relating to the role of PTCs in the governance and administration of Charitable Trusts and Foundations in Australia – refer **Briefing Note B** *(attached)*.

To support this formal request, attached to this letter are some preliminary briefing notes on issues relating to PTCs and their role in the governance and administration of Charitable Trusts & Foundations in Australia:
A. Role of, fees charged by & changed nature of PTCs (**Briefing Note A**)
B. Issues requiring review (**Briefing Note B**)

Absent a court application to remove a PTC, there is no mechanism to change from one PTC to another. Where the PTC is the sole trustee, any such court application would be novel. Therefore PTCs are not exposed to competition and lack accountability. Charitable Trusts & Foundations may not obtain services at the lowest possible price. Unfortunately, this leads to significant decreases in financial and other support to disadvantaged communities across Australia, the ultimate beneficiaries of the Charitable Trusts & Foundations.

Note: this letter and briefing notes seek to bring various matters to the Federal Government's attention and seek pro-active review and change. This is not intended to be a comprehensive submission. Page 1

Charitable Alliance

Professional Trustee Company Issues (continued ...)

Lack of portability is very rare in the financial services sector. For example, Australian consumers have the freedom to move their superannuation benefits from one fund to another and consequently benefit from increased competition. The Federal Government has also recently made it both less burdensome, administratively and financially, for Australian consumers to transfer their mortgages to another bank. The desirability of introducing portability of PTCs to the Charitable Trusts & Foundations sector is compelling.

Please note this letter seeks to bring this matter to the Federal Government's attention and seek pro-active review and changes. However is not intended to be a comprehensive submission.

This matter is of extreme importance to our many community organisations that are adversely impacted significantly by the existing legislation.

The Charitable Alliance requests that The Federal Government:

1. Confirm that a formal review of the CAFSMA will occur in line with the explanatory memorandum;
2. Notify the Charitable Alliance of the CAFSMA review details when finalised, to allow a formal submission(s) to be made; and
3. Ministers meet with Charitable Alliance representatives to discuss these important issues for Charitable Trusts & Foundations – organisations that are committed to supporting those in need in our community.

Kind Regards,

Graeme Danks	Sandy Clark	Tim Costello AO
Honorary Trustee	**Chairman**	**Chairman**
Danks Trust	**William Buckland Foundation**	**Community Council for Australia (CCA)**

This letter is sent on behalf and with the endorsement of an '*Alliance*' of the following concerned trustees of, advisors to and stakeholders of Charitable Trusts and Foundations:

Peter Yates AM, **Chairman Designate, Royal Children's Hospital Foundation, Melbourne**
Simon McKeon, **Chairman, Global Poverty Project Australia & Business for Millennium Dev't**
Ian Smith, **Director, Baker IDI Heart & Diabetes Institute Holdings Ltd** *(Partner, Bespoke Approach)*
David Crosbie, **CEO, CCA & Member, Not-for-Profit Sector Reform Council**
Richard Leder, **Deputy Chairman, Royal Children's Hospital Foundation, Melbourne**
Sue Hunt, **Executive Director, Royal Children's Hospital Foundation, Melbourne**
Graeme Sinclair, **Trustee, William Buckland Foundation**
Jane Gilmour OAM, **Trustee, William Buckland Foundation**
Martyn Myer AO, **President, The Myer Foundation**
Leonard Vary, **CEO, The Myer Foundation & Sidney Myer Fund**
Peter Winneke, **Head of Philanthropic Services, The Myer Family Company**
Dr John Baxter, **Chairman, Percy Baxter Charitable Trust**
Denis Tricks AM, **Chairman, Hugh Williamson Foundation**
Martin Carlson OAM, **Trustee, Hugh Williamson Foundation**
Elizabeth Cham, **IPCS** *(Former CEO, Philanthropy Australia)*
Jill Reichstein OAM, **Chair, Reichstein Foundation**
Esther Abram, **Chief Executive Officer, Changemakers**
Alan Froud, **Deputy Director, National Gallery of Australia**
Andrew Danks, **Honorary Trustee, Danks Trust**
Mike Danks, **Honorary Trustee, Danks Trust**

Copied to: Robert Fitzgerald (Chair) & Susan Pascoe (CEO), ACNC
Sue Vroombout / Irene Sim & Simon Milnes, Retail Investor Division, The Treasury

Note: this letter and briefing notes seek to bring various matters to the Federal Government's attention and seek pro-active review and change. This is not intended to be a comprehensive submission. Page 2

Charitable Alliance

Professional Trustee Company (PTC) Issues
Briefing Note A: Role of, fees charged by & the changing nature of PTCs

The issues identified below result in the **reduction of tens of millions of dollars every year** to the funds available to be distributed in grants to not-for-profit organisations who support important needs in the Australian community.

1. Australian trustee companies administer circa 2,000 Charitable Trusts and Foundations with assets of approx. $3.3 billion, usually as sole trustee. During 2008/09 these trusts are understood to have distributed circa $180 million in grants to the Australian community.

2. When many of the trusts were formed (many in the late 1800's and early 1900's), PTCs were 'pure' Trustee Companies. Today they are often subsidiaries of mainstream commercial financial service providers, with 'trusts' forming a minor part of their business (circa $3.3bn against a total assets managed of over $500bn).

3. The Corporations Legislation Amendment Act 2009 - Financial Services Modernisation (**CAFSMA**), inserted Chapter 5D into the Corporations Act 2001 (Cth) (Corps Act), resulted in changes to the Act that captured 'Trustee Companies' including their role as 'professional' trustees. The CAFSMA refers to an annual fee of 'up to' 1.056% of *capital*. Such a change to the fee structure results in a significant increase in the fees payable to Trustee Companies by many Charitable Trusts & Foundations, thereby reducing substantially the funds available to support those in need in the community.

4. The CAFSMA does not deal with, or limit, the range of other additional fees that are often charged by PTCs over and above the fee structure outlined in the CAFSMA, including, but not limited to, Investment Management or Advisory fees – fees which are not regulated and in many cases are not independent and or competitively tendered. These additional fees further reduce the funds available to support the Australian community.

5. The CAFSMA took effect on 6 May 2010. The explanatory memorandum of the CAFSMA states that "the Government is committed to a review of the fee arrangements in relation to charitable trusts after two years of operation" (paragraphs 2.66 & 7.162 of the EM). This is in relation to the fee arrangements for both existing and new charitable trusts (paragraph 2.93). Two years is May 2012. As at May 2012, it appears no review is currently underway.

6. A large portion of the fees charged by PTCs are paid by Charitable Trusts & Foundations established with monies left by deceased individuals and families on the understanding that the trust/foundation would be maintained in perpetuity for the benefit of the most disadvantaged in the community. In the majority of cases:
   A. The founders, nor any descendants, are no longer there to advocate on their behalf; and
   B. There are no independent trustees to:
      - Ensure independence between the governance role of a trustee and the provision of a range of paid services; and or
      - Challenge additional fees charged over and above the substantial CAFSMA fees under.

   So, in practice, a PTC's 'profit' arm, can tell itself, as the sole trustee of Charitable Trusts & Foundations, that certain fees will be charged and increased at its discretion.

NOW is the time to address the loss to the Australian community of tens of millions of dollars every year. The substantial reduction in funds Charitable Trusts & Foundations are able to distribute to those in need in the community is being reduced at a time when the structure of the Australian economy is changing at a rapid rate, resulting in:

- Ever increasing demands on governments and not-for-profit organisations; and
- A reduction in available funding to not-for-profit organisations from other non-government sources, compounded by many larger not-for-profit organisations' own investments being impacted by the flow on effects of the current uncertainty in global economies

Charitable Alliance

Professional Trustee Company (PTC) Issues
Briefing Note B: Issues Requiring Review

1. **Fee Calculation**
   Recent amendments to legislation (**CAFSMA**) resulted in the method of calculating PTC's fees changing to be a % of *capital*. In many cases that we are aware of, this has resulted in a significant increase in fees being charged to Charitable Trusts & Foundations by PTCs, often with no increase in services provided. Historically, most Charitable Trusts & Foundations have been charged a small percentage of annual *income*. To demonstrate the significant impact of this change, a number of '**Case Studies**' will be provided to the CAFSMA review. In the meantime, two current examples follow showing the significant fee increases being demanded by two PTCs:
   A. **Example A**: Trust assets = $17.5m. 'Will' prescribes the fee at 2.5% of income (~$20,000 to $30,000/year). Post-CAFSMA this PTC is now demanding its '*statutory fee entitlement*', which equates to ~$170,000/year. Increase = $140,000 (550% to 650%).
   B. **Example B**: Trust assets = $57.2m. Pre-CAFSMA PTC fee = ~$179,000/year. Subject to the interpretation of the 'grandfathering provision', the post-CAFSMA fee could be either $328,000 or $604,000/year. Increase = either $149,000 (83%) or $425,000 (237%).

2. **'Grandfathering'**
   Recent amendments (CAFSMA) were 'intended' to 'grandfather' prior arrangements. Due to a lack of clarity in the legislation and 'heavy handed' approach applied by the PTCs, this intention has not been achieved.

3. **'Portability'**
   Australia is unusual in that in many cases individual (honorary) trustees must take court action (at significant risk, time & expense) in order to seek removal of a PTC as a co-trustee (e.g. due to poor service or excessive fees). This results in an inefficient trustee company sector, inflated fees and significantly less funding available for distribution to the Australian community through not-for-profit entities. The introduction of 'portability' of the 'Professional Trustee' role, exercised through a regular competitive tender process for co-trustees and sole trustees would address many of these issues, allowing market forces to bring efficiency to the sector.

4. **Transparent Reporting**
   PTCs manage about 2,000 Charitable Trusts & Foundations, only a handful of which report publicly. Accordingly there is no transparency of these trusts at all. Transparency is required particularly for those Charitable Trusts & Foundations where a PTC is the sole trustee. Issues that can arise in such situations include the inability to ensure fees charged are equitable given the level of services provided. A regulator, such as the Australian Charities and Not-For-Profit Commission (**ACNC**), could monitor this field and have the ability to dismiss a sole trustee due to poor service or excessive fees. Reporting could be a simple process. A return could:
   - Be completed for each trust each year;
   - Include financial statements, list of grants made and detailed expenses including PTC fees;
   - Allow a regulator to review these trusts' activities (currently not monitored by any external body) and be alert for abnormal activities, including excessive fees; and
   - Allow for aggregate information to be released on the size & scope of the philanthropic sector.

5. **Governance Independence**
   An inherent conflict exists across Charitable Trusts & Foundations, where PTCs fulfil roles as both:
   A. Trustee - 'governance', for which fees can be charged under the CAFSMA; and
   B. Paid Service Provider roles (e.g. investment advisory, compliance, administration and or grant making), for which additional unregulated fees are charged, on top of CAFSMA fees.

   This issue is heightened where a PTC is the sole trustee of a Charitable Trust, where founders are no longer alive and there is no independent trustee(s). Independence would open the sector to additional service providers and competition. Independent governance could be achieved by regulating the obligation to separate:
   - The 'governance' function as legal 'trustee'; and
   - Fee charging service provision.

   That is, a paid Trustee may not also be a paid service provider to the same / related trust to which they are a trustee. Beyond independence this will allow efficiency through market forces.

Annexure 3: Charitable Trusts in Australia

A charitable trust is a trust which is dedicated not to a specific class of beneficiaries, but to charitable goals. It is one of the main ways under Australian law that people can devote their money to philanthropic causes.

There is a lack of proper data on how many charitable trusts are managed by TCs. The Financial Services Council (an industry group which includes TCs) says that the TCs manage around 2000 charitable trusts and foundations with assets of approximately $3.2 billion, and in the 2009/10 financial year distributed about $175 million in grants to charitable causes. The uncertainty about the size of this segment will be remedied when the requirement for registration under ACNC will be introduced in order for the taxation concessions to continue.

CAFSMA was introduced to nationalise the regulation of trustee companies by bringing them under the regulation of the *Corporations Act*. Under the amendment the 'traditional services' of trustee corporations were deemed to be 'financial services' for the purposes of the Corporations Act, requiring them to meet the standards and disclosure obligations of other financial services corporations, such as those in Chapter 7 of the Corporations Act. Interestingly CAFSMA treated charitable and non-charitable trusts in different ways and ensured that this review was to be part of ensuring that regulation of charitable trusts met the stated objectives.

Charitable trusts are more reliant on their trustees to conduct themselves properly than other trusts. Many trusts provide for discretionary benefit to organisations who fit the designated charitable purpose, and consequently there are often no beneficiaries which can easily challenge the conduct of the trustees. This has not been remedied by CAFSMA. Rather, it is the role of the States' Attorneys-General to oversee charitable trusts on behalf of the community: it is the duty of the Crown to protect property devoted to charitable purposes. If an Attorney-General considered that it was necessary to intervene in the management of a charitable trust, he or she would make an application to the Court which has an inherent jurisdiction over the management of trusts.

The new regulator that was launched by the Hon. David Bradbury MP on Monday 10 December 2012 – the ACNC Commissioner – has the potential to take over the regulation and oversight of charitable trusts, including setting fees and the suspension and removal of trustees. The reporting requirements will provide valuable information for review and encourage analysis of pricing trends.

The Charitable Alliance is of the view that the best way forward is to ensure that all charitable trusts are overseen by this new regulatory body as there are limitations with any other alternative. ASIC is a corporate regulator and currently only regulates licensing of TCs generally at the macro level. ASIC does not regulate private or lay trustees and public trustees who may fill the trustee role in charitable trusts. These trustees are still only subject to the review of Attorney Generals and Courts of the States.

*A large portion of Charitable Trusts are '**Orphan Trusts**', where TCs are now the sole trustee. These trusts usually exist as a result of:*

- *the death of the original trustees*
- *having been established with a sole trustee*

Orphan Trusts have no one to effectively stand up for the interests of the community, against the commercial imperatives of TCs

Annexure 4: New fees regime under Div 4, Sub-div B of Part 5D.3

A maximum, or an '*entitlement*'?

The enactment of Division 4 of Chapter 5D.3 of the *Corporations Act* on 6 May 2010 permits TCs two alternative options when setting the fees of new charitable trusts:

- A one-off capital commission at a rate not exceeding 5.5% of the gross value of the charitable trust's assets (which can only be charged once during the period while the trustee company is trustee or manager of the charitable trust) along with an income commission of not more than 6.6% of income received on account of the charitable trusts assets.
- Alternatively, an annual management fee not exceeding 1.056% of the gross value of the trust's assets.

As can be seen from the case studies provided in Appendix" ", many TCs have used the introduction of the Commonwealth legislation as an opportunity to charge the maximum allowed fees set out in the legislation. TCs have made it clear that in practice they view Part 5D.3 as setting a statutory entitlement rather than a statutory maximum.

The Charitable Alliance takes the view that Part 5D.3 sets a statutory maximum, a ceiling on fees. In fact, unless the charitable trust is particularly difficult and complicated to manage, the fees should be considerably lower than this maximum and be limited to the actual cost of the service that the TC provides with a reasonable return.

A close inspection of the *Corporations Act* shows this interpretation to be more consistent with the words and intention of the Commonwealth Parliament:

- The two fee options provided by section 601TDC and TDD of the *Corporations Act* provide that a trustee company may charge a commission or fees 'at a rate ***not exceeding***' the prescribed amounts that follow. If the Parliament had intended the fee to be an entitlement the language used would have clearly stated that it was an entitlement.
- Furthermore, the Court is empowered under section 601TEA(3) to review and reduce the fees charged by a trustee company if it considers the amount "excessive". If trustee companies were entitled to charge the amounts prescribed by Division 4 of Chapter 5D.3 of the *Corporations Act 2001*, after all, there would be no need for the Court to assess whether such fees were 'excessive'.

Annexure 5: ASIC Licensing and options for dispute resolution

CAFSMA created a new class of financial services licence to regulate TCs. In order to hold such a licence a company must be able to carry out "traditional trustee company services" and "estate management functions." Specifically, before a company will be allowed to act as a TC it must be capable of:

1 Applying for probate of a will, applying for a grant of letters of administration, or election to administer a deceased estate; and

2 Acting as executor or administrator of a deceased estate, plus one other "estate management function".

The reforms allow for ASIC and consumers to have oversight of TCs providing traditional trustee services for charitable trusts. There are two primary mechanisms by which this occurs: the information gathering procedure and the dispute resolution procedures.

(a) Information gathering procedures

Under CAFSMA, there are two primary methods by which certain persons may gather information about the assets and operation of a charitable trust: trustees' obligation to provide an account and annual information returns.

Trustee's obligation to provide an account

Upon the request of a 'person with a proper interest' in a trust, a trustee of a charitable trust must provide an account of the trust. This account must detail all of the following:

a) the assets and liabilities of the estate; and

b) the trustee company's administration or management of the estate; and

c) any investment made from the estate; and

d) any distribution made from the estate; and

e) any other expenditure (including fees and commissions) from the estate.

In the charitable trust context, a 'person with a proper interest' is defined as follows:

a) the settlor, or one of the settlors, of the trust; or

b) a person who, under the terms of the trust, has power to appoint or remove a trustee of the trust or to vary (or cause to be varied) any of the terms of the trust; or

c) a Minister of a State or Territory who has responsibilities relating to charitable trusts; or

d) a person who is named in the instrument establishing the trust as a person who may receive payments on behalf of the trust; or

e) a person who is named in the instrument establishing the trust as a person who must, or may, be consulted by the trustee or trustees before distributing or applying money or other property for the purposes of the trust; or

f) a person of a class that the trust is intended to benefit.

'Annual information return'

The *Corporations Regulations 2001* (Cth), provides that certain persons are entitled to call for an 'annual information return' from the trustee. In respect of a charitable trust, these persons are:

a) a settlor, or one of the settlors, of a trust;

b) a person who, under the terms of the trust, has power to appoint or remove a trustee of the trust or to vary (or cause to be varied) any of the terms of the trust; or

c) a person, or person's appointed successor, who is named in the instrument establishing a trust as a person who must, or may, be consulted by the trustee or trustees before distributing or applying money or other property for the purposes of the trust.

If requested, the trustee must provide the information in an Annual Information Return about the details of income earned on the person's interest in the trust, details of the operating expenses and the net value of the person's interest in the trust or estate.

(b) Dispute Resolution Mechanisms

The Corporations Act licensing requirements now provide that companies providing "traditional trustee services" must have both internal and external dispute resolution processes that relate to the provision of those services.

Internal Dispute Resolution

A trustee company providing "traditional services" must, under the internal dispute resolution requirements of the Corporations Act, give a final response to a complainant within a maximum of 90 days. From there, the complaint, if not replied to or resolved to the satisfaction of the complainant, must be referred to external dispute resolution.

External Dispute Resolution

External dispute resolution is a type of private dispute resolution whereby the financial services providers, including trustee companies providing traditional services, sign up to be bound by a particular set of dispute resolution frameworks. While the TCs can decide how the external dispute resolution is to operate, it is done principally through the Financial Ombudsman Service (**FOS**). Importantly, the cost of this dispute resolution mechanism is borne by the financial services company. This means that the consumer does not have to pay expensive legal fees and can afford to complain about the conduct of the company providing the service. FOS provides consumers with an avenue of dispute resolution which is focused on conciliation and amicable resolution, but also has the capacity of giving determinations on the merits which are binding on the service provider.

Annexure 6: The position in the States and Territories prior to CAFSMA

a) Victoria

Section 21(1) of the *Trustee Companies Act 1984* (Vic) provided trustee companies could not charge more than a commission of 5.5% of the gross value of the estate and 6.6% of income received by the trustee company on account of the estate. The Act also allowed for an alternative maximum fee at section 21A(2), which provided a TC could receive an administration fee of no more than 1.056% per annum of the value of a perpetual trust.

However, this statutory limit was further complicated by section 21(8) of the Act, which allows a Trustee Company to be paid more than what is permitted by the *Trustee Companies Act* if it was set out in the Trust Deed. While a Trustee Company is not ordinarily entitled to receive both a commission and an administration fee under section 21A(3), this prohibition does not capture payments under section 21(8). Therefore it is possible to envisage a situation – particularly with older trusts – where the Trustee Company could argue it was entitled to more than the maximum in section 21(1).

b) New South Wales

Section 18(1)(c) of the Trustee Companies Act 1964 (NSW) provided that the trustee company may not charge fees exceeding 4.25% of the corpus or capital value of the estate, and 5.25% of the income received by the trustee company on account of the estate.

c) Queensland

Section 41(1) of the Trustee Companies Act 1968 (Qld) provided trustee companies were not charge fees exceeding 5% of the capital value of the estate and 6% of the income received by the trustee company on account of the estate.

d) South Australia

Section 9(1) of the Trustee Companies Act 1988 (SA) permitted a trustee company to charge against each estate committed to its administration or management a commission not exceeding 7.5% of the income by the company on account of the estate, and 6% of the capital value of the estate.

e) Tasmania

Section 18(1) of the Trustee Companies Act 1953 (Tas) allowed a trustee company to charge and receive a commission at a rate not exceeding 5% of the capital value of any estate committed to the company's administration or management, and 5% of the income received by the company.

f) Western Australia

There was no maximum level of fees set in Western Australia. The only limitation was Section 18(2) of the Trustee Companies Act 1987 (WA), which required commissions and charges to be set out in the latest scale of charges of that trustee company published before the administration of the estate commenced.

g) Australian Capital Territory

Similar to Western Australia, there was no statutory maximum level of fees in the ACT. Section 18(1) of the Trustee Companies Act 1947 (ACT) allowed a trustee company to charge fees for its services in relation to the administration or management of an estate in accordance with the published scale of fees of the trustee company.

h) Northern Territory

Section 27(1) of the Companies (Trustees and Personal Representatives) Act 1981 (NT) provided that a trustee company was not permitting to charge more than 5% of the capital value of the estate, and 5% of the income received by the company on account of the estate.

Annexure 7: Private Ancillary Funds

Private Ancillary Funds (PAFs) were introduced by the Federal Government in 2001 to assist grow the philanthropic sector. The Prime Minister at the time, John Howard, stated that "This measure will open up a new vehicle for private philanthropy, similar to that existing in the United States, so that families and individuals can donate to a trust of their own, which then disburses funds to a range of other gift-deductible recipients." The introduction of PAFs has had a strong influence on the growth of the philanthropic sector. Since inception over 1,000 PAFs have been established and they have an aggregate corpus of over $2.2 billion.

The PAF Guidelines were reviewed and tightened in 2009. The Explanatory Statement released with the final 2009 Guidelines stated, "The Guidelines aim to ensure that PAFs are properly accountable and act in the manner expected of an entity holding philanthropic funds for a broad public benefit."

PAFs are best practice philanthropy in Australia. They are the most regulated form of charitable trust in Australia with public accountability initially through the ATO, now to move to the ACNC. PAF governance requirements ensure PAFs:

- Are subject to detailed PAF Guidelines which must be adhered to with penalties for non-compliance;
- Must have at least one independent director or trustee, known as a Responsible Person (it is interesting to note that for Public Ancillary Funds the majority of directors/trustees must hold a position of responsibility within the community);
- Responsible Person must be an active director/trustee;
- Must prepare annual financial statements which must be independently audited;
- Must have a documented investment strategy;
- Must lodge an annual PAF Return with the ATO. This Return includes a summary of:
    - Director/trustee details
    - Income and expenses
    - Assets and liabilities
    - Gifts made
    - Confirmation that a financial audit has occurred
    - Confirmation by the independent auditor of compliance by the PAF and the trustee with the PAF Guidelines

The PAF Guidelines can be reviewed at:
http://www.comlaw.gov.au/Details/F2009L03700/Download

A PAF Return can be reviewed at:
http://www.ato.gov.au/nonprofit/content.aspx?doc=/content/00322934.htm

Annexure 8: Case Studies

Due to the lack of transparency, it has and continues to be difficult to present macro data and or sector wide evidence of the various issues. As a result, the Charitable Alliance has provided some brief 'Case Studies' to provide some specific examples of the significance of the issues surrounding licensed Trustee Companies (TCs) and Charitable Trusts and Foundations.

These case studies are provided in-good-faith without prejudice on an anonymous basis as recommended by Johh Kluver Executive Director of CAMAC.

Case Study 1: Philanthropic Adviser

A member of the Charitable Alliance is aware of numerous cases of philanthropic advisers (non traditional TCs) charging for trustee, secretariat and grant research services on a fee-for-service basis. Similar to other professional service providers (e.g. lawyers and accountants) these philanthropic advisers maintain timesheets and charge clients based upon the actual services provided, based upon hourly rates.

Whilst the fees vary dependent upon the level and number of services provided, including number of grants made, meetings per year and program-related activity (e.g. site visits), and are charged based on hourly rates - **the fees tend to vary between 0.1% to 0.3% of the foundations' corpus** *(ave across the examples = 0.204%)* – compared with a fixed 1.056% of capital regardless of the level of service provided.

For client confidentiality reasons the name of the adviser and clients is not appropriate for including in this submission, however the examples based on actual services provided and fees charged (excluding investment management fees) are:

- Foundation A: corpus $24m with fees for all services equating to 0.23% of corpus
- Foundation B: corpus $16.5m with fees for all services equating to 0.33% of corpus
- Foundation C: corpus $10m with fees for all services equating to 0.22% of corpus
- Foundation D: corpus $28m with fees for all services equating to 0.06% of corpus
- Foundation E: corpus $11m with fees for all services equating to 0.29% of corpus

Refer also to the graph included as Example B in item 3 of this submission.

Comments:

- The TCA / FSC are understood to have argued that without TCs, Charitable Trusts would not be able to be managed prudently and sustainably. The above Case Study has been provided by one of many non-listed managers capable of managing Charitable Trusts on behalf of the community and other similar style organizations exist in the market today.
- In addition, to the existing non ASX listed TCs that exist today, by changing the AFSL license requirements (refer Recommendation 2D) a range of service providers would enter the market creating competitive services – across three categories:
  - 'corporate' / listed TCs
  - Non-listed private TCs focused on providing services to Charitable Trusts
  - Not-for-profit community based TCs, with honorary boards and professional staff

Annexure 8: Case Studies (continued ...)

Case Study 2: Charitable Foundation

- Foundation established in early 1960's in the benefactor's Will
- Five trustees, one of which is a TC
- *"There has always been a vigorous debate over the level of the TCs fees between the independent and TC"*
- In March 2010:
  - Debate heightened when the TC proposed a fee increase of 46%, from 0.30% of capital to 0.58% of capital
  - To avoid cost and risk of going to the court, the independent trustees negotiated in good faith a blended fee of 0.50% = 66% increase
    "The independent trustees considered the fee too high, but it was reluctantly accepted at the time because there was no real alternative, and we had to ensure that we continued to honour the content of the Will"
  - In their 'demands' the TC warned the independent trustees that the TC could cap their fee at 0.96%+GST (1.056%)

Comment / Question:

- The TC's fee demands added no additional value to the trust or the community and were not linked in any way to work done (e.g. hourly rates for services provided) or service standards
- We ask CAMAC – what would happen if this were an 'Orphan Trust', with no independent trustees there to protect the interests of the community beneficiaries?

Case Study 3: Orphan Trust

- Charitable Trust with a single beneficiary and a TC as sole trustee (Orphan Trust)
- TC's fee increased from $4,800 to $18,054 in a single year. When beneficiary queried the TC fee increase, the TC simply advised they were now entitled to charge 1.056% of the corpus and they had done so
- Fee increase = 250% increase in a single year

Comment / Question:

- The TC fee increase adds no additional value to the trust or the community and were not linked in any way to work done (e.g. hourly rates for services provided) or service standards
- We ask CAMAC – with no independent trustees there to 'try to' protect the interests of the community beneficiaries, in a practical sense, how does the current legislation protect the interests of the community beneficiaries?

Annexure 8: Case Studies (continued ...)

Case Study 4: Charitable Trust

- Established in 1949 in VIC. Trustees are two family trustees (descendents of settler) and a TC (named in 1949 trust deed)
- Assets circa $57.2m as of May 2012 invested across ASX shares, cash / fixed interest, property trusts and international shares
- Income of $3,260,000 in FY11/12 (~5.7% yield incl franking credits), fully distributed to charities
- TC fee is 5.0% of income + GST (= ~$179,000 per year)
- Victorian legislated TC fee = 6% of income + GST = $195,600 per year
- TC's fee scale for Charitable Trusts:
  - Pre 6/5/10 = $13,750 + 0.55% of capital for asset portion >$1m (incl. GST) = $328,000 per year
  - Post 6/5/10 = 1.056% of capital (incl. GST) = $604,000 per year
- CAFSMA legislation could result in the fees charged to the Charitable Trust increasing by:
  - A minimum of $149,000 per year (i.e. from $179,000 to $328,000 per year) = 83% increase
  - Up to $425,000 per year (i.e. from $179,000 to $604,000 per year) = 237% increase

Comment / Question:

- The TC's fee demand would add no additional value to the trust or the community and is not linked in any way to work done (e.g. hourly rates for services provided) or service standards
- We ask CAMAC – what would happen if this were an 'Orphan Trust', with no independent trustees there to protect the interests of the community beneficiaries?

Case Study 5: Charitable Trust

- Established in 1969 in NSW. Trustees are two family trustees (descendents of settler) and a TC (named in 1969 trust deed)
- Assets circa $13.0m as of May 2012 invested across ASX shares, cash / fixed interest, property trusts and international shares
- Income of $733,000 in FY11/12 (~5.6% yield incl franking credits), fully distributed to charities
- TC fee is 5.25% of income + $590 per year + GST (= ~$43,000 per year), based on NSW legislation
- TC's fee scale for Charitable Trusts:
  - Pre 6/5/10 = $13,750 + 0.55% of capital for asset portion >$1m (incl. GST) = $80,000 per year
  - Post 6/5/10 = 1.056% of capital (incl. GST) = $137,000 per year
- CAFSMA legislation could result in the fees charged to the Charitable Trust increasing by:
  - A minimum of $37,000 per year (i.e. from $43,000 to $80,000 per year) = 86% increase
  - Up to $94,000 per year (i.e. from $43,000 to $137,000 per year) = 218% increase

Comment / Question:

- The TC's fee demand would add no additional value to the trust or the community and is not linked in any way to work done (e.g. hourly rates for services provided) or service standards
- We ask CAMAC – what would happen if this were an 'Orphan Trust', with no independent trustees there to protect the interests of the community beneficiaries?

Annexure 8: Case Studies (continued ...)

Case Study 6: Charitable Trust

A. Trust was created in late 1920's & was administered by family trustees (*descendents of settler*) until early 1960's. Under the Will, a trustee company (**TC**) was appointed co-trustee in early 1960's. Today there are three family members (*descendents of settler*) and a TC as co-trustees.

B. Trust assets are circa $17.5 m, with annual distributions of between $0.9m and $1.2m

C. In accordance with the Will, the TC has been paid 2.5% of income for past 43 years *(in recent years has equated to $20,000 to $30,000/year + GST)*. Family trustees receive $200 each/year.

D. Will does not specify who is responsible for administration and grant making. This has and continues to be done by family trustees with administrative support provided at no cost to the trust by the executive office of the company formed by the founder, saving trust ~$30,000/year.

E. Other costs: Accountant prepares annual accounts and related compliance activities. Until recently the assets have been illiquid, however the trust is currently in the process of appointing an advisor to manage the trust's investments, a service which will incur an additional cost.

F. In November 2010 the family trustees received notice from the TC that *"... it is the TC's intention to charge the fee to which it is entitled, in accordance with its published fee scale for discretionary perpetual charitable trusts, commencing 1 July 2011.*" The fee scale nominated is:
   - 1.056% of the first $10m of capital; plus
   - 0.88% of the next $10m of capital

G. The TC's demand to charge its '*fee entitlement*':
   - Could equate to a fee of $150,000 to $170,000 per year (*depending on valuation of assets*) *(or up to $185,000 if in the future the TC decides to charge 1.056% on the total capital)*
   - Adds no additional value to the trust or the community
   - Is not linked in any way to work done (e.g. hourly rates for services provided) or service standards
   - Does not include investment services
   - Would result in a 12% to 15% reduction in funds available to distribute to the community every year

H. CAFSMA legislation could result in the fees charged to Charitable Trust increasing over fees charged for the last 43 years, by:
   - A minimum of $125,000 per year (i.e. from $25,000 to $150,000 per year) = 500% increase
   - Up to $160,000 per year (i.e. from $25,000 to $185,000 per year) = 640% increase

At no time has the TC outlined the costs they incur in providing the service or provided any attempt to justify their fee, solely to state and restate "... *it is our entitlement* ..." (relying on CAFSMA legislation). Since November 2010, letters received by the family trustees have included the following statements

- November 2010 *"... it is the TC's intention to charge the fee to which it is entitled ...*"
- June 2011 "*This is a statutory entitlement and is not subject to co-trustee consent*."
- September 2011 *"... we do intend to charge the fee to which the TC is entitled ..."*
- July 2012 *"... we have an entitlement to charge a fee for the trust administration"*
- September 2012 *"... the TC' entitlement arises under Corps. Act ..."*
- November 2012 "*This is our statutory entitlement and is not subject to co-trustee consent*…'

Question: If this case study is not bad enough, we ask CAMAC – what would happen if this were an 'Orphan Trust', with no independent trustees there to protect the interests of the community beneficiaries?

Annexure 8: Case Studies (continued ...)

Case Study 7: 'Community' Foundation vs '*related*' Orphan Trust *(with TC as sole trustee)*

Sadly this case study highlights the stark contrast / difference in community outcomes and impact that a dedicated, discreet and committed approach can have over a profit making, disinterested and disconnected TC - particularly in challenging economic times.

- The Foundation is one of Victoria's largest charitable endeavours, established in 1989 as trustee of funds donated to a children's hospital. Due to the public generosity it has been able to not only support the hospital in its pursuit of excellence, but has also built a considerable fund for the hospital's future. Growth has been strong and the difference that philanthropy has made to the hospital profound

- The Foundation has an Investment Committee with responsibility for managing and growing the corpus, in line with an investment policy adopted by the Foundation Board, designed to:
  - Be in the best interests of the hospital to further its ability to treat and heal sick children
  - Plan for the future of children's health
  - Consider and meet wishes of donors to make the greatest philanthropic return to the hospital

- In addition the hospital is the sole beneficiary of an Orphan Trust, being an estate gifted by a benefactor in 1960 (**Estate**). The Orphan Trust is managed by a TC as sole trustee and the Foundation has no rights over the management and development of Estate

- There is a considerable difference in performance between the funds invested and managed by:
  - The Foundation Investment Committee, which successfully steered its investments through the difficult circumstance of the last five years, presiding over growth overall; and
  - The Orphan Trust managed by the TC, which presided over losses.

- In the five years from 1 July 2007 to 30 June 2012, the Foundation (Investment Committee):
  - Capital funds under management grew by $13.8 million (12.02%), after management fees
  - In addition to the capital growth, distributed to its beneficiary (the hospital) > $80 million
  - By focusing not merely on building a corpus, as a trustee acting in the best interests of its beneficiary, the Foundation has been able to grow capital and continue to distribute

- In the (same) five years from 1 July 2007 to 30 June 2012, the Orphan Trust managed by the TC:
  - Capital funds under management reduced by $15.5 million (21.3%) and the TC purchased $7.04 million in its own growth fund, indicating a capital loss of > $22million for the period
  - Generated $14.5m in income of which $12.6m was distributed to the Foundation and $2.0m was retained by the TC in fees
  - Fees charged by the TC over the 5 year period ranged from 10% to 22% of annual income (*note: the CAFSMA legislation came into effect during that period*), with the average annual fee comprising 13.9% of income

- The Foundation Investment Committee is a group of individuals with considerable expertise in investment management, who act voluntarily and in the interests of the hospital. They are:
  - Not driven by individual or corporate gain, but rather by the genuine desire to do good works
  - Focused on improving society through investment in children's health and well being
  - Associated with the hospital because they understand the role of philanthropy and the importance of making the greatest impact of donors' funds

- The TC has different performance indicators:
  - They have no connection either to the original donor or the beneficiary
  - The fund is part of a much bigger portfolio and is not managed discreetly or with consideration to what the donor might have wanted or what the beneficiary might need
  - While they deliver on the 'Will' (by directing funds to the hospital), the level of income distributed and capital retained is entirely up to the TC
  - TC benefits financially from retaining capital and therefore has a disincentive to distribute income
  - They have discussed their fund and investment strategy with the Foundation, but have dismissed most Foundation suggestions. The TC has not disclosed the comprising the fund

- The Foundation, representing the hospital as beneficiary:
  - Has no governance relationship with the Orphan Trust
  - Is not aware of the underlying assets held by the Orphan Trust
  - Is not in a position to consider the relative benefits of the service provided by the TC, as it has no ability to shift funds, or to ensure its own investments are diversified from the Orphan Trust

Case Study 8: Charitable Trust

Established in 1985 shortly before settlor's death with assets of $4.9m. His Will specified:

- Independent trustees' annual fees at $1,500 and $3,000 for the Chairman, adjusted for CPI.
- Did not specify the fees for the TC, with the rate which applied at the time of establishment was 6% of income. As the Trust grew in value and income, the TC fees increased from approximately $22,000 in 1986 to about $77,000 in 2003.

Trustees' Remuneration (Fees)

In 1996 State legislation authorized TCs to charge an annual fee of 0.96% of capital value. The independent trustees pointed out that the Trust's share market investments returned 4%- 5% on capital and that a rate of 0.96% on capital could equate to some 25% of the annual income of the trust, a huge increase. After further objections from the independent trustees, the TC compromised on fee levels based on approximately 0.38% of capital – almost equaling 6% of income in value.

In 2010 the TC advised that, pursuant to the new federal legislation (CAFSMA), it would increase its charges to approximately 0.7% of capital, almost doubling the previous fee to an estimated $262,000 for 2012. This is based on the capital of the Trust – not on the cost of work done for the Trust which has actually reduced over time.

The investment portfolio is stable, with long term holdings, with very few transactions each year. It has been developed with considerable input from the individual trustees. Grants are driven by activities of the trustees, not by the secretariat services provided by the TC. Grants tend to be few in number, perhaps three for each monthly meeting. TC secretaries send invitations to guests to meetings and provide the correspondence required. During the earlier years of the Trust, TC has provided useful advisory services delivered by their officer who had considerable experience with charitable work. This service is no longer available.

The trust has operated for many years by holding total costs under 9% of income. In 2003 it was 6.3% ensuring 93.7% available for charitable and philanthropic purposes and to build the corpus of the Foundation. As trust is a perpetual trust it is important to control costs because of the long- term compounding effects of higher costs. The doubling of company trustee charges will have an adverse effect on the capacity to deliver to charities. The recent increase will nearly double the above figure.

There have been many personnel changes to the TC representatives on the trust. For many years one officer attended meetings, produced minutes and liaised with charities; lately there have been up to four TC representatives at meetings with no apparent increased benefit to the Trust.

Annexure 8: Case Studies
Case Study 8: Charitable Trust

Investment funds total $31m in mid 2012. Over $21 million has been distributed to the community.

CAFSMA legislation could result in the fees charged to Charitable Trust increasing by:

- A minimum of $100,000 per year (i.e. from $117,000 at 0.38% of capital based on the 6% income to $217,000 per year based on the 0.7% of capital negotiated in 2010) = 86% increase
- Up to $210,000 per year (i.e. from $117,000 to $327,000 per year) = 179% increase

Comment / Question:

- The TC's fee demand adds no additional value to the trust or the community and is not linked in any way to work done (e.g. hourly rates for services provided) or service standards
- We ask CAMAC – what would happen if this were an 'Orphan Trust', with no independent trustees there to protect the interests of the community beneficiaries?

Succession - At risk of becoming an 'Orphan Trust'

The trustees were given wide discretion under the Will, subject to trust law and limited to recognized charities in Victoria. The settlor separately indicated in a note some directions for support he favored. From the beginning, the trustees made a decision to act as an innovative trust, seeking to create new support activities for community in a manner reflecting the view of the settlor. This involved trustees being in close and continuous contact with most projects rather than reliance on paid secretarial direction. Three of the five original trustees with personal knowledge of the settlor are now over 80 years of age and have in mind the need for a continuation of his model for innovative trusts, as well as their advancing years. The three trustees are presently active in carrying out their trustee responsibilities.

It would be prudent for us to prepare for the future growth in the activities of The Trust, if the past 25 years are considered. "Hands On" trustees will be required to manage future activities. We have considered fixed term appointments but consider the merits of experience more important for the activities of this innovative trust.

We believe The Trust should appoint a further two younger trustees at this time to be ready for a transition which will retain the ideas established by those who knew the settlor personally. It is our opinion that the settlor would have supported this proposal without reservation.

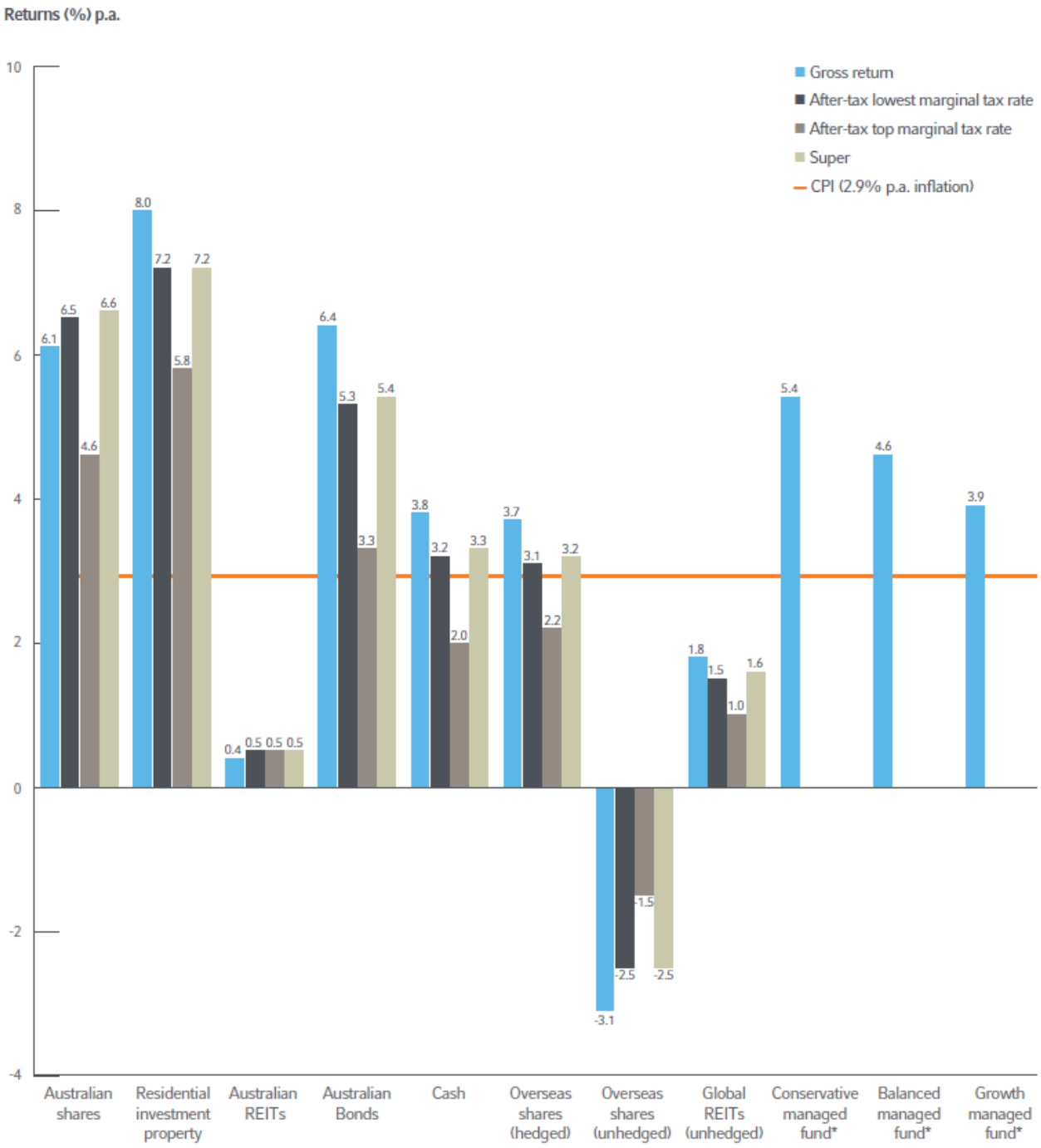
The TC will not allow the proposed succession to occur. However Sec 41(6) 1958 Trustee Act denies appeals to the court as there are more than three Trustees, one of which is a TC. We believe this power is unwarranted and appeals to the courts should be allowed. The Act should be amended.

Summary

1. The Individual Trustees believe the settlor tried to restrict the costs of managing his trust. He was satisfied with fees equating to 6% of income being paid to the TC. This has grown over time
2. The services offered by the TC have diminished over time. The cost control should belong to all the trustees, but is now in the hands of the TC.
3. There is no opportunity to expose trustee company fees to competition
4. TC fees are set according to capital of the Trust and not related directly to cost structures of the particular Trust. The TC fees are excessive in relation to activities.
5. Trustees should have the right to approach the court for relief when they believe the Trust is not been reasonably managed.
6. TC fee limits are far too high for many trusts. The principle of relating costs to fees should be individually applied to each trust.
7. The concept of equity between trusts is not necessarily consistent with the settlor's wishes or relate to each foundation's costs. There is a conflict between the settlor's wishes and the Trustees' powers under the Act - a difficulty arising when a TC is appointed as a trustee.

Annexure 9: The position in the States and Territories prior to CAFSMA

Exhibit 1 Investment returns for the 10 years to December 2011.



Source: Long Term Investing Report, June 2012 by Australian Stock Exchange (ASX) and Russell Investments

Australian Government

Corporations and Markets Advisory Committee

Administration of charitable trusts

Report

May 2013

Corporations and Markets **Advisory Committee**

Administration of charitable trusts

Report

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10 May 2013

The Hon. Bernie Ripoll MP
Parliamentary Secretary to the Treasurer
Parliament House
CANBERRA ACT 2600

Dear Mr Rippoll

I am pleased to present the report by CAMAC on the administration of charitable trusts managed by licensed trustee companies.

In responding to the matters raised in your request for advice, CAMAC puts forward recommendations that seek to ensure that the administrative arrangements for these charitable trusts continue to promote the benevolent and philanthropic objectives for which they were established.

Yours sincerely

Joanne Rees
Convenor

Contents

1 Introduction

This chapter provides background information on the reference, explains the review process, sets out the CAMAC approach, including in relation to the particular questions in the terms of reference, and summarises CAMAC's recommendations concerning this segment of the charities sector.

1.1 Overview

This report deals with administrative arrangements concerning one segment of the charities sector, namely charitable trusts managed by licensed trustee companies (LTCs). The terms of reference do not include charitable trusts administered by other persons, or other types of charitable entities.

The issues and conflicting points of view that have emerged during the course of this review are by no means new. Many have been articulated long before a national approach to the regulation of charitable trusts administered by LTCs was introduced in May 2010. These long-standing areas of contention have involved specific issues concerning the fees and tenure of LTCs acting as trustees of charitable trusts as well as more general matters related to the governance and accountability aspects of charitable trusts managed by LTCs.

One approach in the submissions to CAMAC during the review involved proposals for immediate and sometimes fundamental change to the regulation of charitable trusts operated by LTCs, on the basis that this is needed to ensure the focus remains on the public interest objectives of these trusts. The contrary perspective put forward in submissions was that LTCs (and their officers and employees) are already subject to a range of fiduciary duties and regulatory controls and that calls for change may be based on a misunderstanding of how LTCs manage charitable trusts pursuant to the intentions of the creators of those trusts.

CAMAC's starting point in considering these competing perspectives has been to ask why donors set up charitable trusts in the first place. It considers that the primary intent of each donor is to achieve the philanthropic or benevolent purposes or objectives for which the donor established and funded the charitable trust, within the time frame of the trust, and in an effective and efficient manner. This primary intent should be the policy cornerstone which underpins the regulation of charitable trusts generally.

From this policy standpoint, administrative arrangements for operating a charitable trust, whether sought or agreed to by the donor of the trust, should be assessed according to the extent to which they advance or promote the primary intent of the donor. Administrative arrangements are a means to this end, not ends in themselves.

For the purpose of ensuring that the legislative regime for administering charitable trusts promotes the primary intent of the donor, CAMAC proposes a two-stage reform process.

Stage 1 essentially comprises three measures:

- the conducting of Stewardship audits of a cross-section of charitable trusts administered by LTCs, to address the present deficit of relevant and indisputable information on the state of administration of charitable trusts

- the introduction of a 'fair and reasonable' requirement for all fees and costs charged against a charitable trust

- changes to the judicial dispute resolution procedures to enhance access to the court and to broaden its remedial powers, including in regard to whether fees and costs charged against a charitable trust are excessive or whether an LTC should be replaced as the trustee of a charitable trust.

As well as responding to perceived difficulties or shortcomings in the current legal regime, these proposals are designed to promote a more open market by providing opportunities, where appropriate, to alter administrative arrangements in order to achieve the primary intent of the donor.

Stage 2 would build on the information gathered from the Stewardship audits and any preliminary indications from the enhanced judicial dispute resolution procedure. It would focus on what, if any, additional changes to the regulation of administrative arrangements for charitable trusts are required to promote the primary intent of the donor.

1.2 Terms of reference

By letter of 20 September 2012, the Parliamentary Secretary to the Treasurer, the Hon. Bernie Ripoll MP, requested CAMAC to consider various matters concerning fees, and replacement of trustees, for those charitable trusts that are administered by LTCs, as well as other issues that impact on the charitable purposes of trusts. CAMAC was asked to report to the Government in May 2013.

The terms of reference contain six questions for the consideration of CAMAC. The first four questions deal with various aspects of the fees charged by LTCs for administering charitable trusts. The fifth question deals with replacing the trustee of a charitable trust. The final question asks CAMAC to consider other issues that impact on the objectives of Part 5D of the Corporations Act or the charitable purposes of trusts. The full terms of reference are set out in the Appendix to this report.

1.3 Ambit of the review

The terms of reference focus on various administrative matters concerning charitable trusts administered by LTCs. The reference does not extend to administrative matters concerning other entities in the charities sector, which may take the form of public ancillary funds (PuAFs), private ancillary funds (PAFs),[1] not-for–profit companies or charitable trusts and foundations administered by unlicensed trustees, such as individual accountants and lawyers. It appears, for instance, that more than 1000 PAFs have been established in the last decade, of which 80% are managed by parties other than LTCs.[2] Also, Public Trust offices, being State and Territory government entities, are not within the ambit of this review.

What is common to all charitable entities, including charitable trusts administered by LTCs, is the requirement that they provide a public benefit to preserve a beneficial

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1 All PuAFs and PAFs are subject to specific Commonwealth reporting and other guidelines, in the form of regulations made under the *Taxation Administration Act 1953*. Many trusts and foundations are deductible gift recipients (DRGs), which must lodge information with the Australian Taxation Office.

2 This information on PAFs was provided by the Financial Services Council.

taxation status, for instance income tax exemptions for charities that receive income distributions from the charitable entity.

One consequence for the broader charities context in which this review has taken place is that, in some respects, CAMAC's proposals relating to charitable trusts administered by LTCs could have a broader application. CAMAC refers, for instance, to its proposals in chapter 5 of this report concerning an enhanced dispute resolution role for the court. Arguably, this enhanced procedure, if introduced, could be made applicable throughout the charities sector, not just for charitable trusts administered by LTCs.

This review also took place during the period in which the recently created Australian Charities and Not-for-profits Commission (ACNC) has been developing its regulatory role, including through governance standards and external conduct standards. Some aspects of this ongoing process, including the development of various disclosure or periodic reporting requirements pertaining to administrative functions, have a bearing on the matters discussed in this review. The CAMAC report has been prepared within this context but does not seek to cover transparency matters already under consideration by the ACNC. Also, other relevant disclosure issues for consideration by the ACNC, such as the level of information to be publicly available about the identity and nature of particular charitable entities, are not covered in this review.[3]

1.4 Background

LTCs are professional trustee companies that hold an Australian financial services licence issued by the Australian Securities and Investments Commission (ASIC).[4] LTCs manage a range of legal arrangements, including charitable trusts.

A charitable trust is established by an individual or entity (the donor, alternatively described as the settlor) donating assets under a deed of trust (when the donor is alive) or by will, for a charitable purpose or purposes. The trustee holds the donated assets in trust, and administers the trust, which includes managing its assets and making distributions to other entities or persons (donees), according to the philanthropic or benevolent objectives or purposes identified in the deed or will.

The concept of donees has sometimes been extended to persons, or classes of persons, eligible to receive distributions under the terms of the trust, even when no distribution to them has taken place. However, the terms of the trust may preclude any particular individual or entity claiming an entitlement to a distribution in the same manner as a named beneficiary under some other forms of trust.

The donor may choose one of a number of entities, not just an LTC, as the trustee or one of the trustees of the charitable trust. The terms of reference cover only those charitable trusts where an LTC is the sole trustee (sole trustee trusts) or is a co-trustee (co-trustee trusts).

For the purpose of this review, a distinction needs to be made between two types of charitable trust administered by LTCs:

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3 For instance, some donors may wish to avoid the identity or nature of a charitable entity being made public for various reasons, including to maintain the anonymity of the donor or to avoid undue numbers of requests being made by outside parties for funds from the trust.

4 See s 766A(1A).

- those sole trustee trusts and co-trustee trusts that were established before 6 May 2010. They are referred to in the legislation,[5] and in this report, as existing client charitable trusts

- those sole trustee trusts and co-trustee trusts that were established on or after 6 May 2010. They are referred to in the legislation,[6] and in this report, as new client charitable trusts.

Currently, there are eleven LTC corporate groups. Most LTCs are members of the Financial Services Council (FSC). All LTCs are regulated under Chapter 5D of the Corporations Act, which came into force in May 2010. Prior to that date, matters now within Chapter 5D came within the exclusive jurisdiction of the States and Territories. Chapter 5D was the outcome of an agreement reached by the Council of Australian Governments (COAG) in 2008 that the Commonwealth assume responsibility for the uniform regulation in Australia of LTCs, including their management of charitable trusts.

1.5 The review process

CAMAC invited written submissions from interested persons on any aspect of the matters set out in the terms of reference.

Responses on the policy questions raised in this review were received from:

- the Charitable Alliance, and a number of its members

- the Financial Services Council, and a number of its LTC members

- Philanthropy Australia

- RBS Morgans

- others.

CAMAC also conducted a Roundtable in Melbourne on 11 April 2013 which involved representatives from these respondents.

CAMAC was greatly assisted in its consideration of the issues related to the administration of charitable trusts by the information and views provided by respondents. The Committee expresses its thanks to all those who participated in this consultation process.

CAMAC also acknowledges, with appreciation, the work of the CAMAC charitable trusts sub-committee (Greg Vickery (chair), Rosey Batt, Damian Egan, David Gomez, Kate Hamilton (ASIC), Rachel Webber) on this review.

5 s 601TDG.
6 s 601TDA.

1.5.1 Submissions on trustee fees and replacement of trustees

The submissions on trustee fees and the replacement of trustees pointed to what appear to be some fundamental differences of view on these matters. These issues are not of recent origin.[7]

For instance, some respondents asserted that, in some instances, LTCs of existing client charitable trusts have relied on the 'letter of the law' to increase their fees in an unreasonable and unjustified manner over recent years. The relevant provision in the Corporations Act, s 601TDH, permits LTCs post-May 2010 to charge the fees that they 'could' have charged, not what they actually charged as at May 2010. These assertions of undue fee increases pursuant to s 601TDH were denied by LTCs, with supporting data.

Various respondents also asserted that the terms of some charitable trusts have, in effect, entrenched various LTCs, and this lack of ability to replace a trustee, other than in limited circumstances, has excluded the operation of market forces, with negative consequences for the services provided compared with the fees charged. These assertions were, in turn, challenged by LTCs, who pointed to the express terms of trust instruments to have the trust administered by the LTC, asserting that some of the calls for greater ability to replace an LTC as trustee of a charitable trust may be motivated by a desire to change the philanthropic or benevolent purposes or objectives of the trust, contrary to the intention of the donor.

As a result, respondents differed, sometimes sharply, in their proposals for policy change. For instance, LTCs expressed the view that the current arrangements regulating fees under Part 5D.3 are largely satisfactory, as also are the rights of trustees under relevant trust instruments to remain in that role and the role of the court in dispute resolution. Any change, it was submitted, should focus on removing fee caps for new client charitable trusts, to allow for competitive market forces on fees and servicing. Also, an investment management fee for implementing any chosen investment strategy should be allowed in relation to all investments, not just investments in common funds.

Other respondents proposed a range of measures to regulate fees charged by LTCs more closely and to facilitate the replacement of trustees, with differing types and degrees of regulatory intervention being proposed.

1.5.2 Submissions on other issues

Some respondents argued that issues concerning trustee fees and replacement of trustees are symptomatic of a broader range of unresolved stewardship and disclosure issues regarding the role of LTCs in the administration of charitable trusts. For instance, the issue was raised in this context as to whether greater external scrutiny or other regulatory initiatives are needed in regard to the administration of sole trustee trusts.

1.5.3 Constitutional powers

One respondent raised questions concerning the constitutional power and capacity of a national government in regard to various policy options raised in the course of this review.

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7 For instance, the article 'A game of give and take' in the *Business Review Weekly* 29 June-5 July 2006 refers to differences of view between trustees of charitable trusts and other interested parties, including descendents of donors, concerning fees charged and various other aspects of the administration of those trusts.

CAMAC seeks to make clear that matters concerning constitutional power and capacity are not within its expertise. The Committee has not sought to assess the proposals in submissions, or its own approach and recommendations, from this perspective.

1.6 Primary intent of the donor

Trust law has long recognised the importance of determining the settlor's/donor's intention in establishing a trust.[8] As summed up in one recent judicial observation:

> the polestar of trust or will interpretation is the settlor's intent.[9]

In determining a donor's intent, one approach put forward in submissions was to focus on the administrative arrangements stipulated or agreed to at the time that the charitable trust was created. The trust instrument might, for instance, expressly stipulate a particular entity to act as the trustee, either conditionally or unconditionally and either for a stipulated period or during the life of the trust. On this view, these statements of intent should continue to be respected. Accordingly, it was argued, there is no proper basis for, say, removing a trustee of a charitable trust appointed pursuant to the trust instrument where the trustee is administering the trust in accordance with the terms of the trust instrument, unless the trustee has abused its powers or breached its obligations.

CAMAC considers that while this approach may be employed in the context of private and commercial trusts generally, charitable trusts fall into a separate category, given their public benefit role, which calls for a different approach. CAMAC takes as its policy starting point the need to identify the purpose for which donors establish charitable trusts in the first place. It considers that the primary intent of each donor is to achieve the philanthropic or benevolent purposes or objectives[10] for which the donor established and funded the charitable trust, within the time frame of the trust, and in an effective and efficient manner. Administrative arrangements for operating a charitable trust should be assessed according to the extent to which they achieve the primary intent of the donor of the trust.

This policy approach would permit adjustments to the administrative arrangements of a charitable trust where they are called for in order to achieve the primary intent of the donor of that trust, even where those adjustments differed from the terms of the trust instrument. In this way, any impediments to the effective administration of charitable trusts, which in some cases may not arise or become apparent until many years after the creation of these trusts, and long after donors have had any capacity to influence the trust structure, can be overcome.

The various means by which adjustments to administrative arrangements for charitable trusts might be made in order to achieve the primary intent of the donor are discussed elsewhere in this report. In this context, for instance, proposed guidance to the court in construing and applying the primary intent of the donor is set out in Section 5.5.4 of this report.

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8 *McPhail v Doulton* [1970] 2 All ER 228, [1971] AC 424.

9 *Bryan v. Dethlefs* 959 So. 2d 314, 317 (Fla. Dist. Ct. App. 2007).

10 The court may be called upon to consider the 'spirit' of a charitable trust where its particular benevolent objectives can no longer be achieved: *The Trust Company (Australia) Limited as trustee of the Kyle Williams Home Trust v Attorney-General of New South Wales (No. 2)* [2012] NSWSC 1505.

1.7 Questions in the reference

The terms of reference asked CAMAC to advise the Government on a number of questions, as set out below.

> ***Question 1***
>
> the impact [of Chapter 5D of the Corporations Act] on the quantum of fees that are, or could be, charged to charitable trusts and/or foundations (trusts) by [LTCs] and the net funds available for trusts to distribute to not-for-profit organisations. In doing so, consideration should be given to what fee arrangements would be available if trusts were able to operate in an 'open' market

Quantum of fees

A number of respondents to the review described instances where, in their view, substantial trustee fee increases occurred following the introduction of Chapter 5D of the Corporations Act in May 2010, without any apparent independent justification for these increases. However, the FSC provided data that pointed to few fee increases since May 2010 for surveyed LTCs and explained that the increases were the residual effect of State and Territory provisions that applied prior to the introduction of Chapter 5D. What was beyond doubt, however, was the existence of widely differing views about whether the quantum of fees charged by some LTCs was reasonable or excessive.

CAMAC considers that it is not possible at this point to provide a precise answer in regard to the impact of Chapter 5D on the quantum of fees charged by LTCs. It considers that whether there is an appropriate link between the quantum of fees charged by LTCs and the services provided by them in managing charitable trusts cannot be determined without a much closer analysis of the way in which LTCs have administered, and are administering, charitable trusts. For this reason, and for other stated reasons, CAMAC recommends the conducting of Stewardship audits of charitable trusts managed by LTCs, to provide necessary foundational information, including whether trustees are providing value for the fees they receive.

This matter is further discussed in Chapter 2 of this report.

Funds available for distribution

CAMAC makes the preliminary observation that increases in the quantum of trustee fees may not necessarily result in reducing the trust funds available for distribution to not-for-profit organizations. It is not a simple equation that more fees means less distributable funds. It also depends upon the quality of the service provided by the trustee, including the extent to which the trustee has managed to increase the value of the trust assets overall, or has forestalled a decline in that value that otherwise may have taken place.

A number of respondents argued that the Chapter 5D provisions that link permissible trustee fees to a percentage of the trust assets are not consistent with a fee for service approach. In their view, this may lead to the possibility of unjustified fee increases that unduly reduce the trust assets available for distribution.

CAMAC considers that whether the fees charged have unduly reduced the trust funds available for distribution cannot be determined without a much closer analysis of what is occurring in practice by the undertaking of Stewardship audits of a cross-section of charitable trusts.

This matter is further discussed in Chapter 2 of this report.

Open market

New charitable arrangements

Persons who wish to commit their funds for benevolent or philanthropic purposes may do so in a number of ways. They may gift money outright to an existing charitable organization, either during their lifetime or under their will. Alternatively, they may establish an entity for particular charitable purposes, to commence during their lifetime or by operation of their will.

When persons decide to establish an entity for charitable purposes, they must make a number of key preliminary decisions, including:

- the legal structure to be adopted (such as a trust, a not-for-profit company, a PAF or a PuAF)
- the person(s) to administer the chosen legal structure (such as an LTC, a public trustee, an unlicensed trustee entity, an accountant, a lawyer, a financial adviser or some other individual[11])
- what, if any, provision to include for later adjustment to the administrative arrangements
- the fees, if any, for administering the chosen legal structure.

Persons wishing to commit their funds in this way would be assisted by having access to comprehensive information on the options available to them on each of these matters and the legal and financial consequences of these options. Greater awareness on the part of intending donors could encourage competition between possible service providers, thereby promoting a more open market in the charities sector. CAMAC suggests that the ACNC might consider ways to assist persons in obtaining access to this information.

The terms of reference are confined to where a person chooses the legal structure of a charitable trust, to be operated by an LTC. In the context of fees, an open market exists to the extent that an intending donor (or a representative with legal capacity) negotiates with a number of LTCs on possible fee arrangements for the provision of trustee services. Any agreement reached on fees is not affected by the fee caps in the legislation.[12] Therefore the LTC may negotiate with the donor a separate fee for any service required to be performed by the LTC in administering the trust.

Existing charitable trusts

One view in submissions was that while competition among possible service providers at the time of establishing a charitable trust is worthwhile and should be encouraged, once decisions have been made on administrative matters, the original wishes of the donor on these matters should continue to be respected, even where the trust is intended to operate for many years or in perpetuity.

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11 There is no requirement for an entity to hold an Australian financial services licence in order to act as a trustee. Traditional trustee services only constitute a financial service for the purposes of Chapter 7 of the Corporations Act when provided by a trustee company: s 766A(1A).

12 s 601TBB. This is reinforced by s 601TDB(2).

The contrary view in submissions was that this approach creates a closed and anti-competitive market, to the possible prejudice of the charitable objectives for which the trust was established. It was pointed out that administrative arrangements entered into many years ago will remain in place indefinitely, regardless of any significant change in circumstances concerning the trustee or the environment within which the trust operates.

CAMAC considers that while the express wishes of a donor on administrative arrangements for a charitable trust should be acknowledged, the circumstances that may have influenced the original decisions of the donor may have materially changed since that time. In this context, the wishes of the donor on administrative matters should be construed from the perspective of the primary intent of the donor (see further Section 1.6 of this report). The overriding consideration should be whether those administrative arrangements continue to promote that primary intent.

As well as responding to perceived difficulties or shortcomings in the current legal regime, CAMAC's proposals concerning fees, the tenure of trustees, and the role and powers of the court in regard to disputes concerning charitable trusts are designed to promote a more open market by providing opportunities, where appropriate, to alter administrative arrangements in order to achieve the primary intent of the donor.

These matters are further discussed in Chapters 3-5 of this report.

Question 2

the range of additional fees beyond those regulated under [Chapter 5D of the Corporations Act] that are, or could be, charged to trusts by LTCs

Chapter 5D regulates fees charged by LTCs for 'traditional trustee company services'[13] that consist of being the trustee or manager of a charitable trust[14] as well as various other stipulated fees and costs,[15] including through the imposition of various fee caps. It also covers disbursements in this regard.[16] The Chapter does not cover any other amounts that an LTC may seek to charge against the trust. Also, various activities, including where an LTC is acting as the responsible entity of a managed investment scheme, fall outside the concept of traditional trustee company services.[17]

The issue of the width of the concept of traditional trustee company services that consist of being the trustee or manager of a charitable trust (traditional services) has particularly arisen within the context of the extent to which various investment-related services do or do not come within that concept and, therefore, are or are not included in the legislative fee caps for charitable trusts.

As indicated elsewhere in this report (Section 3.1), the FSC has drawn a distinction between:

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13 s 601RAC(1)(a), (2)(a). Operating a common fund is also carrying on a traditional trustee service: s 601RAC(1)(d).

14 ss 601TDA, 601TDG.

15 These cover fees where trust assets are invested in a common fund (ss 601TDE, 601TDI) and some other fees, including for the provision of an account (s 601TBC) and for the preparation of taxation returns (ss 601TDF, 601TDJ).

16 s 601TBD.

17 s 601RAC(3)(a).

- *trusteeship services*, which the FSC considers to be within the concept of traditional services and which are therefore subject to the statutory fee caps, and

- *investment management services*, which the FSC considers to be outside the concept of traditional services and which are therefore not subject to the statutory fee caps.

A contrary view is that investment management of trust assets is inherent in the role of trusteeship, and therefore comes within the concept of traditional services.

CAMAC considers that the scope of the concept of traditional services, and what additional fees and costs beyond those services can reasonably be charged by an LTC, require further consideration.

As a first step, the proposed Stewardship audits (in addition to their other functions) could:

- examine what fee-charging practices are being adopted by the LTCs, including what particular services provided by LTCs they classify as either traditional services or other services, and to what extent LTCs adopt a uniform approach in this regard

- identify what services are outsourced and for what reasons, and whether the costing arrangements for these services can be justified

- determine whether there is a need for clarification of what services, in principle, should be covered by the concept of traditional services

- determine whether there are good grounds, in principle, for LTCs to charge a separate fee for various investment-related services.

Stewardship audits are further discussed in Chapter 2 of this report.

Question 3

the effectiveness of regulating 'new' fee arrangements between an LTC and a trust in the manner contained in Division 4, Subdivision A of Part 5D.3 [new client charitable trusts]

Many of the comments in response to Question 1, above, as they apply to new client charitable trusts, also apply to this Question.

For the reasons set out in Chapter 3 of this report, CAMAC recommends that a 'fair and reasonable' fee requirement apply, and that it act as a qualifier to the statutory fee caps, in the sense that the caps should be seen as fee maximums rather than statutory entitlements, and are not necessarily to be regarded as fair and reasonable in all instances.

CAMAC recommends that the 'fair and reasonable' requirement apply to all fees and costs charged against the trust, even those negotiated between the LTC and a donor or other person with authority to deal with the LTC on this matter. This extended application of the 'fair and reasonable' requirement to these agreements will also promote the primary intent of the donor that the trust achieve the philanthropic and benevolent purposes for which it was established. To this extent, the principles governing fees and other aspects of the administration of public interest charitable trusts should depart from those applicable to private and commercial arrangements.

CAMAC also considers that where disputes arise concerning fees for particular new charitable trusts, there should be an accessible and effective way to resolve them. For this

purpose, CAMAC proposes an enhanced judicial procedure for the consideration of disputes over alleged excessive fees charged by LTCs of these trusts. This matter is further discussed in Chapters 3 and 5 of this report.

Question 4

the effectiveness of grandfathering of 'existing' fee arrangements between an LTC and a trust under Division 4, Subdivision B of Part 5D.3 [existing client charitable trusts]

As an immediate measure, and consistently with the approach adopted in regard to Question 3, above, CAMAC recommends that in regard to 'grandfathered' fees for existing client charitable trusts:

- a 'fair and reasonable' requirement apply for all fees and other charges against the trust, acting as a qualifier on applicable fee caps
- there be an expansion of the jurisdiction of the court to deal with disputes alleging the charging of excessive fees.

From a longer-term perspective, however, CAMAC considers that the policy rationale behind the fee grandfathering provision (s 601TDH) may need to be reviewed. Consideration could be given, at Stage 2 or subsequently, to whether the provision is consistent with the move towards a national uniform approach to the regulation of charitable trusts administered by LTCs, and whether it should be replaced with a uniform fee regime based, say, on the fee provisions applicable to new client charitable trusts.

These matters are further discussed in Chapter 3 of this report.

Question 5

what the current position is with regard to the removal and replacement of a trustee of a charitable trust, whether this position is unsatisfactory from a consumer protection perspective and if so, what, if any, reforms are necessary to address this

By way of clarification, CAMAC considers that the reference in the question to a 'consumer protection perspective' refers, in a general sense, to the public interest philanthropic or benevolent purposes for which charitable trusts are established. CAMAC does not read this term as requiring the identification of a particular group or groups of persons and a consideration of the question purely from their perspective.

Under the current law, the regulator or the court may remove the trustee of a charitable trust, usually for some form of breach or maladministration. Otherwise, subject to any removal provision in a trust instrument, trustees of charitable trusts typically have a high level of security of tenure. For many long-term charitable trusts, this provides a level of guaranteed tenure and income for the trustees, to the point where they may construe their position as amounting to a proprietary right, with any attempt to displace them as trustee (beyond the current powers to do so) as involving a loss of their property amounting to a penalty.

CAMAC is of the view that in order to achieve the primary intent of the donor, there should be a process to permit the replacement of an LTC as the trustee of a particular charitable trust in appropriate circumstances, beyond those that currently apply. However, given the potential financial and reputational consequences for the affected LTC, that power of specific removal should be exercised only by a court. CAMAC has also proposed

guidance on how the court should construe and apply the primary intent of the donor in that context.

These matters are further discussed in Chapters 4 and 5 of this report.

Question 6

other issues that impact on the objectives of [Part 5D of the Corporations Act] or the charitable purposes of trusts

A number of respondents raised other issues that were seen to impact on the objectives of Part 5D of the Corporations Act or the charitable purposes of trusts.

CAMAC considers that some of these matters could be considered at Stage 2 of the proposed ongoing review process.

These matters are further outlined at Section 1.8, below.

1.8 CAMAC recommendations

CAMAC recommends that a two-stage approach be taken regarding the future regulation of this segment of the charities sector.

Stage 1 would involve initiatives in three areas, as outlined below, for early implementation.

Stage 2 would involve a consideration of other issues and policy alternatives, taking into account the outcome of the Stage 1 initiatives.

The overriding consideration in all matters at both Stages is to ensure that the regulatory regime for administering charitable trusts promotes the primary intent of the donor.

1.8.1 Stage 1

Information gathering

CAMAC recommends that the ACNC, or some other independent party or parties appointed by the ACNC, initiate Stewardship audits of a cross-section of charitable trusts administered by LTCs, with a particular, but not exclusive, focus on sole trustee trusts.

This initiative could be implemented without the need for legislation or the enactment of regulations.

This matter is further discussed in Chapter 2 of this report.

Fees

CAMAC recommends that the following amendments be made to Chapter 5D of the Corporations Act:

- adoption of a ‘fair and reasonable’ requirement for all fees and costs (including disbursements and other charges) charged against an existing or new client charitable trust, including for outsourced services, and including any fees that have been settled by agreement. This ‘fair and reasonable’ requirement should act as a qualifier on applicable statutory fee caps, which should remain as fee maximums. Each LTC

would be required to provide an annual statement to the designated regulator that the fees and costs charged against the trust are fair and reasonable (see further Section 3.5.3 of this report)

- expansion of the jurisdiction of the court in dealing with disputes alleging the charging of excessive fees, to cover all fees and costs charged against existing and new client charitable trusts, whether or not concerning the provision of traditional services and including any fees that have been settled by agreement (see further Section 3.5.4 of this report).

CAMAC also recommends the adoption of a standardised approach to the disclosure of services and fee schedules, to make it easier for intending donors to compare the fee regimes of different LTCs and to better understand the fees that would be charged by each if appointed as trustee. This enhanced disclosure regime might be introduced by the regulator or through an industry-based initiative (see further Section 3.4.3 of this report).

Dispute resolution

CAMAC recommends the introduction, by legislation, of an enhanced judicial procedure to resolve disputes concerning charitable trusts administered by LTCs.

The procedure proposed by CAMAC is designed to increase access to the court and to give it an enhanced power to determine matters concerning any aspect of the administration of a charitable trust, including, in addition to fee disputes, the tenure of the trustee of a particular trust, in accordance with the primary intent of the donor.

These matters are further discussed in Chapters 4 and 5 of this report (see particularly Section 4.3.3, while details of the proposed enhanced judicial dispute resolution procedure are set out in Section 5.5).

1.8.2 Stage 2

Depending upon the information obtained from the Stewardship audits, and any preliminary indications from the enhanced judicial dispute resolution process, consideration should be given to whether further regulatory or other initiatives are warranted.

CAMAC considers that, notwithstanding the concern with the current situation that has been expressed in some submissions, a clear case for a prescriptive alternative regulatory framework to that introduced in May 2010 in this segment of the charities sector has not yet been made out. As earlier stated, there is a deficit of relevant, indisputable and compelling information on the administration of a sufficient number of charitable trusts administered by LTCs.

This situation may change as information is gathered through the Stewardship audits. That information may point to the need for further remedial action. Alternatively, it may indicate that the administration of charitable trusts by LTCs is working satisfactorily, or that specific areas of concern can be appropriately resolved with little or no further regulatory intervention.

Set out below is a range of policy issues that have arisen in the current review and which could be further considered in Stage 2 in light of the outcome of the Stewardship audits.

The Stage 2 review could be conducted, or co-ordinated, by the ACNC in co-ordination with ASIC, or be undertaken by a designated external review body.

Traditional services

One key area for consideration in Stage 2 is whether, in light of the Stewardship audits, the statutory concept of traditional services needs clarification or reformulation, given that the capped fee regime in Chapter 5D of the Corporations Act applies only to these services (see further Sections 3.1 and 3.5.1 of this report).

In this context, consideration could also be given to whether there are good grounds, in principle, for permitting LTCs to charge an extra fee for various investment-related services (see further Section 3.4.2 of this report).

A related question concerns the possible unbundling of the various services in light of current practices and whether conflicts of interest have arisen or could arise (see further Section 3.4.7 of this report).

Outsourcing of services

A further related matter concerns what would be suitable fee and cost arrangements for services that are outsourced by an LTC, taking into account information from the Stewardship audits on outsourcing practices (see further Section 3.5.2 of this report).

Sole trustee trusts

Another key area for consideration in Stage 2 would be the state of administration of sole trustee trusts.

Differing views were expressed in submissions on the future of these trusts. For example, it was proposed in submissions that each trust henceforth have at least one independent non-paid trustee, whose role would be to monitor the administration of the trust by the LTC. It was also proposed that a prohibition be placed on the creation of new sole trustee trusts.[18] The contrary view in submissions was that the sole trustee structure performs an important role and should be retained. Intending donors may prefer appointing an LTC as a sole trustee, to ensure that the trust is administered only by an independent professional party (see further Section 2.3.1 of this report).

Based on the outcome of the Stewardship audits, it may be possible to say with some level of certainty whether some form of increased external oversight or other regulatory initiatives for these trusts is warranted.

Fee disclosure

The question of whether each LTC should be required to report to the ACNC on the quantum of fees and costs charged against each charitable trust it administers (or trusts above a certain threshold size) could be considered in light of information gathered in the Stewardship audits on the quantum of fees and costs that have been charged against trusts (see further Section 3.4.3 of this report).

Fee caps

Data obtained through the Stewardship audits on the services provided for the fees charged may also give some indication of whether adjustments should be made to the current statutory fee caps, such as abolishing the caps or, conversely, reducing them (see further Sections 3.4.1 and 3.4.6 of this report).

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[18] It was pointed out in submissions that a precedent in this regard is found in the structure for PAFs, which must have at least one independent director or trustee, known as the Responsible Person.

Other possible fee arrangements

The Stewardship audits may also provide useful information on which to assess the merits of other possible fee options raised in this review, such as a fee for service approach (see further Section 3.4.5) or periodic review of fees (see further Section 3.4.8).

Fee grandfathering

A further matter that could be considered at Stage 2, or subsequently, concerns the policy rationale for the fee 'grandfathering' provision for existing client charitable trusts.[19] CAMAC raises the question whether this approach to the determination of fees for these trusts should be replaced by, say, the same uniform fee regime as applies to new client charitable trusts (see further Section 3.4.4 of this report).

Tenure of trustees

The information gathered in the Stewardship audits might also be instructive in considering whether the current, in effect permanent, tenure system for various trustees (subject to a court order for the replacement of a trustee) should be changed to, say, a general spill/periodic tender system for trustee appointments (see further Section 4.3.2 of this report).

This assessment might best take place following a period to assess the effectiveness of the enhanced role of the court in regard to the replacement of particular trustees, if introduced (see further Sections 4.3.3 and 5.5 of this report).

Legal structures

A broader issue that may also arise in Stage 2, or subsequently, is whether there should be greater harmonization of the various legal structures within the charities sector generally, including charitable trusts, not-for-profit companies, PuAFs and PAFs, and, if so, how this might be achieved.

Whilst any move at this time to change the present legal structures would be clearly premature, and may prove to be unnecessary, the benevolent and philanthropic purposes for which charitable trusts are established should remain the paramount consideration. The legal form adopted should always be considered within the context of achieving those charitable objectives, for the benefit of the community.

1.9 Advisory Committee

The Advisory Committee is constituted under the *Australian Securities and Investments Commission Act 2001*. Its functions include, on its own initiative or when requested by the Minister, to provide advice to the Minister about corporations and financial services law and practice.

The members of the Advisory Committee are selected by the Minister, following consultation with the States and Territories, in their personal capacity on the basis of their knowledge of, or experience in, business, the administration of companies, financial markets, financial products and financial services, law, economics or accounting.

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[19] s 601TDH.

The members of CAMAC during the course of this review[20] were:

- Joanne Rees (Convenor)—Chief Executive Officer, Allygroup, Sydney
- David Gomez—Chief Financial Officer, Land Development Corporation, Darwin
- Jane McAloon—Group Company Secretary, BHP Billiton Limited, Melbourne
- Alice McCleary—Company Director, Adelaide
- Denise McComish—Partner, KPMG, Perth
- Marian Micalizzi—Chartered Accountant, Brisbane
- Michael Murray—Legal Director, Insolvency Practitioners Association, Sydney
- Geoffrey Nicoll—Co-Director, National Centre for Corporate Law and Policy Research, University of Canberra
- John Price—Commissioner, Australian Securities and Investments Commission (nominee of the ASIC Chairman)
- Ian Ramsay—Professor of Law, University of Melbourne
- Robert Seidler AM—Consultant, Ashurst Australia, Sydney
- Greg Vickery AM—Special Counsel, Norton Rose Australia, Brisbane.

The Executive comprises:

- John Kluver—Executive Director
- Vincent Jewell—Deputy Director
- Thaumani Parrino—Office Manager.

[20] Some changes to this CAMAC membership took effect from May 2013.

2 Stewardship audits

In this chapter, CAMAC recommends that the ACNC implement, or co-ordinate, Stewardship audits of a cross-section of charitable trusts administered by LTCs. The purpose of the audits would be to obtain information on how LTCs have performed their administrative responsibilities in the context of the philanthropic and benevolent purposes of these trusts.

2.1 Survey of LTCs

At the request of CAMAC, the FSC surveyed a number of its LTC members concerning the existing client charitable trusts and the new client charitable trusts that they administer.

2.1.1 Existing client charitable trusts

Of the approximately 1120 existing client charitable trusts referred to in replies to the survey:

- 90% were sole trustee trusts, with a total capitalisation of some $2 billion
- 10% were co-trustee trusts, with a total capitalisation of some $1.2 billion.

2.1.2 New client charitable trusts

Of the 90 new client charitable trusts referred to in replies to the survey:

- 95% were sole trustee trusts, with a total capitalisation of some $120 million
- 5% were co-trustee trusts, with a total capitalisation of some $40 million.

The FSC has also indicated that, in total, LTCs are the sole trustee or co-trustee of some 1500 charitable trusts, with a combined capitalisation of approximately $3.4 billion. The FSC estimates that the entire charitable trust sector is valued at around $7 billion. The FSC has further indicated that (excluding charitable trusts that are PAFs or PuAFs administered by LTCs) LTCs, on average, distribute annual trust income amounts equivalent to 4-6% of the total capital value of the charitable trusts that they administer.

2.2 Analysis of the survey

Based on the above information, and assuming the same general trend for charitable trusts administered by LTCs not covered in the survey, it is clear that the overwhelming majority of charitable trusts administered by LTCs are sole trustee trusts. These trusts, collectively, hold the bulk of the combined capital of charitable trusts administered by LTCs, though the average capitalisation of co-trustee trusts administered by LTCs is considerably higher than for sole trustee trusts.

It was pointed out in submissions that often the express wish of a donor is for a sole trustee arrangement, sometimes to ensure that control of the charitable trust remains in the hands of a fully independent party.

The total capitalisation of all charitable trusts administered by LTCs is small, compared with that of listed companies, the superannuation sector, or managed investment schemes. However, their proper regulation is important in the public interest, given the philanthropic or benevolent purposes for which they have been established.

2.3 Need for further information

Apart from some overall statistics,[21] it is difficult at this point in time to determine what is happening generally with the administration of charitable trusts. Greater transparency as to industry practice generally is needed.

2.3.1 Sole trustee trusts

There is a deficit of readily available information on the quality of administration of sole trustee trusts, including the relationship between the fees charged by particular LTCs and the service provided to the trust. Also, the older the sole trustee trust, the less likely it is to have descendants of the donor or other interested persons to inquire how the trust funds have been managed and whether distributions have been made in the manner envisaged by the donor.

LTCs of sole trustee trusts would be well aware of the fiduciary context in which they operate and the obligations this entails in operating the trust. For instance, LTCs are required to adhere to a 'prudent person' principle in investing trust funds as part of their fiduciary duty to a charitable trust.[22] Equally, however, with no co-trustee to act as a monitor, and with security of tenure as the trustee, there may be a concern, accurate or otherwise, that administrative complacency may develop, with little or no external pressure on a trustee of a particular trust to achieve the benevolent purposes of the trust efficiently and effectively. This issue may be exacerbated where there is no group of actual or potential donees with an interest in monitoring the affairs of a particular trust, or the level or type of distributions from that trust.

2.3.2 Co-trustee trusts

Similar issues to those discussed above may arise with the administration of charitable trusts where LTCs are co-trustees. This may particularly be the case where a co-trustee lacks the ability or inclination to monitor the performance of the LTC or unresolved disputes remain between a co-trustee and an LTC regarding the administration of a particular charitable trust.

2.4 CAMAC proposal

CAMAC is of the view that a productive way to gain a better understanding of what is occurring in practice with the administration of charitable trusts operated by LTCs is through a structured review in the form of Stewardship audits. The purpose of these audits would be to focus on how each trustee has exercised its powers and assumed its responsibilities for the purpose of fulfilling the primary intent of the donor. These audits should be implemented as part of Stage 1 (see Section 1.8.1 of this report).

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21 In addition to Section 2.1, see also Section 3.2 of this report, which contains some overall statistics concerning fees, which were obtained through a survey of FSC members.

22 See, for instance, *Australian Securities Commission v AS Nominees Limited, Ample Funds Limited, AS Securities Pty Limited and Peter Grenfell Windsor* [1995] FCA 1663.

The Stewardship audits would consider the history and current administration by LTCs of a cross-section of charitable trusts, focusing on such matters as:

- the level, and type, of active administration employed, including the history of investments and distributions and investment management practices
- the relationship between the trustees of co-trustee trusts, including how any disputes between them have been resolved
- how the concept of traditional services has been interpreted and applied in practice, in particular the range of activities that LTCs consider come within/outside the scope of that concept
- the types and quantum of fees and other costs charged against the trust, including what fees and costs LTCs treat as coming within/outside the concept of traditional services (and therefore as coming within/outside those regulated under Part 5D.3 of the Corporations Act)[23]
- the method of valuation of the assets of the trust (for fee and other purposes) and the extent of involvement of any independent external party in that valuation exercise
- the nature of any investment-related services in operating the trust (beyond investments in common funds) and the costing arrangements for those services
- what services are outsourced, for what reasons, and the costing arrangements for these services
- the extent to which the trust has received identifiable value for the various fees and costs charged against the trust
- the nature and extent of any conflicts of interest that have arisen in the administration of charitable trusts
- the extent to which the benevolent and philanthropic objectives of the trust have been achieved, including the implementation strategies that have been employed.

The views of donees on relevant matters should also be sought, where appropriate.

Such a review would go well beyond the type of information required under the disclosure and reporting requirements of the ACNC Act, such as annual information statements and annual financial reports (the contents of which are being developed).

CAMAC proposes that Stewardship audits be conducted or co-ordinated by the ACNC, with the trusts included for audit being selected by the ACNC or the party it appoints to conduct the audits. A sufficient representative sample of trusts managed by each LTC would need to be audited so that an overall assessment of this segment of the charities sector could reliably be reached.

It is anticipated that participation in Stewardship audits would be on a voluntary basis. Use by a regulator of investigative powers to conduct these audits would be inappropriate, as there is no suggestion of improper conduct. However, any failure by an LTC to fully

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[23] See also the CAMAC discussion under Question 2 in Section 1.7 and in Sections 3.4.2 and 3.4.3 of this report.

co-operate in the audit process may raise questions about the willingness of that LTC to account for the management of the charitable trusts that it administers. It may point to the need for greater external oversight in some respect.

CAMAC envisages Stewardship audits providing a controlled form of transparency. It would be a matter for the ACNC to determine what information gathered by the Stewardship audits should be published. However, CAMAC envisages that the most appropriate and useful information for public release would be overall assessments of the state of administration of this segment of the charities sector, not information concerning the administration of particular identified charitable trusts.

It could be argued that the time taken to conduct Stewardship audits may delay what some parties see as more pressing and urgent regulatory initiatives. However, these audits are required to gain a clear, balanced and accurate understanding of the way in which LTCs are presently administering charitable trusts. More broad-sweeping legislative or other reform, if needed, should not be driven by particular instances, without an appreciation of the extent to which, if at all, they point to more endemic and enduring problems.

Conversely, it could also be argued that, without some clear evidence of problematic conduct by LTCs, the conducting of Stewardship audits constitutes an unjustified intrusion into the affairs of LTCs, with their commercial reputations being unfairly placed at risk. However, the purpose of the Stewardship audits is to move beyond the present environment, with its elements of conjecture, assertion, and allegation by various interest groups, to a more fully informed understanding of what is happening in practice and the level of alignment of administrative practice with the public interest, benevolent and philanthropic objectives of charitable trusts.

3 Trustee fees

This chapter reviews a range of alternative approaches to the regulation of trustee fees suggested in submissions and outlines CAMAC's proposals, including that fees and costs charged against a charitable trust be subject to a requirement that they be fair and reasonable, with an extended power of the court to deal with disputes alleging the charging of excessive fees or costs.

3.1 Services in administering a charitable trust

As earlier indicated,[24] Chapter 5D of the Corporations Act regulates fees charged by LTCs for traditional services (as well as various other stipulated fees and costs). It also covers disbursements in this regard.[25] Chapter 5D does not cover any other amounts that an LTC may seek to charge against the trust.

What is involved in managing a charitable trust is not fully clear. For instance, one area of contention concerns the status of investment management services.

On one view, managing a charitable trust necessarily involves managing the capital and other assets of the trust. The process of asset management would include making investment decisions concerning those assets, which, in turn, may require the obtaining of investment advice. On that interpretation, matters related to investment-related services would come within the scope of traditional services, with fee arrangements for these services regulated by Part 5D.3 of the Corporations Act.

The FSC has indicated that its LTC members adopt a different approach. They divide the charitable trust services that they provide into two categories:

- *trusteeship services*, which they consider to be within the concept of traditional services
- *investment management services*, which they consider to be outside the concept of traditional services.[26]

In consequence, according to the FSC, the costs of providing investment management services, and other services provided by a related or third party, such as direct property

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24 See the discussion under Question 2 in Section 1.7 of this report.

25 s 601TBD.

26 The FSC states that investment management services include:
- advice on formulation, implementation and monitoring of investment strategies
- development of investment proposals and recommendations where applicable
- provision of investment research
- customised performance reporting
- advice on corporate actions and implementation thereof
- preparation of customised investment research based on periodically updating current capital market assumptions
- preparation of regular asset allocation and portfolio reviews and reports thereon
- preparation of investment proposals in line with approved investment strategy
- research into investment proposals put forward by co-trustees, advisory boards and donees
- management of pooled investment vehicles
- provision of specialist advice on the management of direct property and other non-listed asset management.

management services, are not subject to the statutory caps in Part 5D.3 and can be recouped by the LTC as an expense of the trust.

CAMAC considers that there is a pressing need for clarification of what trustee services are/are not covered by the concept of traditional services and therefore are/are not regulated by the fee provisions in Part 5D.3 of the Corporations Act. The CAMAC approach in this regard is discussed in Section 3.5.1 of this report.

There is also the related question of what services can properly be outsourced, and what constitute suitable costing arrangements where outsourcing occurs. The CAMAC approach in this regard is discussed in Section 3.5.2 of this report.

3.2 Fees for traditional services

3.2.1 Existing client charitable trusts

Fees for existing client charitable trusts, which may have been agreed to many years ago at the time of creation of the trust, can be subsequently amended by agreement.[27] In practice, it is unlikely that this will occur often, given the requirement that there be 'a person or persons who have authority to deal with the trustee company on matters relating to the provision of the service'.[28] In many cases, particularly with long-standing charitable trusts, there may no longer be any person with this capacity.

Pursuant to s 601TDH (the 'grandfathering' fee provision), LTCs may charge the fees that they 'could have charged', not necessarily what they actually charged, as at May 2010 for traditional services. This is clear from the wording of the provision, notwithstanding that the section is headed: 'Trustee company not to charge more than was being charged before section commenced'.

In determining the effect of s 601TDH, it is necessary to take into account that the provision relates back to fees that were permitted under differing State and Territory legislation prior to May 2010.

Originally, trustees received an income commission under State and Territory trustee legislation enacted in the early 20th Century. Subsequently WA, ACT, VIC and SA amended their legislation to allow either deregulated fees (WA and ACT) or fees based on capital. NSW, QLD and TAS did not change their income commission provisions.

Given this, when s 601TDH came into force in May 2010, the relevant legislation in NSW, QLD and TAS prescribed an income commission amount, not a capital linked cap. The FSC has stated that LTCs in those States were charging the full income commission and in line with s 601TDH continued to charge the same commission amount after May 2010. The FSC has also stated that it is only in regard to LTCs operating in VIC, SA, WA and ACT (relevant LTCs) that the fee that **was** being charged may be different to what **could** have been charged. Also, according to the FSC, this is because fees in these States and the ACT were either capped or uncapped. Hence, an LTC could have charged an amount equivalent to the cap but might have been charging less than the cap.

The survey of a number of LTC members of the FSC indicated that in regard to relevant LTCs, there were 9 instances where the total dollar quantum of fees charged by an LTC

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27 s 601TBB. Subsection (1) provides that nothing in Part 5D.3 prevents its application.
28 s 601TBB(2).

against the trust increased at any time subsequent to the coming into force of s 601TDH. The FSC pointed out that this represents 0.8% of the total number of charitable trusts in the survey.

The FSC has stated that these increases were thus due to the left-over effect of prior State legislation, grandfathered by s 601TDH (its emphasis included):

> Section 21A of the Victorian Trustee Companies Act 1984 [introduced in 2006] (and the equivalent SA provision, s 10(2)(a)) introduced an annual capped commission based on the capital value of the trust [1.065%]. Before section 21A and s 10(2)(a), commissions were prescribed in those jurisdictions as a percentage of income. Naturally, switching from a commission that is based on a percentage of income (small amount) to a commission that is based on a percentage of capital (larger amount) will result in an overall higher percentage change. This is because the change in the multiple value is significant (change from income value to capital value). In other words, many Victorian and South Australian trusts that moved from income commission to section 21A or s 10(2)(a) capital commission (regardless of when they were moved) could have experienced fee increases of up to 200%.
>
> The only incidence of any fee increase after [the coming into force of s 601TDH] is a result of an organisation wide audit that identified a handful of trusts that did not move across to section 21A, s 10(2)(a) or published rate fees when all of the company's other trusts moved across. This was due to an administrative oversight and nothing to do with [the coming into force of s 601TDH] albeit the actual increase occurred post May 2010.

The FSC has also indicated that, on average, the LTC members of the FSC charge annual trustee fees for existing client charitable trusts that equate to 0.5% of the combined capital value of the trusts they administer.

3.2.2 New client charitable trusts

Trustees of new client charitable trusts, in regard to the provision of traditional services, may choose between:

- agreement between the parties,[29] or
- a capital commission and income commission formula,[30] or
- an annual management fee, at a rate not exceeding 1.056% (GST inclusive) of the gross value of the charitable trust's assets.[31] This fee may only be drawn from the income of the trust unless approval from ASIC to pay it from capital has been granted.[32]

In regard to fee arrangements for trusts coming within the survey of LTC members of the FSC:

- 75% of those trusts had fees determined by agreement between the parties
- 0% of those trusts had fees determined by a capital commission and income commission formula

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29 s 601TBB.
30 s 601TDC.
31 s 601TDD.
32 s 601TBE(3).

- 25% of those trusts had fees determined by an annual management fee.

3.2.3 Application of the statutory caps

The fee caps in Part 5D.3 of the Corporations Act for the provision of traditional services are maximum amounts. LTCs may charge less than an applicable cap. Likewise, an LTC might choose to, say, offer a fee for service arrangement within a cap as a way of showing the value it has provided to the trust for the remuneration it receives.

The FSC has indicated that, on average, its LTC members charge annual management fees for new client charitable trusts that equate to 0.8 - 1% of the combined capital value of the trusts they administer, compared with the 1.056% cap on such fees.[33]

3.3 Judicial review of alleged excessive fees

The court has been given an express legislative power in s 601TEA to hear disputes alleging the charging of excessive fees by an LTC.[34] The relevant provision applies to 'fees charged by a licensed trustee company in respect of any estate',[35] which includes fees charged for 'acting as a trustee of any kind, or otherwise administering or managing a trust'.[36] It therefore covers fees for the provision of traditional services.

The legislation provides that the fee review power of the court does not apply to:

- fees agreed between the parties, or
- fees for new client charitable trusts that are charged as permitted under the legislation.[37]

The effect of this provision is that the judicial review power does not apply to fees charged to administer new client charitable trusts.

While the provision does apply to fees for the provision of traditional services for an existing client charitable trust, there are a number of uncertainties that arise as to its scope, including:

- in what circumstances does the exemption for fees agreed between the parties[38] apply in this context, that is, whether fees reached pursuant to an agreement between an LTC and a donor many years ago constitute fees agreed under this provision.[39] The absence of any temporal limitation in the fee agreement provision (for instance, an express statement that the provision only applies to post May 2010 fee agreements) leaves open the possibility of this very wide interpretation. The courts have yet to consider this matter

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33 s 601TDD(1).
34 The court can also review these fees on its own motion: s 601TEA(4).
35 s 601TEA(1).
36 The definition in s 601RAA of 'licensed trustee company' is based on the trustee company holding a licence that covers 'the provision of one or more traditional trustee company services'. 'Traditional trustee company services' includes 'performing estate management functions' (s 601RAC(1)(a)). 'Acting as a trustee of any kind, or otherwise administering or managing a trust' is an estate management function (definition of 'estate management functions' in s 601RAA, s 601RAC(2)(a)).
37 s 601TEA(2).
38 s 601TBB.
39 s 601TBB(2)(a).

- even if the judicial review provision does apply to particular fee arrangements for existing client charitable trusts, an application for review of fees can only be made under the provision by or on behalf of a person with a 'proper interest' in the trust.[40] A person with a proper interest is defined to include ASIC, the donor, anyone with a capacity to remove a trustee, and 'a person or a class that the trust is intended to benefit'.[41] There is no express reference to co-trustees in this definition, leaving open what rights, if any, they may have under this provision. Further, the width of the concept of 'a person or a class that the trust is intended to benefit' remains uncertain. The courts have yet to consider this matter.

Where the judicial review provision does operate, and a lawful application is made or the court acts on its own motion,[42] the court may take a number of non-exhaustive factors into account in determining whether fees charged by an LTC to administer a trust are excessive.[43]

The court also has particular powers in regard to costs.[44]

3.4 Submissions

A range of approaches was put forward in submissions, either to deregulate trustee fees or to further regulate them in various ways.

In responding to each of these proposals, CAMAC has indicated the degree to which it sees merit in the general policy direction of each proposal. CAMAC notes, however, that some of these proposals, particularly in regard to increased regulation of fees, are, in effect, alternative approaches that could not operate simultaneously.

The policy approaches that CAMAC considers should be implemented as a matter of priority in Stage 1 are discussed in Section 3.5 of this report.

3.4.1 Abolition of fee caps

Submissions

One view expressed by LTCs was that fee caps for new client charitable trusts[45] should be abolished, with fees for these trusts henceforth left to market forces as influenced by relevant industry standards. It was argued that fees in financial services generally are deregulated and that there are no capped fee arrangements comparable to those that apply to charitable trustee services.

CAMAC position

Abolition of the fee caps would permit the charging of fees in excess of the former caps. CAMAC is of the view that a compelling case has not been presented for any proposition that the existing fee caps are too low. However, the proposed Stewardship audits may provide useful information on this matter.

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40 s 601TEA(4).
41 s 601RAD(1)(a), (b).
42 s 601TEA(4).
43 s 601TEA(3).
44 s 601TEA(5), (6).
45 ss 601TDC(1), (4), 601TDD(1).

Market forces

CAMAC observes that the provision permitting parties to reach an agreement on fees[46] already provides scope for the operation of market forces. Also, an LTC that chooses, say, an annual management fee is not obliged to charge up to the cap of 1.056% of capital.[47] LTCs, and other potential trustees, could create a market at the time of creation of a charitable trust by competing on the management fees that they are prepared to charge under the cap, if appointed as trustee.

Fees in financial services

CAMAC considers that there is no direct analogy between fees charged to administer a charitable trust and fee arrangements in financial services in which an LTC may be involved.

CAMAC is of the view that the administration of charitable trusts should not be considered simply as another type of financial service. The public benefit objectives of a charitable trust are fundamentally different from the private gain objectives of financial products and services generally. The objectives of a charitable trust do not change simply because an LTC that is administering that trust is also licensed to be involved in profit-making enterprises in the financial services sector. That is, the identity of a particular trustee does not change the nature of a charitable trust.

The various matters concerning fee caps could be considered in Stage 2 (see Section 1.8.2 of this report).

3.4.2 Investment management fee

Submissions

One proposal was that the legislation specifically provide for a fee to cover investment management services in addition to those that involve a common fund, for which additional fees are already recognised in the legislation.[48] This fee (which might alternatively be described as an investment administration fee) would be in addition to trusteeship fees, and could be introduced, for example, by way of an additional amount for fair and reasonable investment management services, determined in accordance with ordinary market rates, as capped or agreed.

It was argued that this change would provide neutrality between the fee treatment of common fund investments and other kinds of investment and would ensure that LTCs could recoup the costs associated with various investment strategies and not just the costs associated with investment in a common fund.

Recognition of this additional fee, it was argued, would overcome any disincentive to invest beyond common funds. It was stated that if trustees are only able to recoup the cost of making investments into a common fund but not any other kind of investment, this carries an increased risk to the ultimate beneficiary that the trustee will prefer common fund investments over other types of investments.

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46 s 601TBB.
47 s 601TDD.
48 s 601TDE.

CAMAC position

CAMAC would be concerned if it emerged that a trustee was giving preference to the investment of trust funds in a common fund, rather than an apparently better alternative investment, because of additional fees it could receive from adopting the first option. Any such approach may be difficult to reconcile with the duty of a trustee to make investment decisions according to the 'prudent person' principle.

The issue of investment management fees is part of the broader question of what matters should come within the concept of traditional services, given that the capped fee regime in Chapter 5D of the Corporations Act applies only to these services. As discussed elsewhere in this report (Section 3.5.1), CAMAC proposes that this matter be included in the Stewardship audits, for further consideration in Stage 2 of the review, in light of information gathered in those audits.

3.4.3 Greater disclosure of fees

Each LTC must make publicly available its schedule of fees for the provision of traditional services,[49] and must disclose to the client any changes to the fees charged.[50] However, the current ACNC disclosure regime does not require LTCs to report the actual total quantum of fees they charge for administering each charitable trust.

Submissions

It was pointed out that an enhanced fee disclosure regime commenced in 2006 in the area of superannuation and managed investment schemes. It introduced standardised terminology and a fee disclosure template, which could be adopted in the present context.

CAMAC position

CAMAC supports a standardised approach to the description of the types of fees charged in the charitable trust sector, and how they are calculated. This would make it easier for intending donors to compare the fee regimes of different LTCs and to better understand the fees that would be charged by each if appointed as trustee.

In order to be meaningful, a standardised approach would need to clearly identify such matters as:

- the various services that are included
- the various categories of fees and costs for each of these services, and the fee/cost formula employed
- what effect outsourcing will have on the fees/costs chargeable by the trustee.

Consideration might also be given to a requirement that all LTC fee schedules for managing charitable trusts be disclosed on one designated website (in addition to the current disclosure obligation) using fee templates, thereby providing easily accessible, complete and comparative information at one location.

This enhanced disclosure regime might be introduced by the regulator or through an industry-based initiative.

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[49] s 601TAA.
[50] s 601TAB.

CAMAC is of the view, however, that while the disclosure of types of fees charged and fee schedules is important, it does not suffice, of itself, to ensure a satisfactory regulation of the actual quantum of fees charged by LTCs for services provided to charitable trusts.

CAMAC elsewhere proposes the introduction of a requirement that all fees and costs actually charged against the trust be fair and reasonable, and that the court have an extended jurisdiction to consider whether fees and costs are excessive (see Sections 3.5.3 and 3.5.4 of this report).

The further question of whether each LTC should be required to report to the ACNC on the quantum of fees and costs charged against each charitable trust it administers (or trusts above a certain threshold size) might best be considered in light of information on fees gathered in the proposed Stewardship audits. This matter could be further considered in Stage 2 (see Section 1.8.2 of this report).

3.4.4 The fee 'grandfathering' provision

The operation of s 601TDH, the fee 'grandfathering' provision for existing client charitable trusts, has been described in Section 3.2.1 of this report. According to the Explanatory Memorandum to the Bill that introduced the provision:

> 'Grandfathering' generally means that, when rules change, current participants remain unaffected and the new rules only apply to new participants.[51]

Submissions

Some submissions argued that s 601TDH should be amended to grandfather the quantum of fees that were actually being charged as at May 2010. The view was put that this change would bring the provision into line with the section heading, namely: 'Trustee company not to charge more than was being charged before section commenced'.

A contrary view was that s 601TDH should be retained in its current form, on the basis that LTCs are not charging fees to existing client charitable trusts that exceed the fees that they could have charged if Chapter 5D of the Corporations Act had not been introduced.

CAMAC position

CAMAC understands why some differences of view may have arisen as to the intent of s 601TDH. On the one hand, the heading of the Section refers to fees 'being charged' in May 2010. Also, the Explanatory Memorandum to the Bill that introduced the provision stated that 'grandfathering' of fees charged to existing client charitable trusts:

> means that those existing clients will continue to pay the same fees as they did before the new legislation [May 2010].[52]

On the other hand, the provision refers to fees that an LTC, as at May 2010, 'could have charged' in relation to traditional services, not necessarily the fees that they actually charged at that time, which may have been lower.

While aware that s 601TDH may have created conflicting expectations among affected parties, CAMAC is not convinced that any alternative formulation of the provision offered

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51 Explanatory Memorandum to the Corporations Legislation Amendment (Financial Services Modernisation) Bill 2009 paragraph 2.110.

52 Explanatory Memorandum to the Corporations Legislation Amendment (Financial Services Modernisation) Bill 2009 paragraph 2.66, Supplementary Explanatory Memorandum paragraph 2.69.

in submissions is clearly preferable. For instance, changing the wording from fees that an LTC 'could have charged' to, say, fees that an LTC 'actually charged' as at May 2010 (presumably with some inflation factor) could in some instances lead to anomalous results, such as fee 'windfalls' for the trust, depending upon what had been the arrangements as at May 2010.[53]

CAMAC, however, is also of the view that the policy approach behind s 601TDH may need to be reconsidered at some later stage. The section was introduced to preserve fee arrangements for existing charitable trusts with the movement from State and Territory to national regulation in May 2010. While that policy approach may have assisted in achieving the transition in May 2010, the permanent preservation of differential fee arrangements based on State/Territory legislation as it stood in May 2010 seems out of step with the notion of a uniform regulatory regime for charitable trusts under a national scheme.

CAMAC also takes into account that its recommendations in regard to fees, particularly a 'fair and reasonable' requirement (Section 3.5.3 of this report) and an enhanced jurisdiction of the court concerning alleged excessive fees (see Section 3.5.4 of this report), may result in less fee disparity over time, and therefore reduce the effect of differential fee arrangements based on State and Territory legislation.

Within that context, CAMAC considers that the principles underlying s 601TDH should be revisited, at Stage 2 or subsequently. If greater fee uniformity is considered necessary or desirable, one possible approach is to provide that henceforth the fee regime for existing client charitable trusts be more closely aligned with that for new client charitable trusts.

3.4.5 Fee for service approach

Submissions

Some respondents proposed a fee for service approach, whereby fees would be charged by an LTC having regard to the actual time and effort involved in servicing the trust, either by using a time-sheet system, or pursuant to a settled budgeted estimate of the time likely to be taken. This approach would be comparable to the fee charging arrangements typically adopted by lawyers and accountants.

A contrary position in submissions was that there are good reasons why LTCs do not offer a fee for service arrangement. For instance, it was argued that fees charged by LTCs include an intangible element of the risk and responsibility inherent in the role of a professional trustee. The element of risk and responsibility is not something that can be appropriately priced on an hourly rate. Further, fee for service providers do not assume this risk or responsibility, since they merely act in accordance with instructions from the trustee.

It was also argued that there is no solid evidence to show that a fee for service model is necessarily the cheapest means for the provision of trustee services, particularly at a time when best practice pricing in the legal profession is moving away from time-based charging.

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[53] The FSC has indicated that in May 2010 there were a number of trusts where the trustee, through administrative oversight, was, in effect, undercharging, compared with other trusts administered by that trustee: see Section 3.2.1 of this report.

CAMAC position

One of the intended purposes of a fee for service approach is to better align fees charged with work actually and properly done for the benefit of the trust.

To achieve this, it would be necessary to:

- settle an appropriate formula (for instance, $X per unit time of a particular category of work done)
- ensure that the fees charged reflect the actual time spent on behalf of the trust
- ensure that the fees charged reflect services performed for the actual benefit of the trust.

A suitable formula for determining fees would have to properly recompense the trustee, while also being in the best interests of the trust and having appropriate and workable monitoring mechanisms.

CAMAC notes that there is nothing to preclude an LTC, at any time, choosing to adopt a fee for service model, provided that the fees charged do not exceed any existing agreement on fees or relevant fee caps.

However, CAMAC has also taken into account the contention that mandating a fee for service system would require a fundamental restructuring of an LTC's business model, involving considerable cost.

On the basis of the above concerns raised in submissions, CAMAC is not convinced of the benefits to be gained from introducing a fee for service requirement. CAMAC notes, however, that voluntary adoption of this approach (within applicable statutory caps and any other agreed fee limits) may be one way for an LTC to indicate that the fees it charges are fair and reasonable in the particular circumstances of that trust (see further Section 3.5.3 of this report).

The matter of a fee for service approach could be further considered in Stage 2 (see Section 1.8.2 of this report).

3.4.6 Revise the fee caps

Submissions

Some respondents argued that the existing fee caps under Part 5D.3 are unduly generous, compared with comparable financial service sectors, including superannuation administration.

One approach was to reduce the caps. Another proposal was to introduce scaled fee caps, on the basis that present caps which permit a fee based on a flat percentage of capital[54] would not be sustainable in a competitive market, nor do they currently reflect a reasonable fee for service. On that view, the cap fee percentage should decrease as the size of the fund increases, given the economies of scale involved. These benefits of scale, it was argued, should be passed on to the charitable objectives of the trust.

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[54] A flat percentage of capital fee is permitted under ss 601TDC and 601TDD for new client charitable trusts.

A contrary contention, supported by an actuarial study commissioned by a respondent, was that fees charged by charitable trustees were only marginally higher (20 basis points) than those charged by superannuation funds.[55]

CAMAC position

Reduce the caps

CAMAC is not in a position at this point to make any determination whether the existing statutory fee caps are unduly high. It may be possible to reach a more informed view on this matter in light of the outcome of the proposed Stewardship audits.

In any event, it would also be necessary to ensure any reduction of existing fee caps did not unduly disadvantage LTCs, given the time and effort involved in discharging their trustee obligations.

Scaled fee caps

CAMAC is of the view that while the principle of a sliding fee scale has merit, its adoption would require the setting of appropriate scales. There is also the possibility that any sliding scale could be interpreted as an entitlement, on the basis that the scale itself is sufficient to guard against undue fee recovery.

CAMAC considers that the voluntary adoption of scaled fees, within applicable statutory caps and any other agreed fee limits, may be one way for an LTC itself to establish that its fees are fair and reasonable (see further Section 3.5.3 of this report).

The various matters concerning fee caps could be further considered in Stage 2 (see Section 1.8.2 of this report).

3.4.7 Unbundling of services

Submissions

One proposal was that the services now provided by an LTC should be 'unbundled', including by separating out the trustee role from the investment management role. It was argued that this would provide greater open market competition for the provision of each of these services, with greater potential for the objective comparison of fees charged against services promised and services delivered. The comment was also made that this approach would be a response to what, on one view, was the possibility of conflicted remuneration where, for instance, an LTC outsources investment-related activities to a related party provider.

A contrary perspective was that there should be no prohibition on a trustee offering a bundled product or service. The key reason for a donor choosing to appoint a particular LTC as the trustee of the charitable trust is the expertise and experience of that LTC in increasing funds under management.

It was also pointed out that a donor who wishes the investment management function to be separated from the trusteeship role may include a direction to this effect in the terms of the trust instrument itself.

It was also suggested that the disclosure regime could be enhanced by requiring all professional trustees to disclose information about the ability of a donor to elect to

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[55] Rice Warner Actuaries *Charitable Trustee Fees* (May 2013), commissioned by the FSC.

separate the trustee and investment management roles. It was further stated that where these roles are separated, the 'prudent person' duty of a trustee nevertheless dictates that the trustee remain responsible for the prudent investment of trust assets. The trustee cannot delegate its responsibilities in that regard and therefore continues to be responsible for the oversight of the investments and the making good of losses that may be incurred as a result of any breach of that duty. It was argued that it should always be at the trustee's discretion whether to accept trusteeship business that mandates appointment of a separate investment manager.

CAMAC position

CAMAC notes that the unbundling proposal seeks to ensure efficient pricing of fees for each aspect of the administration of a trust through market forces, as well as overcoming any perceived conflicts of interest.

However, CAMAC is not persuaded that LTCs are necessarily in positions of conflict where they perform the role of investment manager as well as trustee. On one view, investment management of trust assets is inherent in the role of trusteeship. Also, important issues remain concerning the potential liability of a trustee under any unbundling arrangement. More information on these matters may become available through the Stewardship audits, which in turn may assist any further consideration of the unbundling of service provision at Stage 2.

3.4.8 Periodic review of fees

Submissions

A further proposal in submissions was to the effect that there be a systematic and periodic review of fees to assess their fairness and competitiveness in the market.

For this purpose, the regulator or some other independent assessor would be required to review the fees charged by LTCs in administering charitable trusts (possibly with a threshold asset size test for relevant trusts) every five years or so, comparing the fees charged with those of other trusts of the same size and complexity. Under this approach, increases in fees would be by way of application to the regulator or assessor with supporting evidence to ensure that any increase was reasonable and justified according to the particular charitable trust.

It was also proposed that there be a requirement to disclose the reason for any increase in fees, with the information disclosed being freely available to allow for public scrutiny of the increase.

ACNC

The ACNC already has a role in this area. The ACNC has advised that under proposed Governance Standard 1, a charitable trust must (among other things) comply with its purposes and character as a not-for-profit entity. If a trustee of a charitable trust was receiving benefits that did not constitute genuine compensation for services provided to, or reasonable expenses incurred on behalf of, the trust, those excessive fees may constitute non-compliance with the governance standard and enliven the ACNC's enforcement powers. Depending upon the circumstances, the ACNC could exercise its power to issue a direction on the quantum of fees that could be charged, and any repayment of excessive fees. Alternatively, the ACNC could seek a court injunction to prevent the charging of excessive fees.

CAMAC position

CAMAC considers that the proposal in various submissions for periodic reviews of fees would go well beyond the current ACNC powers set out above. It would require a periodic review of all fees charged by LTCs for administering charitable trusts, at least those with capital assets above a stipulated threshold.

CAMAC has considerable reservations about the practicality of this proposal. It questions whether any regulator, for instance, should be asked to become this closely involved in reviewing the operation of each relevant charitable trust and in making decisions on fees on a trust-by-trust basis. It is of the view that this may go well beyond the usual functions of a regulator.

3.4.9 Power to replace the trustee

Submissions

It was suggested in some submissions that the ACNC, or some other non-judicial body, should have the power to replace a particular trustee where it considers that the fees or expenses charged by that trustee are excessive and that co-trustees should have standing to apply to that body for the exercise of this power. One particular proposal was that an independent trustee review board be established, with powers to examine fee issues and refer cases to the ACNC, which could then consider the use of its powers to suspend or remove particular trustees.

CAMAC position

CAMAC would be concerned if a regulator was given an express power to replace a particular trustee on the basis of its conclusion that the fees charged by that trustee were excessive.

Also, as the removal of a particular trustee on the basis of the fees it has charged may have significant financial, as well as reputational, implications for that entity, a right of appeal to a court from the decision of a regulator or other non-judicial body would be necessary.

CAMAC considers that a better and more direct approach is to enhance the powers of the court to review whether fees charged by a particular trustee are excessive, with additional provisions to improve access to the court. A regulator such as the ACNC would have a right of application to the court. This matter is further discussed in Section 3.5.4 and Chapter 5 of this report.

CAMAC also proposes an enhanced court role in the replacement of a trustee of a particular charitable trust, where this is called for in order to achieve the primary intent of the donor of that trust. In that context, the fees charged by an incumbent trustee could be a relevant factor. This matter is further discussed in Section 4.3.3 and Chapter 5 of this report.

3.5 CAMAC proposals

3.5.1 Scope of traditional services

As earlier indicated, Chapter 5D of the Corporations Act regulates fees charged by LTCs for traditional services (as well as various other stipulated fees and costs). It also covers disbursements in this regard.[56] The Chapter does not cover other amounts that an LTC may seek to charge against the trust.

CAMAC considers that more information is needed on how the concept of traditional services has been interpreted and applied in practice, in particular the range of activities that LTCs consider come within the concept, and whether some statutory clarification or elaboration is called for. For this purpose, CAMAC has proposed that this matter be included in the proposed Stewardship audits, and be reviewed in Stage 2 (see further Question 2 in Section 1.7, Stage 2 in Section 1.8.2 and Section 2.4 of this report).

3.5.2 Outsourcing of services

An LTC may be reimbursed for all disbursements properly made in the provision of traditional services.[57] Beyond that, no guidance is provided in the legislation in relation to what activities might properly be outsourced and the costing arrangements for outsourced services.

CAMAC considers that more information is needed on current outsourcing arrangements and charging practices concerning those arrangements. For this purpose, CAMAC has proposed that this matter be included in the proposed Stewardship audits, and be reviewed in Stage 2 (see further, Stage 2 in Section 1.8.2 and Section 2.4 of this report).

3.5.3 A 'fair and reasonable' requirement

The principle that fees and costs charged to administer a charitable trust must be fair and reasonable is in one way axiomatic. No respondent to the review disagreed with this as a general proposition, which also would be consistent with the primary intent of the donor.

The issue, however, is the means of implementation of this principle.

Possible approaches

One approach in submissions was to rely on the fiduciary duties applicable to LTCs in administering trusts, on the argument that these duties include an obligation to ensure the fees charged are fair and reasonable. It was also argued that there is no evidence that the fees actually charged by LTCs, and in accordance with relevant statutory caps, are not in fact fair and reasonable for the provision of trusteeship services.

Various other respondents argued for a more regulatory approach, either in legislation or by governance standards to be enforced by the regulator.

Preference for a legislative or regulatory approach

While recognising the fiduciary context within which LTCs operate, CAMAC nevertheless considers that a principle of such fundamental importance to the operation of

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56 s 601TBD.
57 s 601TBD.

charitable trusts should be expressly and specifically stated in legislation, or in the governance standards of a regulator, as a public benchmark. This outcome would also be consistent with ensuring that the primary intent of the donor in setting up a charitable trust is fulfilled, by ensuring that the fees and costs charged do not unduly inhibit the ability of the trust to achieve the philanthropic and benevolent purposes and objectives for which it was established.

Enshrining such a requirement in this way would provide a general and non-prescriptive approach to ensuring a properly balanced fee regime, while at the same time dealing with some of the issues identified in other proposals put forward in submissions. For instance, for the purpose of establishing that particular fees charged are fair and reasonable, a trustee may choose to adopt a fee for service approach, or charge scaled fees so that the trust benefits from any economies of scale involved.

A 'fair and reasonable' requirement for fees and costs should be implemented as part of Stage 1 (see Section 1.8.1 of this report).

Precedent

A reasonable fee requirement already applies to the preparation and lodgement of taxation returns by an LTC.[58] A fair fee concept also applies to the payment of certain fees to an LTC out of capital of the trust estate for the performance of estate management functions.[59]

A 'fair and reasonable' remuneration requirement is also found in the tax guidelines for public ancillary funds (PuAFs) and private ancillary funds (PAFs). It acts as a qualifier to the stipulated statutory caps. Under Guideline 43 (emphasis added):

> - The trustee is only permitted to pay **fair and reasonable remuneration** for the services of the trustee in administering the trust, at a rate **not exceeding** 1.056% annually (GST inclusive) of the gross value of the trust fund; and
>
> - the trustee is only entitled to be reimbursed for reasonable expenses incurred as trustee of the trust.

CAMAC considers that adoption in statutory form of the same principle for charitable trusts regulated under Chapter 5D of the Corporations Act would facilitate a degree of uniformity and harmonization in regard to fees within the various segments of the charities sector.

Elements of a fair and reasonable requirement

CAMAC considers that an LTC, as the party with overall responsibility for managing a charitable trust, should be under an obligation to ensure that all claims for payment against the trust, from whatever source, are fair and reasonable.

To achieve this, the terms of a legislative or regulatory requirement that all fees and costs involved in the administration of a charitable trust by an LTC be fair and reasonable (the standard) should make clear that:

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58 ss 601TDF, 601TDJ.
59 s 601TBE(4).

- the standard applies to all fees and costs charged against the charitable trust, including, but not confined to, fees charged by LTCs for traditional services. All charges arising from outsourced services would also be included

- the standard applies to fees agreed under s 601TBB

- the standard applies within relevant statutory fee caps, which would remain. Charging fees that are no more than the statutory fee caps does not necessarily satisfy the standard. In that respect, fee caps are maximums rather than a statutory entitlement, with the standard acting as a qualifier on those caps

- the factors set out in s 601TEA(3) (which the court takes into account when considering whether fees are excessive) are relevant in determining and applying the standard

- LTCs must turn their mind to all fees and costs charged against each of the charitable trusts that they administer through a periodic statement to the designated regulator that, in regard to each of those trusts, the fees and costs comply with the standard, with supporting reasons.

Some of these matters are further discussed below.

Caps are maximums, not automatic entitlements

CAMAC considers that mere compliance with the statutory caps under Part 5D.3 regarding fees for the provision of traditional services would not necessarily meet the standard, or necessarily encourage the best administrative practices to achieve the charitable objectives of the trust. CAMAC would be concerned with any approach that automatically deems fees that do not exceed an applicable statutory cap to be, ipso facto, fair and reasonable.

CAMAC considers that the standard should be treated as a qualifier on the existing statutory fee provisions in Part 5D.3. The standard should apply to all charitable trusts, whether existing or new client charitable trusts. It would reinforce the fact that the existing statutory caps are fee maximums, not necessarily fee entitlements for the provision of traditional services.

Agreements on fees

CAMAC has given consideration to whether the standard should apply where the parties themselves have agreed on the fee regime.[60] In this context, 75% of the fee arrangements for new client charitable trusts covered in the FSC survey were determined by agreement between the parties.[61]

The view was expressed in submissions that LTCs may compete over fees in seeking to build their client base and that this market mechanism, as reflected in fee agreements reached with donors, helps to ensure that fees are fair and reasonable.

CAMAC takes a different approach. It considers that entry into a charitable trust arrangement, which is intended for public benefit philanthropic purposes, should not be treated in the same manner as a private benefit or commercial transaction, where fees and

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60 s 601TBB.
61 See Section 3.2.2 of this report.

other matters are usually determined through a once-off negotiation process, with the obligation resting on each of the parties to obtain their own advice on these matters.

With charitable trusts, there should be a recognition that a financially/legally literate donor (or any other person with a legal capacity to deal with an LTC on fee matters[62]), even when independently advised, might still make decisions about fee arrangements, which, considered objectively (either at the outset or in light of changed circumstances), are not fair and reasonable in the shorter or longer term. The achievement of the benevolent or philanthropic purposes for which a charitable trust was established should not be forever compromised by a once-off poor fee decision of this nature.

For these reasons, CAMAC considers that even where fees are negotiated with the donor or a representative with legal capacity, the fee regime should remain subject to an overriding 'fair and reasonable' test.

Compliance

There should be a requirement that each LTC, in respect of each of the charitable trusts that it administers, provide an annual statement to the designated regulator that all the fees and costs charged against the trust are fair and reasonable, with an explanation by the LTC of the basis for that conclusion for each relevant trust, including supporting information. Merely stating, for instance, that fees charged are not in excess of statutory caps should not be considered a satisfactory explanation.

The annual statement by the LTC would include any amounts charged against the trust arising from outsourcing services or for any services that are not traditional services.

The factors set out in s 601TEA(3) would be relevant in determining a 'fair and reasonable' standard, and could be applied in the explanation accompanying the annual statement.

CAMAC considers that these annual compliance statements should be publicly available.

Implementation

A 'fair and reasonable' requirement and a compliance statement could be introduced by legislative amendment or by regulation under Chapter 5D of the Corporations Act, if possible. Either approach has the benefit of all the provisions concerning LTC fees for administering a charitable trust being in one location. Alternatively, they could be introduced through amendment to ACNC governance standards and financial reporting regulations.

CAMAC considers that regulatory or industry guidance should be provided on the elements to be taken into account in assessing whether fees are fair and reasonable. That guidance could point out that the standard does not necessarily constitute the imposition of a uniform or minimal fee requirement. In determining what is fair and reasonable, full consideration may be given to the tasks and responsibilities involved in administering the particular charitable trust, including the type and level of expertise required.

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62 s 601TBB(2)(a).

3.5.4 Expanding the jurisdiction of the court to deal with disputes alleging the charging of excessive fees

CAMAC notes that just as it is axiomatic that fees charged to administer a charitable trust must be fair and reasonable, it is axiomatic that fees and costs that are excessive cannot be fair and reasonable. Also, charging excessive fees and costs would be inconsistent with the primary intent of the donor.

As previously indicated, the court has a power under s 601TEA in some circumstances to review the fees charged by an LTC to determine whether they are excessive. However, there are significant limitations, and uncertainties, on the operation of this power, as outlined in Section 3.3 of this report.

CAMAC considers that to ensure the full effectiveness of s 601TEA, the provision should be amended to extend the jurisdiction of the court to all fees and costs charged against a charitable trust, from whatever source:

- whether in relation to an existing or new client charitable trust
- whether for the provision of traditional services or otherwise
- whether related to services provided by the LTC or outsourced services
- whether or not any of those fees and costs were agreed to by the donor or any other person with proper authority.[63]

CAMAC acknowledges that extending the jurisdiction of the court to negotiated fee agreements could lead to their re-opening. However, CAMAC restates its view that the achievement of the benevolent or philanthropic purposes for which a charitable trust was established should not be forever compromised by a fee agreement that turns out to be flawed from the perspective of achieving the primary intent of the donor.

The factors that the court may consider in determining whether fees are excessive are already set out in s 601TEA(3) and should be retained, with adjustments for the extended application of the provision to all fees and costs against the trust, from whatever source.

The proposed judicial dispute resolution procedure should apply to disputes alleging the charging of excessive fees. The procedures proposed in Section 5.5 of this report should be adopted in lieu of the current procedural aspects of s 601TEA.[64]

These amendments to s 601TEA should be implemented as part of Stage 1 (see Section 1.8.1 of this report).

63 s 601TEA(1)-(2) would need to be amended.
64 s 601TEA(4)-(6) would need to be amended.

4 Replacement of a trustee

In this chapter, CAMAC considers issues concerning the tenure of LTCs as trustees of charitable trusts and the possible procedures for replacing a trustee. CAMAC proposes an enhanced role for the court in replacing a trustee, where called for in order to achieve the primary intent of the donor.

4.1 Current position

A trustee of a charitable trust may be replaced by:

- the donor, if alive and with legal capacity to do so
- the terms of the trust instrument itself, for instance, where a person is given a power in the instrument to replace the trustee, or (very rarely) where the instrument itself makes provision for change, such as a periodic 'spill' of the trustee
- legislative process, such as where a trustee is no longer capable of acting in that role[65]
- a regulator in certain circumstances
- the court.

A trustee may also choose to retire, thereby necessitating the appointment of a new trustee.

4.1.1 Role of the regulator

Both the ACNC and ASIC have powers, within the context of their respective enabling legislation, to replace a trustee.

The ACNC may suspend or remove a trustee of a charitable trust for breach of the ACNC Act or its regulations, including governance standards and external conduct standards. The ACNC Act requires the ACNC to give consideration to a range of factors, including the nature, significance and persistence of any non-compliance, before exercising its suspension or removal powers. The exercise by the ACNC of its powers to suspend or remove a trustee is also subject to internal review and subsequent review by the Administrative Appeals Tribunal or a court.

LTCs must hold an Australian financial services licence, issued by ASIC. In various circumstances, ASIC may cancel the licence of an LTC, in which case it may transfer the estate assets and liabilities of the LTC to another LTC or in certain circumstances to a Public Trustee.[66] There are procedural requirements for cancellation of a licence, including that ASIC be satisfied that certain misconduct has taken place.[67]

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65 See, for instance, s 41 of the *Trustee Act 1958* (Vic).
66 See generally Part 5D.6, Div 2 of the Corporations Act.
67 s 915C of the Corporations Act.

4.1.2 Role of the court

A court of equity under its inherent powers, or pursuant to specific powers under State or Territory trustee legislation, may remove a trustee in various circumstances, including where the trustee has acted in breach of trust. The relevant principles are set out in Section 5.2.2 of this report.

4.2 Tenure of a trustee

In circumstances other than those set out in Section 4.1 above, a trustee, once lawfully appointed, remains in office for the period of the trust. It appears that most charitable trusts administered by LTCs have trustees with this form of extended tenure (sometimes described as permanent tenure, if the trust was established as a trust in perpetuity[68]).

4.2.1 Submissions

Support for continuing tenure

One perspective was that the current position provides certainty of administration, and is consistent with the intention of the donor. The donor of each trust that employs an LTC has specifically selected that entity as the trustee. Except in circumstances of misconduct, that LTC should have the right to continue as trustee pursuant to the stated terms of the trust instrument.

It was also argued that giving other parties, such as co-trustees or donees, some unilateral power to replace the trustee (except if so provided for in the trust instrument) would be contrary to the intention of the donor and would be at odds with trust law. It could also give those other parties undue influence, such as seeking to have the trust operate, or make distributions, in a manner contrary to the donor's original intention.

It was further argued that there is ample opportunity for open competition at the time a charitable trust is created concerning whom to appoint as the trustee of that trust. LTCs may compete for that role with each other, with individuals, and with unlicensed professional trustees. The FSC estimated, for instance, that LTCs are the trustees of less than 50% of all charitable trusts.

In this context, it was argued that for new charitable trusts, there could be an enhanced disclosure regime which would explain to donors, prior to creating the trust, that they could include specific powers within the trust instrument concerning the tenure of the trustee. Such a regime could, for example, mandate that professional trustees and solicitors specifically point to the permanency of appointing a professional trustee and advise the donor of the right to choose other options, such as including a provision granting another person or entity the power to replace the trustee in stated circumstances and/or periodically. It was noted that a similar disclosure regime has been implemented for enduring powers of attorney.

Proposals for change

Other respondents were critical of the current position which, in their view, inhibited any attempt at effective ongoing competition for the delivery of trustee services for charitable trusts. It was pointed out, for instance, that charitable trusts are often in the unique position that the individual who established the trust and appointed the LTC is no longer capable of

[68] Charitable trusts are not subject to the common law rule against perpetuities.

reviewing and, if thought appropriate, replacing the LTC. In effect, following the demise of the donor, the trusteeship defaults to a perpetual appointment.

It was also argued that some LTCs have changed fundamentally in their professional profile since they were designated the trustee in the trust instrument. This may particularly be the case with some older trustee companies which, through internal changes or external takeovers, may have become far removed in philosophy and business practice from what they were when chosen years ago by the donor. All that may remain, in effect, is the name of the LTC. Those LTCs, it was argued, may no longer be suitable for such a key role in the philanthropic sector, where non-commercial considerations should be given greater prominence.

Some respondents also pointed to other situations where provision is made for altering existing administrative arrangements, such as with managed investment schemes. Reference was also made to 'portability' rights given to various parties in superannuation and banking and other aspects of financial services provision.

4.2.2 CAMAC response

CAMAC makes the initial observation that the notion of trustee tenure, to the extent, say, that it is reliant on the terms of a trust document, is not a fully mutual arrangement. An LTC can retire as trustee of a particular trust, notwithstanding any statement of the donor in the trust instrument that the LTC remain in that role.

Analogy with managed investment schemes

CAMAC is of the view that it is not useful to try to draw any analogy between removing the trustee of a charitable trust and removing the responsible entity of a managed investment scheme. Unlike a charitable trust, a managed investment scheme has investors who, in that capacity, are entitled to determine who should continue to manage their funds on their behalf. There are no investors in a charitable trust, apart from the donor. It is thus unproductive to try to equate actual or potential donees of a charitable trust with scheme investors.

Analogy with concept of portability

CAMAC also considers that it is unproductive to bring into the discussion of replacing an LTC as trustee of a charitable trust the concept of 'portability' rights. This concept has been applied, for instance, to the right of superannuation contributors to change their superannuation fund, to the right of mortgagees to transfer their home loans and to certain other rights of retail consumers of financial services. There is no direct analogy between the position of these persons and co-trustees or donees of a charitable trust.

Current provisions contemplating the replacement of a trustee

It was argued in submissions that Part 5D.6 of the Corporations Act already permits the replacement of a trustee company without reference to the donor of the charitable trust, thereby constituting legislative recognition of limitations on the principle of trustee tenure.

For instance, Part 5D.6 regulates the particular situation where an incumbent LTC needs to be replaced in consequence of the cancellation of its Australian financial services licence. This Part also permits the transfer of the trust to a new trustee in certain circumstances.[69]

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[69] See ASIC Regulatory Guide 237 *Trustee companies: Transfer determinations by ASIC* (June 2012).

In addition, various State and Territory provisions contemplate circumstances where a trustee may need to be replaced.[70]

CAMAC considers that Part 5D.6 is clearly designed for particular circumstances which would not necessarily be in the contemplation of a donor and which are driven in part by the impetus towards uniform national regulation of LTCs, not in consequence of some underlying general principle concerning the tenure of a trustee.

Change of control within an LTC

CAMAC has considered the argument in submissions that since the shareholders of an LTC can agree to an internal change of shareholding control, such change, in effect, constitutes a change of trustee. Since May 2010, Ministerial approval is required for an acquisition of more than 15% of the voting power in an LTC.[71]

While CAMAC does not agree with this proposition on its face, it nevertheless considers that a change of internal control of a trustee is a relevant consideration for a court to take into account in reviewing whether it is appropriate for that LTC to be replaced (see further the Note to Principle (4) in Section 5.5.4 of this report).

Competitive market approach

CAMAC acknowledges that there may be a competitive open market to determine who will be appointed as the trustee of a particular charitable trust (and the terms of that appointment) at the time the trust is created.

However, CAMAC is concerned to ensure that any competitive process to select a trustee at the outset not also entrench that trustee, thereby foreclosing any competitive market influence for the remaining life of the trust. There needs to be some continuing capacity to adjust administrative arrangements, including by replacing a trustee of a particular charitable trust, where called for to achieve the primary intent of the donor of that trust.

Disclosure approach

CAMAC notes that the proposed disclosure approach, in referring to 'the permanency of appointing a professional trustee' except where the donor chooses a non-entrenchment option,[72] might be viewed by some as an indirect attempt to entrench a trustee in that role.

CAMAC does not support any form of trustee entrenchment for charitable trusts administered by LTCs, whether or not intended. As indicated above, there needs to be some continuing capacity to adjust administrative arrangements, including by replacing a trustee, where this is called for to achieve the primary intent of the donor.

4.2.3 CAMAC proposal

As with other aspects of the regulation of charitable trusts, CAMAC considers that the primary intent of the donor should be the policy cornerstone which underpins consideration of the tenure of trustees of these trusts.

In accordance with this principle, provision would need to be made for the possibility of replacing the trustee of a charitable trust in the interests of achieving its philanthropic and

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70 See, for instance, s 41 of the *Trustee Act 1958* (Vic).
71 See Part 5D.5 of the Corporations Act.
72 See the fourth paragraph under *Support for continuing tenure* in Section 4.2.1 of this report.

benevolent purposes and objectives, even where this replacement overrides the express wishes of the donor in the trust instrument and in circumstances where the incumbent trustee has not breached any applicable law or regulatory requirement.

Furthermore, these circumstances may arise even where the particular arrangements concerning the nomination and tenure of a trustee were originally entered into by a fully informed and properly advised donor.

CAMAC proposes in Section 4.3.3 of this report that the court have the power to replace a trustee, to be exercised in the context of achieving the primary intent of the donor.

4.3 Procedure for replacing a trustee

4.3.1 Submissions

Some proposals centred on giving a regulator, or some other independent person, a range of review and replacement powers over trustee appointments. It was argued that these procedures were necessary to stimulate greater competitive market forces in the administration of charitable trusts.

A further suggested procedure was the adoption of some form of mandatory periodic review of trustees, combined with a tendering process for the role of trustee of a charitable trust (above a threshold capital size).

Proponents of these initiatives argued that introduction of a more competitive open market for trustee services would be consistent with principles of transparency and accountability of trustee conduct, while at the same time improving consumer protection by requiring LTCs to continue to provide high quality and cost effective services to charitable trusts or otherwise risk losing their tenure.

4.3.2 CAMAC response

Role of the regulator

As earlier indicated, both the ACNC and ASIC may remove a trustee for various forms of regulatory breach.

Neither regulator has the power to remove an LTC in other ‘non-fault’ circumstances where there is no evidence of a regulatory breach or other misconduct by the LTC, but rather, say, where there is irreconcilable disputation between an LTC and a co-trustee, or between an LTC and donees.

CAMAC has earlier expressed its reservations about calling upon a regulator to make decisions about the trusteeship of a particular charitable trust in such ‘non-fault’ circumstances. Such a power and responsibility would go well beyond the usual administrative role of such a body (see Section 3.4.9 of this report).

If such a procedure were to be contemplated, CAMAC considers that, given the potential financial and reputational consequences for the affected LTC, a right of appeal to a court from any decision of the regulator to remove that entity as a trustee of a particular charitable trust would be required as a matter of fairness.

Independent person

CAMAC has the same reservations regarding any procedure whereby some other designated independent person or persons, such as a specialist independent trustee review board, would have the power to decide from time to time matters concerning who should manage a particular charitable trust.

Spill and tender

Various submissions proposed a procedure involving a general spill of existing trustees of all charitable trusts (or those trusts with capital in excess of a minimum threshold), followed by an ongoing periodic tendering process for trustee services of those trusts.

While the intended purpose of a general spill/tender procedure may be to bring more competitive market forces into play in the administration of charitable trusts, CAMAC has concerns about its workability and possible detrimental consequences to trusts, including the diversion of trust funds in meeting the substantial costs that may be involved in any properly conducted spill and tender process. Also, such an approach could generate ongoing uncertainty and unnecessarily destabilise those trustees who are seeking to fully advance the interests of the trusts they administer. Further, a spill and tender process may result in important knowledge and expertise concerning the administration of particular trusts being lost.

The question also arises of how determinations under the spill/tender process should be made and whether there should be some form of regulatory guidance or oversight in this regard.

Taking all these matters into account, CAMAC considers that the case for an immediate move to a general spill/tender procedure for trustee services has not been sufficiently made out at this time, nor have all the necessary elements of any such procedure been identified.

In the event that the Stewardship audits indicate that, overall, the primary intent of donors is being materially compromised by the current trustee tenure arrangements, then the general spill/tender proposal for trustee appointments could be revisited. In those circumstances, however, close consideration would need to be given to the tendering regime, including how tenders are to be assessed, as well as the appropriate duration of contract periods for the administration of charitable trusts.

4.3.3 CAMAC proposal

Having considered the competing proposals, CAMAC is of the view that the power to replace a particular LTC as trustee of a particular trust (over and above the powers already given to the regulators) should reside in the court, not in a non-judicial body, given the potential reputational as well as financial damage to that entity from being removed as trustee.

This situation differs from any general spill and tender process that might be introduced, which would apply to the trustees of all charitable trusts (or those above a particular capital threshold) and which, therefore, would not be directed at the trustee of a particular trust. All trustees would be equally affected by the change in tenure arrangements under a spill and tender approach.

CAMAC is further of the view that the court should be given a general power to replace a trustee of a particular trust in circumstances other than breach, where this is called for in order to achieve the primary intent of the donor of that trust (see further Section 5.5 of this

report, which sets out proposed guidance to the court on this matter). This should be implemented as part of Stage 1 (see Section 1.8.1 of this report).

CAMAC observes that giving the court a power to replace a trustee of a particular trust does not mean that this power should be employed without due consideration of the possible consequences for the trust. The court may need to take into account, for instance, that the trusteeship of a particular charitable trust may be much more than merely a series of administrative tasks. It may require skilled judgement and particular expertise in managing substantial assets over a long period. The skills and experience of both the current trustee and any proposed replacement trustee would need to be closely assessed in this regard.

5 Dispute resolution

This chapter sets out proposals by CAMAC for an enhanced judicial process for the resolution of disputes over the administration of charitable trusts.

5.1 Context

During the course of this review, it became clear that, in addition to general policy issues concerning the administration of charitable trusts managed by LTCs, conflicting views were held on the suitability and effectiveness of the current means to resolve disputes concerning these trusts. This concern was driven, in part at least, by what appeared to be some long-standing and unresolved disputes between particular LTCs on the one hand and co-trustees or other interested parties on the other.

CAMAC considers that having an effective dispute resolution procedure is an important element in a properly functioning regulatory environment for charitable trusts. The objective should be to ensure that the dispute resolution mechanism is properly accessible to bona fide involved parties while at the same time producing binding outcomes on administrative matters which are consistent with the purposes for which charitable trusts were established.

5.2 Current position

5.2.1 Non-judicial dispute resolution

LTCs, as a condition of their licence, must have a dispute resolution system, including being a member of an external dispute resolution (EDR) scheme.[73] The Financial Ombudsman Service (FOS) is the EDR for trustee services. However, the question remains as to who has access to this EDR scheme in this segment of the charities sector generally. As well, there are constraints on the FOS considering fee-related disputes.

5.2.2 Judicial dispute resolution

Prior to the coming into force of Chapter 5D of the Corporations Act in May 2010, judicial review of matters concerning charitable trusts was the exclusive preserve of State and Territory courts, under their inherent equity jurisdiction over trusts, as well as pursuant to judicial powers under the various Trustee Acts.[74]

The introduction of Chapter 5D did not disturb this inherent jurisdiction:

> Any inherent power or jurisdiction of courts in respect of the supervision of the performance of traditional trustee company services is not affected by anything in [Chapter 5D].[75]

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73 s 912A(2).
74 See, for instance, s 70 of the *Trustee Act 1925* (NSW).
75 s 601SAA(1).

Relevant case law provides judicial guidance on the exercise of this inherent jurisdiction, including the removal of a trustee. For instance:

> The jurisdiction to remove a trustee is exercised with a view to the interests of the beneficiaries, to the security of the trust property and to an efficient and satisfactory execution of the trusts and a faithful and sound exercise of the powers conferred upon the trustee. In [any decision] to remove a trustee the Court forms a judgment based upon considerations, possibly large in number and varied in character, which combine to show that the welfare of the beneficiaries is opposed to his continued occupation of the office. Such a judgment must be largely discretionary.[76]

In the case of a charitable trust, it has been further held that:

> the focus, of course, must be on whether the objectives of the trust are opposed to the continuation of the trustee, since a charitable trust has no beneficiaries.[77]

Applying these principles, the Court in a recent decision refused an application to replace the trustees of a charitable trust on the basis that:

> there is no suggestion that those trustees have failed to execute the trust in accordance with the testator's wishes and in a way that best achieves the objects of the trust … In addition, it is not obvious that the trust would be more effectively administered if the current trustees were replaced.[78]

The court will also replace a trustee where the trustee has breached its fiduciary duties, has acted, or failed to act, in circumstances that endanger the trust property or has displayed a lack of honesty, or where the trustee no longer has a proper capacity to undertake the administration of the trust.[79]

As previously indicated, the court in some circumstances may review the fees charged by an LTC to see if they are excessive.[80] There are significant limitations and uncertainties on when this power can be exercised (see Section 3.3 of this report). CAMAC has elsewhere put forward proposals regarding the future application of that provision (see Section 3.5.4 of this report).

5.3 Non-judicial dispute resolution

5.3.1 Submissions

One approach proposed was to expand the non-judicial dispute resolution mechanism for disputes between an LTC and other affected parties. This could involve, for instance, empowering the ACNC to set up a body to hear and resolve disputes in this segment of the charities sector. A suggested model was the Takeovers Panel, which, in the corporate area, can make various binding determinations.

5.3.2 CAMAC position

CAMAC places importance on an accessible non-judicial dispute resolution procedure in this segment of the charities sector. An independent arbitrator, such as the FOS, may have

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76 *Miller v Cameron* (1936) 54 CLR 572 at 580-581 per Dixon J.
77 *Crowle Foundation v NSW Trustee & Guardian* [2010] NSWSC 647 at [33].
78 *Sir Moses Montefiore Jewish Home & Ors v Perpetual Company Limited & Anor* [2012] NSWSC 210 at [31]-[32].
79 See, for instance, *Garrett v Yiasemides* [2004] NSWSC 828 at [27].
80 s 601TEA.

a valuable role to play in mediating between parties, and assisting them to reach a mutually-agreed position on a contentious matter.

It may be beneficial if thought is given to clarifying and, if necessary, expanding the role of the FOS in mediating disputes involving the administration of charitable trusts, including those involving co-trustees or donees of a trust. CAMAC suggests that the ACNC could liaise with the FOS on these matters.

The parties to a successful mediation could be required to execute a deed of settlement, to be lodged with the ACNC. This would be an end to the dispute, unless it can later be shown that the settlement did not involve full candour on both sides.

CAMAC, however, would be concerned about going beyond the role of mediation and giving the FOS, or any other non-judicial intermediary, the power to make non-agreed and binding determinations on matters concerning the administration of charitable trusts, such as the fees to be charged by a trustee or who shall administer a particular trust.

In CAMAC's view, any non-judicial determination on matters not agreed to by the parties would have to be open to appeal to a court, given the financial interests and commercial reputations that may be at stake. CAMAC considers that the preferable option to ensure greater finality of proceedings, and to avoid the time and costs of a two-tier review process, is to vest the original jurisdiction to make non-agreed binding determinations in the court.

5.4 Judicial dispute resolution

5.4.1 Submissions

One view was that the current role, powers and processes of the court are satisfactory and should not be changed. Parties with a sufficient interest who are dissatisfied with any aspect of the administration of a charitable trust can seek remedies through a judicial determination.

A contrary view was that, while a judicial dispute resolution procedure exists, it does not function in a suitable manner. Respondents pointed particularly to the difficulties that can arise in establishing sufficient standing to bring a matter concerning a particular charitable trust to court. They also pointed to the potential costs that may arise from a judicial hearing, including a possible adverse costs order. The view in various submissions was that these matters can act as a strong, sometimes decisive, deterrent to the use of this dispute resolution procedure, even for the most deserving of cases.

5.4.2 CAMAC position

CAMAC places considerable importance on the effective role of the court in resolving disputes in this segment of the charities sector which cannot be successfully mediated, as proposed in Section 5.3.2, above. However, it appears that currently there are a number of actual or perceived barriers to the effective utilisation of the court in this area. These matters are considered in the judicial dispute resolution procedure proposed by CAMAC, below.

5.5 CAMAC proposal for enhanced judicial dispute resolution

5.5.1 Overview

As outlined in this Section, CAMAC proposes the enactment of enabling legislation[81] to give the court an enhanced role in the resolution of disputes involving charitable trusts administered by LTCs. This legislation would be in addition to the current inherent powers of the court in regard to these trusts. It should be implemented as part of Stage 1 (see Section 1.8.1 of this report).

The enabling legislation should deal with:

- standing to apply for a judicial hearing
- grounds for granting a hearing
- guidance on applying the primary intent of the donor
- powers of the court to make orders
- grounds of appeal
- costs of the parties.

The legislation should provide that the court means the Federal Court and any court of a State or Territory given jurisdiction to hear and decide applications pursuant to the enabling legislation.

While the CAMAC proposals in this Section focus on charitable trusts managed by LTCs, it is arguable that, in principle, and to achieve greater harmonization, a uniform and consistent approach to the role and powers of the court in dispute resolution should apply to all segments of the charities sector.

5.5.2 Standing to apply for a judicial hearing

Current position

Historically, the affairs of charitable trusts have been regulated through State and Territory laws and courts. While rules of standing to apply for a judicial hearing have differed, some jurisdictions have permitted an 'interested person' in the administration of a trust to apply for a judicial hearing. Generally, the courts have held that an 'interested person' is someone with an interest that is 'materially greater than or different from that possessed by ordinary members of the public'. That category could include a potential donee of a charitable trust.[82]

Under Chapter 5D of the Corporations Act, a 'person with a proper interest', as defined under s 601RAD, has standing to apply to the court in relation to various matters under that Chapter, the most relevant one being in relation to the power of the court in disputes alleging the charging of excessive fees.[83] In the context of a charitable trust, those persons

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81 The enabling legislation could be an additional Part of Chapter 5D of the Corporations Act.

82 *In re Hampton Fuel Allotment Charity* [1988] 3 WLR 513 per Nicholls LJ. See further GE Dal Pont *Law of Charity* (LexisNexis Butterworths, 1st ed, 2010) at 375.

83 s 601TEA. Other provisions involving a 'person with a proper interest' are ss 601SBA and 601SBB, dealing with accounts in relation to estates.

are set out in s 601RAD(1)(b), which includes 'a person of a class that the trust is intended to benefit'. There remains doubt, or differences of view, as to the width of that class. To date, there has been no judicial determination on the matter. Also, notably, co-trustees are not expressly included in the statutory definition.

Submissions

One proposal was that a regulator, such as the ACNC, be granted the power to make a preliminary assessment of whether a person should be classified as someone with a sufficient interest to apply for a judicial hearing and the merit of that person's claim. The regulator could consent to, or refuse, the interested person bringing such an action. Such an approach, it was argued, would dispense with the costs associated with seeking the leave of the court, while ensuring that only properly interested parties with a serious claim gain access to the court.

CAMAC approach

Application by the regulator

CAMAC proposes that the ACNC be given automatic standing to itself request a judicial hearing or to intervene at any stage in a hearing regarding the administration of a charitable trust commenced by any other party. The regulator might decide to act in response to complaints regarding a particular trustee or the administration of one or more trusts.

Application by other parties

CAMAC is of the view that the determination of the question of standing for persons other than the regulator should remain with the court, not an external body.

A broad test of standing should be adopted to include co-trustees and other persons with an interest in the administration of the trust, including actual and potential donees. This could be achieved by adopting in the enabling legislation the 'interested person' test as it has been interpreted by the courts, namely someone with an interest that is:

> materially greater than or different from that possessed by ordinary members of the public.[84]

It might be made clear in the Explanatory Memorandum to the enabling legislation that one of the intended effects of this proposed test is to permit applications to be made concerning trusts where an LTC is the sole trustee, where there are no involved parties that can be linked to the donor of that trust, and where there may be no recipients of benefits from the trust. Persons within any general class of potential donees of these sole trustee trusts may have such a material interest.

5.5.3 Grounds for granting a hearing

To curtail unmeritorious applications, CAMAC considers that the legislation should state that the court should hear a matter only if satisfied at the prima facie level that:

- the applicant with standing is acting in good faith
- there is a genuine dispute concerning the administration of a trust, and

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[84] *In re Hampton Fuel Allotment Charity* [1988] 3 WLR 513 at 520.

- it is in the best interests of the trust that the matter proceed to a hearing.

The legislation should also provide that where it is the regulator that makes an application, the court need only be satisfied as to the third element, namely that it is in the best interests of the trust to proceed to a hearing.

The legislation should further provide the court with a discretionary power to make directions for mediation between the parties before further considering a matter concerning a charitable trust. The Financial Ombudsman Service might be a suitable body to mediate in such cases.

5.5.4 Guidance on applying the primary intent of the donor

CAMAC proposes that guidance be provided to assist the court in determining a matter concerning a charitable trust in accordance with the primary intent of the donor.

This guidance, which could be set out in the Explanatory Memorandum to the enabling legislation, should include the following:

(1) the primary intent of the donor in establishing a charitable trust is to achieve the benevolent or philanthropic purposes or objectives for which the trust was created, (or to achieve the 'spirit' of the trust where its particular benevolent objectives can no longer be achieved), within the time-frame of the trust, and in an effective and efficient manner

(2) the administrative arrangements for a charitable trust should at all times be consistent with achieving the primary intent of the donor

(3) further to (2), the administrative arrangements of a charitable trust, including the fees and costs charged against the trust, the tenure of a trustee, and the relationship between co-trustees, should be assessed according to how well they achieve the primary intent of the donor

(4) the primary intent of the donor should prevail over any statement by the donor in a charitable trust instrument or otherwise as to the administrative arrangements for the trust, including the nomination of a particular trustee

Note: the commercial profile of a particular trustee (including in consequence of any internal changes of control of the trustee or external changes of control of any corporate group of which the trustee is a member), the particular tasks required of the trustee, and the markets within which the trust operates, may change over time, and in a manner unforeseen by the donor.

(5) in considering whether particular administrative arrangements should be changed in order to achieve the primary intent of the donor, the court may determine the matter:

- whether or not the donor was fully informed and independently advised on those administrative arrangements at the time of establishment of the trust

- notwithstanding that a trustee has not breached any legal or fiduciary obligation or requirement.

This guidance would provide the court with the flexibility to adjust administrative arrangements for a particular trust in a manner that departs from, or even in some respects is contrary to, the terms of the trust instrument, where the court considers that the adjustment is called for in order to achieve the primary intent of the donor of that trust.

5.5.5 Powers of the court to make orders

CAMAC considers that the court should be given a general power to consider any matter in dispute concerning a particular charitable trust being administered by an LTC, including any aspect of its administration, whether or not any allegation of breach or misconduct is being asserted.

Fees

CAMAC has earlier proposed that the court have an enhanced jurisdiction to deal with disputes alleging the charging of excessive fees or costs against a trust, whether in relation to the provision of traditional services or otherwise (see Section 3.5.4 of this report). The factors to be taken into account in reaching a determination would be those set out in the current legislation.[85]

The CAMAC proposals in this Section regarding the procedural aspects of any such application would substitute for the existing procedural provisions in s 601TEA.[86]

Replacing the trustee

CAMAC has earlier proposed that the court have an enhanced jurisdiction concerning whether the trustee of a particular charitable trust should be replaced (see Section 4.3.3 of this report).

The court could replace a trustee where it considers that this is called for to achieve the primary intent of the donor of the trust. The exercise of that power would not depend on the court being satisfied that any form of maladministration by the incumbent trustee has taken place.

Other matters affecting the trust

The court should also have the power to make other adjustments to the administration of a trust, where considered necessary to achieve the primary intent of the donor. The Explanatory Memorandum might set out examples of orders, including that:

- one or more unpaid (or minimum paid) independent trustee(s) be appointed to a trust, with powers to monitor the conduct of the LTC in administering the trust. This power would be particularly relevant in the context of sole trustee trusts

- a trustee provide certain disclosures to, or adopt some other course of conduct in relation to, a co-trustee or some other person.

Legal structure

The court should have the power, in exceptional cases, to convert the charitable trust into some other legal structure, such as a not-for-profit company or a PAF, where it considers

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85 s 601TEA(3).

86 If s 601TEA is to remain as a discrete provision, then the procedures in subsections (4)-(6) would need to be amended to bring them into line with the approach in Section 5.5 of this report.

that such a change is necessary in all the circumstances to fulfil the primary intent of the donor, which can no longer be attained by the continuance of the trust in its current form.

Evidence

CAMAC has also considered whether the strict application of the rules of evidence may unduly inhibit a bona fide party seeking to challenge any aspect of the administrative arrangements of a charitable trust.

While pre-trial discovery may be used to obtain admissible information, CAMAC can also see a benefit in giving the court a discretion not to be bound by the strict rules of evidence. The legislation could make clear that the court can determine the weight to be accorded to any information that it admits other than pursuant to the rules of evidence.

5.5.6 Grounds of appeal

The legislation should provide that any right of appeal against the determination of the court under the enabling legislation is limited to an error of law.

The Explanatory Memorandum could point out that, for the purpose of achieving finality within a reasonable time, the intention of this limited right of appeal is to exclude any form of re-hearing of the facts of the matter, or any challenge to the lawful exercise by the court at first instance of a discretion based on those facts.

5.5.7 Costs of proceedings

From time to time the courts have made determinations on disputed matters concerning charitable trusts. However, a number of respondents have argued that the potential costs of litigation act as a strong disincentive to the commencement of an action. For this reason, it is asserted, the existing judicial remedy may in large measure be beyond the reach of many bona fide involved parties.

Private parties

It has been argued in some submissions that trustees may have the comfort of indemnity rights against trust assets to cover their legal costs in judicial proceedings. By contrast, persons seeking to challenge the conduct of a trustee may remain personally exposed, including to any adverse costs order in the event that their application is unsuccessful.

For these reasons, CAMAC has considered two options:

- exclude all parties, including trustees, from recouping their costs from the assets of the trust in judicial dispute resolution matters, or
- expand the range of parties who may recoup their costs from the trust assets.

In regard to the first option, it may be argued that, given the benevolent and philanthropic purposes for which charitable trusts are established, their assets should only be used directly for those purposes. To permit a number of parties to, in effect, access these assets to fund court actions to settle their disputes, albeit ones directly related to the trust, may be difficult to reconcile with the charitable objectives of those trusts.

Notwithstanding this, CAMAC considers that excluding altogether a right of recoupment from trust assets could result in the judicial dispute resolution procedure becoming even more inaccessible, especially where there is a genuine dispute that needs to be resolved in the best interests of the trust.

On balance, CAMAC considers that the better approach is to increase the level of access to judicial dispute resolution by adoption of the second option. Without some financial comfort, recourse to the judicial process to resolve genuine disputes involving charitable trusts may largely be beyond the reach of deserving parties.

Under this approach, the legislation could set out the cost principles for parties in court actions involving charitable trusts, along the following lines:

> each party to have their reasonable costs met by the trust, except where the court is satisfied that a party has acted improperly, vexatiously or otherwise unreasonably, in which case the court can make such orders as to costs concerning that party as it thinks fit in the circumstances, including an order that the party shall bear all or some of its own costs and/or the costs, including on an indemnity basis, of another party to the hearing.[87]

CAMAC is aware that, in some cases, this prima facie right of access to trust assets could materially reduce those assets, thereby compromising to some extent the philanthropic or benevolent objectives of the trust. CAMAC considers, however, that the above costs constraints will act as a deterrent to unmeritorious claims.

The regulator

A further question arises as to whether the ACNC should be able to recoup its costs from the trust assets when it commences or intervenes in an action concerning a particular charitable trust.

An argument for recoupment is that costs incurred by the ACNC in what might, in effect, be an internal dispute within a particular charitable trust should not be borne from public revenue. A further argument in favour of recoupment is that parties might otherwise seek to have the ACNC, rather than themselves, initiate judicial proceedings, to avoid any drain on trust assets.

An argument against recoupment is that the ACNC regulates in the public interest, and recovery of its costs from private trusts is out of step with the performance of that role.

CAMAC considers that, on balance, the ACNC should not have a right of access to trust assets to recoup its costs when it commences or intervenes in an action concerning a particular charitable trust. CAMAC anticipates that the ACNC would initiate or intervene in proceedings to resolve a matter of material public interest, which should be funded from public revenue.

5.5.8 Implications of an enhanced judicial procedure

It is not possible at this point in time to accurately predict the extent of recourse to the proposed enhanced judicial dispute resolution procedure, if introduced.

On current indications, it may initially attract a number of applications, in particular in relation to some long-standing disputes. Equally, however, it may also provide an incentive for co-trustees or other interested parties to reach agreement on matters of contention, given the greater access of parties to the judicial review mechanism and the knowledge that the court can order them to mediation in any event.

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87 cf s 664F(4).

CAMAC considers that some time needs to be given for this judicial dispute resolution machinery to operate before any meaningful assessment of its effect can be made. It may then be possible to determine whether the enhanced court powers provide an effective mechanism to resolve disputes in this segment of the charities sector, or rather highlight embedded structural problems within the administration of charitable trusts which may need to be addressed by further legislative or other regulatory initiatives.

Appendix Terms of reference

20 September 2012

Ms Joanne Rees
Convenor
Corporations and Markets Advisory Committee
GPO Box 3967
SYDNEY NSW 2001

Dear Ms Rees

I am writing to refer to Corporations and Markets Advisory Committee a matter for its consideration and to report back to Government by May 2013. The matter relates to the regulation of certain aspects of the activities of trustee companies under the *Corporations Act 2001* and the portability of their services.

By way of background, in 2009 the Parliament passed the *Corporations Legislation Amendment (Financial Services Modernisation) Act 2009* (CLAFSMA). Among other things, this Act established a national regulatory framework for the traditional activities of trustee companies in the Corporations Act replacing diverse legislation that previously existed at the state/territory level.

One of the key objectives of the reforms was to promote efficient pricing of services provided by trustee companies.[88] As part of achieving this objective, the Act placed a cap on the amount a trustee corporation can charge a charitable trust to act as manager or trustee of either:

- a one-off capital commission of 5.5 per cent of the trust's assets plus an annual income commission of 6.6 per cent of the trust's income; or
- an annual management fee of 1.056 per cent of the trust's assets.

These provisions do not affect the ability of a charitable trust and the trustee company to negotiate different fee arrangements. The trustee company may also charge common fund administration fees and fees for returns for any duties or taxes. Fee arrangements already in place prior to this date were grandfathered and are not subject to these caps.

When introducing these reforms, the Government indicated that it would review the fee arrangements in the CLAFSMA after they had been in operation for two years.

In light of the objectives of the reforms and the experience of industry since the commencement of the reforms, I request that CAMAC inform the Government on:

88 Refer to Objective Six outlined in the Regulation Impact Statement.

- the impact the CLAFSMA has had on the quantum of fees that are, or could be, charged to Charitable Trusts and/or Foundations (Trusts) by Professional Trustee Companies (PTC) and the net funds available for Trusts to distribute to not-for-profit organisations. In doing so, consideration should be given to what fee arrangements would be available if Trusts were able to operate in an 'open' market;

- the range of additional fees beyond those regulated under CLAFSMA, that are, or could be, charged to Trusts by PTCs;

- the effectiveness of regulating 'new' fee arrangements between a PTC and a Trust in the manner contained in Division 4, Subdivision A of Part 5D.3;

- the effectiveness of grandfathering of 'existing' fee arrangements between a PTC and a Trust under Division 4, Subdivision B of Part 5D.3;

- what the current position is with regard to the removal and replacement of a trustee of a charitable trust, whether this position is unsatisfactory from a consumer protection perspective and if so, what, if any, reforms are necessary to address this; and

- other issues that impact on the objectives of CLAFSMA or the charitable purposes of trusts.

CAMAC may, depending on the issues raised under the sixth Term of Reference, choose to consider these issues further. Furthermore, for those issues which CAMAC considers are pertinent but is not in a position to review, CAMAC could bring these to the attention of the Government for its further consideration.

I note that CAMAC, as part of this review, will be consulting with interested parties including through the hosting of roundtables with relevant stakeholders.

Yours sincerely

BERNIE RIPOLL

Charitable Alliance

11 April 2014

Charitable Alliance
c/- Community Council for Australia
Level 1, The Realm, 18 National Circuit,
Barton, ACT, 2600

The Hon. Joe Hockey MP, **Treasurer**
PO Box 6022
House of Representatives
Parliament House
Canberra ACT 2600

Senator The Hon. Mathias Cormann, **Assistant Treasurer**
PO Box 6100
House of Representatives
Parliament House
Canberra ACT 2600

Dear Ministers

CAMAC Report: Administration of Charitable Trusts May 2013
Excessive fees & governance issues continue to cost Australian community millions annually

We write to you on behalf of the Charitable Alliance (**CA**) in response to the above report.

CA is an alliance of concerned trustees, stakeholders of and advisors to charitable trusts and foundations. These trusts and foundations have a corpus in aggregate that exceeds $1 billion and provide significant financial (>$1 billion annually) and other support to those in need in communities across Australia.

The *Corporations Legislation Amendment (Financial Services Modernisation) Act* 2009 (**CAFSMA**) changed the regulation of fees charged by licensed trustee companies to charitable trusts.

In September 2012, as a result of concerns expressed by CA and many organisations across the charitable sector about the negative impact of CAFSMA, the then Government requested the CAMAC review leading to the CAMAC Report published in May 2013.

The major finding of the CAMAC Report is that Charitable Trusts should not be treated in the same manner as other trusts. They are established for the benefit of the community and it is this benefit to the community that must be held as the primary purpose, the reason for their existence and the measure of their performance. It is also this primary purpose that bestows special status upon Charitable Trusts. These Charitable Trusts are not just another financial instrument or the property of financial services companies to be exploited for income purposes.

While CA welcomes the Report, particularly this core finding, CA is concerned that there are no immediate actions arising from the Report. Put simply, the Report's only substantive recommendation is a further review, namely the Stewardship Audits.

This lack of any action to address the current situation is very disappointing to CA. Any delay to the review process is unacceptable in light of the public benefit at stake. As you are aware, Charitable Trusts play a unique and vital role in building community resilience, inter-connectedness and citizenship across Australia. We contend that licensed trustee companies are, in some instances, charging unreasonable and excessive fees. This directly reduces the funds available to the not for profit sector for whose benefit these trusts were established.

CA is calling for the recommended Stewardship Audits to occur as a matter of priority. CAMAC's finding was that these audits will be a productive way to gain a better understanding of what is occurring in practice with the administration of charitable trusts operated by licensed trustee companies, as they would focus on how each trustee has exercised its powers and assumed its responsibilities for the purpose of fulfilling the donor's primary intent.

CA would welcome the opportunity to liaise with the Government on the specific terms of the audits to make sure that they address issues meaningful to the completion of the promised review. CA fully supports that the audit results and further consultation should properly inform proposals for the further amendment of the Corporations Act. It is only then that the public can be confident that the regulation of licensed trustee companies will provide fair and reasonable fees for the management of charitable trusts.

We attach CA's Policy Position provided to CAMAC and CA's Response to the CAMAC Report.

We would like to thank you in advance on behalf of CA for your attention to this very important issue.

Yours sincerely

Graeme Danks **Honorary Trustee** **Danks Trust** **Australia (CCA**	Sandy Clark **Chairman** **William Buckland Foundation**	Tim Costello AO **Chairman** **Community Council for**

Att: CA's Policy Position summary provided to CAMAC
CA's response to the CAMAC Report (summary)

Copy: The Hon. Kevin Andrews MP, Minister for Social Services, PO Box 124, Doncaster VIC 3108

Senator The Hon Mitch Fifield, Assistant Minister for Social Services, 42 Florence Street, Mentone, VIC, 3194

The Hon Josh Frydenberg MP, Parliamentary Secretary to the Prime Minister, 695 Burke Road, Camberwell, VIC, 3124

Annexure A

Members of the Charitable Alliance

Graeme Danks
Honorary Trustee
Danks Trust

Sandy Clark
Chairman
William Buckland Foundation

Tim Costello AO
Chairman
Community Council of Australia

Peter Yates AM
Chairman
Royal Children's Hospital Foundation

Martyn Myer AO
President
The Myer Foundation

Sue Hunt
Executive Director
Royal Children's Hospital Foundation

Denis Tricks AM
Chairman
Hugh Williamson Foundation

Simon McKeon AO
2011 Australian of the Year

Jill Reichstein OAM
Chair
Reichstein Foundation

Martin Carlson
Honorary Trustee
Hugh Williamson Foundation

Elizabeth Cham
IPCS
Former CEO, Philanthropy Australia

Ian Smith
Hon. Trustee, Baker IDI Heart & Diabetes Institute
Principal, Bespoke Approach

Graeme Sinclair
Trustee
William Buckland Foundation

David Crosbie
Chief Executive Officer
Community Council of Australia

Jane Gilmour OAM
Trustee
William Buckland Foundation

Leonard Vary
Chief Executive Officer
The Myer Foundation

Andrew Danks
Honorary Trustee
Danks Trust

Peter Winneke
Head of Philanthropic Services
The Myer Family Company

Michael Danks
Honorary Trustee
Danks Trust

Richard Leder
Honorary Trustee
Royal Children's Hospital Foundation

Alan Froud
Deputy Director
National Gallery of Australia

Peter Whitehead
Client Director Trustee Services
The Myer Family Company
Former Public Trustee of NSW

CAMAC Review of Charitable Trusts and Foundations
Charitable Alliance Policy Position Summary for 20 March 2013 Round Table

This summary should be considered alongside the Charitable Alliance (**CA**) CAMAC Submission 21 Dec 2012.

Background

The introduction of the *Corporations Amendment (Financial Services Modernisation) Act 2009* (**CAFSMA**) changed the regulation of fees charged by 'Licensed Trustee Companies' (**TC**s) to charitable trusts. In September 2012, as a result of concerns expressed by the charitable sector about the impact of CAFSMA, the federal government requested this CAMAC Review.

Third Pillar of Economy, First Pillar of Society

- ✓ Operating solely for the public benefit, Charitable Trusts play a unique and vital role in building community resilience, inter-connectedness and citizenship across Australia.
- ✓ Charitable Trust funding supports thousands of charities and their invaluable work.
- ✓ Issues impacting on Charitable Trusts are not just about fees, or ASX listed trustee companies profiting at the expense of the community - at the heart of these issues, is the strength of our communities.
- ✓ The fundamental goal of any change to charitable trust regulations or operations must be to strengthen their capacity to fulfil their *charitable purpose.*

Regulation Impacts Charitable Trusts' Capacity to fulfil their '*Charitable Purpose*'

The current regulatory environment surrounding TCs impacts negatively on the ability of Charitable Trusts to fulfil their *charitable purpose*. Issues include, but are not limited to:

- ✖ High fees due to CAFSMA:
  - Allowing a TC to charge a percentage of capital 'trustee fee', with no connection to service provided; and
  - Excluding the, at times significant, additional 'investment, common fund and other fees' charged by TCs
- ✖ No transparency on 'total fees charged' by TCs, leading to TCs having no public accountability;
- ✖ TCs being appointed in perpetuity, meaning there is no competition (*the only exception being removal by the Supreme Court for breach of trust or gross negligence*); and
- ✖ No separation between the trustee and investment roles and no requirement for independent investment advice.

Underlying Principles

The CA policy position and solutions package (*below*) is driven by the underlying principles that:

A. Charitable trusts are public assets established by the settlor for the benefit of the community. They are not the exclusive 'property' of TCs; and
B. The ultimate 'consumer' of a charitable trust is the community, for whom the trust was set up to benefit and in whose name the trust should be protected.

CA Policy Position

Today, TCs have a monopoly that has largely ineffective oversight. CA believes that the original aims of CAFSMA to provide more effective national regulation of TCs, increased competition and consumer protection are critical, but can only be achieved through a 'package' of:

- ✓ Transparency and public accountability;
- ✓ Competition through market based review mechanisms and true portability;
- ✓ Fee for service that is *competitive in an open market*; and
- ✓ Independent investment advice.

CA Solutions '*Package*'

1. *Open Market Competitive Pricing*:
   A. TCs should set fees based on the time and effort involved in the service provided (*i.e. fee for service*). Where the fee proposed is not based on a fee for service (*e.g. a % of income, which may be applicable to small trusts*), the TC be obliged to demonstrate the fees are *competitive in an open market* (i.e. *not excessive*).
   B. Set a '*maximum*' fee that can be charged by a TC, as the lower of:
      - 5.5% of income annually (*incl. GST*) and a one-off establishment fee in the first year; and
      - The actual level of fees charged prior to CAFSMA for matters commenced prior to CAFSMA (*i.e. real grandfathering*).
   C. Charitable trusts with assets >$1 million to undertake an open market review of TC services and fees every 5 years (*refer also the TRB independent review under item 3A*).

CA Solutions 'Package' (continued ...)

2. *Enhanced and Transparent Reporting:*
   A. CA supports the obligation for all charitable trusts to lodge an on-line annual report to the ACNC that includes details of any and all services provided by, and benefits received by, (each) trustee(s).
   B. Irregularities (incl. TC fees) detected by automated review of on-line reports be referred for review by a 'Trust Review Board' (*refer item 3A*). This seeks to overcome the ineffective CAFSMA reporting.

3. *Enhanced Accountability to facilitate Portability:*
   A. Establish alongside ACNC a specialist independent 'Trust Review Board' (e.g. *ASIC 'Takeovers Panel'*)
      - Trust Review Board (**TRB**) independently reviews charitable trusts to ensure they are fulfilling their charitable purpose and complying with *Open Market Competitive Pricing* (*items 1A & 1B*), with priority to:
        - Trusts where an irregularity is identified by the automated review of annual reports (*item 2B*);
        - Trusts with assets >$1 million, for which reviews occur on a rolling five (5) year basis, utilising information received from annual ACNC reports (*item 2A*); and
        - Trusts where there is a dispute.
      - Co-trustees, settlors, funding recipients and public be able to request the TRB review a trust(s).
      - TRB could then request that the ACNC investigate nominated charitable trust(s), with the ACNC able to apply its powers to remove/replace trustees (*refer item 4C*) and impose suitable penalties.
   B. Protect existing orphan trusts and prevent the creation of 'new' orphan trusts by legislating:
      - A fee for service model should be charged, with a statutory '*maximum*' fee of 5.5% of income annually (incl. GST) (*as per item 1B above*).
      - Where a Charitable Trust has multiple trustees today (alongside TCs), the Charitable Trust be obliged to retain multiple trustees (*e.g. replace trustees that retire with independent trustees*).
      - Where assets of a Charitable Trust exceed $1m, TCs receiving fees from a charitable trust must constitute a minority of the trustees of that trust (*as is the case in the UK*). This may require the appointment of new trustees and independent *responsible persons.*

4. *Competition through Portability*
   A. Charitable trusts with assets >$1 million to undertake an open market review of TC services and fees every 5 years (*implemented as set out under items 1C & 3A*). Where actual fees charged by a TC have increased by more than 100% since the passing of CAFSMA, the trust be prioritised for review.
   B. Where TC services and fees are not deemed to be '*open market competitive*':
      - Under item 1C, the review is referred to the TRB for independent review, following which the TRB can recommend to the ACNC a change in TC; or
      - Under item 3A, the TRB can recommend to the ACNC a change in TC.
   C. Failure to comply with *Open Market Competitive Pricing* (*items 1A & 1B*) be a trigger to replace a TC.

5. *Promote Independence and Market Competition*
   A. TC may only perform both trustee and investment manager roles for the same charitable trust, when the governing deed expressly authorises it, or where there is more than one trustee the dual roles are expressly disclosed to and approved by the independent trustees.
   B. Before investing funds of charitable trusts in financial instruments of companies related to a trustee, trustees must receive 'independent' investment advice recommending such an investment is prudent.
   C. Allow market entry for TCs that specialise in charitable trusts by providing a new specialist charitable trust license (*i.e. creating a license option that does not include a mandatory licence requirement for deceased estate administration*), allowing for specialist / dedicated charitable trustees.

CA recommends a review of the regulation after 5 years of operation, aligned with the completion of the first cycle of the TRB's rolling five year review process.

CA Policy Position Summary: This summary has been prepared in good faith by a 'CA Steering Group'. Unfortunately, due to the short notice provided by CAMAC it has not been able to be reviewed by all individuals listed in the CA submission. This summary does not over-ride any positions outlined in individual submissions CAMAC may receive from CA members.

Australian Government
The Treasury

TSY/AU

Review of Australian Charities and Not-for-profits Commission (ACNC) legislation

Terms of reference

20 December 2017

Terms of reference - 20 Dec 2017

This review will enable Government to meet its statutory obligation that a review of *ACNC Act 2012* and *ACNC (Consequential and Transitional) Act 2012* (together, **ACNC Acts**) must be undertaken after five years.

Review Panel will inquire into and make recommendations on appropriate reforms to ensure the regulatory environment established by ACNC Acts remains contemporary, ACNC Acts deliver on their policy objectives and ACNC Acts do not impair work of ACNC Commissioner to deliver against the objects of the principal Act:

(a) Maintain, protect and enhance public trust and confidence in the Australian NFP sector; and

(b) Support and sustain a robust, vibrant, independent and innovative Australian NFP sector; and

(c) Promote the reduction of unnecessary regulatory obligations on Australian NFP sector.

The review should evaluate the suitability and effectiveness of ACNC Acts. In particular, the review should:

1. Examine extent to which the objects of the ACNC Acts continue to be relevant.
2. Assess effectiveness of provisions and regulatory framework established by ACNC Acts to achieve objects.
3. Consider whether powers & functions of ACNC Commissioner are sufficient to enable objects to be met.
4. Consider whether any amendments to the ACNC Acts are required to enable the achievement of the objects and to equip the ACNC Commissioner to respond to both known & emerging issues.

Review should be informed by public submissions, international experience, round table discussions and consultation on substantive issues identified before recommendations are made to Government.

A report on the review's findings and recommendations will be made to the Government by 31 May 2018. This report will be laid before each House of the Parliament within 15 sitting days of its receipt.

Some issues may be identified by review that fall outside scope of a statutory review of ACNC legislation. Review panel should advise government of these issues and whether further examination should be undertaken.

Public submissions

Public submissions are invited in response to the issues raised in the terms of reference by sending through written submissions using the details below. Some focusing questions for submissions could be:

1. Are the objects of the ACNC Act still contemporary?
2. Are there gaps in the current regulatory framework that prevent the objects of the Act being met?
3. Should regulatory framework be extended beyond just registered charities to cover other NFPs?
4. What activities or behaviours by charities and not-for-profits have the greatest ability to erode public trust and confidence in the sector?
5. Is there sufficient transparency to inform the ACNC and the public more broadly that funds are being used for the purpose they are being given?
6. Have the risks of misconduct by charities and not-for-profits, or those that work with them, been appropriately addressed by the ACNC legislation and the establishment of the ACNC?
7. Are the powers of the ACNC Commissioner the right powers to address the risk of misconduct by charities and not-for-profits, or those that work with them, so as to maintain the public's trust and confidence? Is greater transparency required and would additional powers be appropriate?
8. Has the ACNC legislation been successful in reducing any duplicative reporting burden on charities? What opportunities exist to further reduce regulatory burden?
9. Has the ACNC legislation and efforts of the ACNC over the first five years struck the right balance between supporting charities to do the right thing and deterring or dealing with misconduct?

There will be further opportunities for stakeholders to contribute views on substantive issues that are identified by the Review Panel, including through roundtables and face-to-face consultation.

Closing date for submissions: 28 February 2018

Email: ACNCReview@treasury.gov.au

Mail: Mr Murray Crowe, Individuals and Indirect Tax Division, Treasury, Langton Cres, PARKES, ACT, 2600

Enquire: Enquiries can be initially directed to ACNCReview@treasury.gov.au / 02 6263 3992