The Institute of Chartered Accountants in Australia

16 May 2012

Mr Chris Leggett
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Philanthropy and Exemptions Unit
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The Treasury
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Dear Chris

Revised exposure draft: Restating the "in Australia" special conditions for tax concession entities

The Institute of Chartered Accountants in Australia (the Institute) welcomes the opportunity to comment on the revised exposure draft legislation and the accompanying explanatory material released on 17 April 2012 by the Assistant Treasurer, the Hon David Bradbury MP.

As mentioned in the Institute's submission on the initial exposure draft legislation, the Institute supports the Government's policy aims underlying these measures. We are pleased that many of the issues and concerns raised in relation to the initial exposure draft have now been addressed in the revised exposure draft. However, we remain concerned that the proposed changes to the 'in Australia' requirement, as currently drafted, will have unintended and adverse consequences for certain not-for-profit entities (NFPs) with deductible gift recipient (DGR) and/ or tax exempt status. In particular, we believe the proposed requirement for the tracing to the ultimate use of money or property will have unintended and adverse consequences for these entities as the requirement will be unworkable in practice.

With the exception of NFPs impacted by the standardisation of the definition of 'not-for-profit entity', the Institute notes that the proposed 'in Australia' amendments are to apply to income years starting on or after the date of Royal Assent. However, the Institute's preferred position is that the amendments ought to be considered in the context of, and in conjunction with, the other tax and non-tax reforms to the NFP sector (such as the establishment of a national regulator, changes to the tax concession for unrelated commercial activities and a statutory definition for charities).

At the very least, given the potential impact on NFPs and the possible need to restructure their activities, the Institute is of the view that a minimum 12 month transitional period should be provided in respect of all the amendments in Schedule 1 and not just in respect of the standardisation of the definition of 'not-for-profit entity'.

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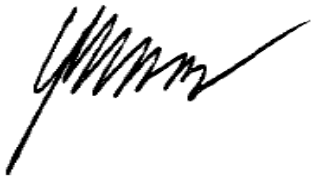
Please do not hesitate to contact Karen Liew on (02) 9290 5750 if you need clarification in respect of any of our comments.

Yours sincerely



Yasser El-Ansary
General Manager – Leadership & Quality
The Institute of Chartered Accountants in Australia

GENERAL COMMENTS

1. With the exception of NFPs impacted by the standardisation of the definition of 'not-for-profit entity', the Institute notes that the proposed 'in Australia' amendments are to apply to income years starting on or after the date of Royal Assent. However, the Institute's preferred position is that the amendments ought to be considered in the context of, and in conjunction with, the other tax and non-tax reforms to the NFP sector (such as the establishment of a national regulator, changes to the tax concession for unrelated commercial activities and a statutory definition for charities).

   At the very least, given the potential impact on NFPs and the possible need to restructure their activities, the Institute is of the view that a minimum 12 month transitional period should be provided in respect of all the amendments in Schedule 1 and not just in respect of the standardisation of the definition of 'not-for-profit entity'.

2. It is not clear whether the DGRs specifically listed by name in the tax legislation will be exempt from the 'in Australia' special conditions. The Institute is of the view that these DGRs should be grandfathered as some of them may have been granted DGR status with full knowledge of their overseas activities being considered acceptable under the current 'in Australia' requirement. If these DGRs are not grandfathered then they should, at the very least, be given a 12 month transitional period from the commencement date to allow them to restructure to maintain their DGR status.

3. We note that the exemption from the DGR 'in Australia' special conditions has been extended to authorised entities on the Register of Environmental Organisations. In light of the growing international co-operation between NFPs and NFPs becoming more internationally connected, it is likely that environmental organisations are not the only category of organisations that need to operate more broadly on the global stage to bring benefit to Australia, eg. health, cultural and educational organisations. Therefore, the Institute maintains the view that the exemption should be made available to a wider category of entities if they can meet appropriate integrity requirements similar to the requirements for authorised entities on the Register of Environmental Organisations.

DETAILED COMMENTS

1. Proposed section 30-18 - 'in Australia' special condition

Based on the drafting of the amendment to subsection 30-15(2) and the insertion of section 30-18, i.e. items 1 and 2, it is not clear how section 30-18 is intended to operate. As there is no reference in the special conditions in the table in section 30-15 that makes reference to section 30-18, it is not apparent whether section 30-18 is a special condition for all of the items in that table or is it a special condition for only item 1.

2. Proposed subsection 30-18(3) and subsection 50-50(4) – the use of the money or property by a recipient entity

We understand the integrity concern that this proposed requirement is intended to address. Nevertheless, the requirement for a DGR/tax exempt NFP to look through a recipient entity and consider the final use of its donated money or property will be difficult to comply with in practice. For example, how would a DGR trace the funds donated to another entity where the other entity simply pools its funds with other donated funds and these funds are directed to a number of different not-for-profit purposes including an overseas purpose? Would the recipient entity be required to keep separate accounts for funds donated from different DGRs to ensure that these DGRs can satisfy the 'in Australia' special conditions?

Moreover, the words '(or any other entity)' in the proposed subsections suggest that a DGR/tax exempt NFP will need to trace the use of funds through to the ultimate use of the money. Given these entities usually have limited resources, the requirement to trace donated funds to the ultimate user is

highly unworkable and would discourage DGR/tax exempt NFPs from donating to more than one organisation per income year or even donating at all. Accordingly, at a minimum, we submit that the words '(or any other entity)' be deleted from the proposed subsection 30-18(3) and subsection 50-50(4).

On another note, we suggest the following drafting amendments:

- under the proposed subsection 30-18(3), the words 'into account' after the words '(or any other entity)' should be deleted
- the reference to the use of property needs to be included in the proposed subsection 50-50(4) as it only takes into account the use of money.

3. Proposed paragraph 50-50(3)(b) – Use its income and assets solely for the purpose…

To be consistent with the drafting used in section 50-1 and paragraph 1.51 of the explanatory material, paragraph 50-50(3)(b) should be redrafted along the lines of:

'(b) use its income and assets ~~solely~~ to pursue the purposes for which the entity is established …'

Also, the way the paragraph is currently drafted, ie. 'use its income and assets solely for the purpose for which the entity is established…' could be interpreted more narrowly than what is reflected in the explanatory material. We therefore suggest that the word 'solely' be replaced with another less restrictive term, such as 'principally', that is more consistent with the explanatory material.

In addition, we suggest further clarification be included in the explanatory material on the condition in paragraph 50-50(3)(b). Some examples of an entity using some of its income and assets outside Australia in pursuing its purposes principally in Australia would be useful.

4. Application provisions - Item 161 paragraph 3

Based on the paragraph 1.124 of the explanatory material, the extended 12 month period is intended to apply to a NFP who no longer qualifies as a NFP as a result of the standardisation of the definition of 'not-for-profit entity'. Therefore, item 161, paragraph 3 will need to be amended to make reference to Part 3 which contains the new definition of 'not-for-profit entity'.

5. Suggested amendments to the explanatory material

- Paragraph 1.108 – For consistency in drafting, delete 'and' after the words 'activities of the entity,' and replace with the word 'or'.
- Paragraph 1.46 – For consistency in drafting, the reference to 'property and benefits' should be reference to 'money and property' instead.
- Paragraph 1.68 - We note that the reference to 'gifts' in paragraph 1.68 should probably be 'distributions'.
- The examples titled 'Incidental activities', ie. Examples 1.15, 1.16, 1.17 and 1.18 will need to be revisited as some of the examples are more reflective of the meaning of 'minor in extent and importance'.
- Paragraph 1.113 – the word 'of' should be inserted after the words 'change that will be' in the second sentence.
- Paragraph 1.119 – the words 'or property' should be inserted after the word 'money' in this paragraph.