

Dear Ms Purnell

Thank you for the opportunity to make a submission in relation to the exposure draft legislation (“ED”) and explanatory memorandum (“EM”) to introduce a statutory definition of charity.

We believe that a statutory definition for charities is a fundamental step in the overall reform of the Not-For-Profit sector as it will provide certainty to charities with respect to the activities they may perform without placing their charitable status at risk.

In summary our submission addresses the following:

1. use of the definition of the term ‘associate’ from the 1936 Tax Act;
2. the need for a dominant rather than exclusively charitable purpose;
and
3. the inadequate transitional period.

Associate definition

We note that we have had the advantage of reading in draft form the submission that will be made by the Taxation Committee of the Business Law Section of the Law Council of Australia (“the Committee”) and agree with many of the points that it makes. In particular, we can only but echo the concerns raised by the Committee that:

... the incomprehensible definition of “associate”, in section 318 of the Income Tax Assessment Act 1936, is employed, rather than more targeted drafting. Whilst presumably appropriate for business operating across borders, such a definition will not assist an NFP, with limited resources, in understanding the meaning of “public benefit”.

Section 318 is difficult enough for an experienced tax adviser to work through let alone a charity with limited resources and sometimes utilising volunteers with no / limited knowledge of the law.

Dominant purpose

Despite submissions to the contrary on the earlier Consultation Paper, a ‘dominant purpose’ test is not used in the ED - accordingly, an entity will effectively need to have an almost exclusively charitable purpose(s) in order to meet the definition of a “charity” in the ED.

In this regard, we note that in their submissions on the earlier Consultation Paper the St Vincent de Paul Society, the Salvation Army and the YMCA all raised concerns about using an exclusively charitable test. Here is what the St Vincent de Paul Society said in its submission:

Are there any issues with amending the 2003 definition to replace the Dominant Purpose requirement with the requirement that a charity have an Exclusively Charitable Purpose?

St Vincent de Paul Society operates over 600 Vinnies stores across Australia. Vinnies stores serve multiple purposes - they provide affordable clothing and other household goods to the community at large, and free clothing and material assistance to those experiencing financial hardship. They create employment (including supported employment) and volunteering opportunities for people in the community. They also raise funds for the broader charitable work of the St Vincent de Paul Society. Vinnies stores also create an interface between the community and the St Vincent de Paul Society as a whole. Our ability to be innovative in the way we operate and use our Vinnies stores has been a considerable factor in our successful engagement in local communities, and our financial sustainability and independence.

We are cautious about the inflexibility “Exclusively Charitable Purpose” could entail, especially in the absence of any clear definition of what it might mean. It is crucial that the requirement of either dominant or exclusive purpose not create fetters on charities’ creative approaches to financial sustainability and service delivery. This is especially relevant given the growth of social enterprise in the sector. It is in both the sectors’ interests and the interests of government to encourage a diverse, flexible and innovative charitable sector to respond to changing economic and social conditions, community needs and expectations.

In Recommendation 3 of the 2001 Report on the inquiry into the definition of charities and related organisations states:

i. “If the entity has other purposes, those purposes must further, or be in aid of, the dominant purpose or purposes, or be ancillary or incidental to the dominant purpose or purposes.”

We believe that this recommendation, made in light of 250 submissions to the inquiry, allows for flexibility while maintaining the integrity of charitable purpose.

The Salvation Army in its submission on the Consultation Paper made these points:

Charitable Purposes

The Charities Bill 2003 was an attempt to codify the definition of both a charity and a charitable purpose. It is noted the current consultation process is not revisiting the codification of what is a charity and a charitable purpose, rather it is to introduce a statutory definition of ‘charity’ for application across all Commonwealth laws.

In the drafting of the statutory definition of charity, The Salvation Army does not support the use of the phrase “exclusively charitable”.

The Charities Bill 2003 uses the phrase “dominant purpose” and the Australian Taxation Office (ATO) in Taxation Ruling TR 2011/4 Income tax and fringe benefits tax: charities (TR 2011/4) uses the phrase “its only, or its ‘main or predominant or dominant purpose”.

The Salvation Army recommends the proposed statutory definition of charity uses the current concept of dominant charitable purpose.

The Salvation Army recognises the importance and need of the flexibility that is gained in using terminology such as ‘dominant’ as opposed to ‘exclusively’ when considering the strict legal

and literal interpretations that can arise when reviewing governing or constitutional documents. This is particularly relevant when considering older style constitutional documents that may have drafting styles that are listed as purposes when in fact what is intended is only a power of an organisation. It is also noted that organisations are established by Acts of Parliament, and these organisations have very little scope to change the Acts of Parliament to amend technical deficiencies that could otherwise result in an 'exclusive' definition not being met.

The YMCA was also concerned about the move away from a dominant purpose test:

In order to achieve the necessary flexibility in the definition and more broadly, to reflect the contemporary nature of social economy organisations it will be important to retain the 'dominant purpose' requirement contained in the 2003 definition. Requiring that a charity have an 'exclusively' charitable purpose will narrow the definition and does not adequately reflect the diversity of the sector and the current context in which not-for-profit organisations operate.

It will be critical for there to be clarity in how a dominant charitable purpose will be tested and that an 'activities' test will not form part of the determination of charitable status. While the YMCA agrees that some activities carried out by an entity may not in themselves be intrinsically charitable, provided these activities are in support of the dominant charitable purpose, these activities should not be the primary determinant of charitable status. This appropriately reflects the current context in which the sector operates in that many organisations seek to diversify their revenue stream through fees for services, social enterprise and the reinvestment of surplus revenue in support of charitable purposes. Acknowledging this in the definition will support the growth of a more independent, self-reliant and innovative sector.

In light of the above therefore, we believe that it would be preferable if an approach more in keeping with current approach of the ATO (refer below) and the following extract from the Explanatory Memorandum to the unenacted Charities Bill 2003 had been adopted:

1.28 For the dominant purpose of an entity to be charitable, the entity must have a purpose or purposes that are charitable.

1.29 Similarly, for the dominant purpose of an entity to be for the public benefit, the entity must have a purpose or purposes that are for the public benefit.

1.30 Further, for the purpose or purposes of an entity to be dominant, any other purposes of the entity must further or be in aid of, and be ancillary or incidental to the dominant purpose.

1.31 It may be that multiple charitable purposes for the public benefit, when taken together, form a dominant charitable purpose for the public benefit. Therefore, it is not necessary for an entity to show that a single purpose is their dominant purpose.

1.32 In determining the dominant purpose of an entity, items that may be considered include, but are not limited to:

- the constituent documents of the entity, if the entity has such documents; and*
- the activities of the entity.*

In short, we submit that it needs to be made clear in the final Bill (and its EM) that the legislation does not impose any greater / more stringent test than what is currently faced by charities under the approach adopted by the ATO in TR 2011/4.

In this regard, paragraph 5 of TR 2011/4 defines 'sole purpose' to include the "main or predominant or dominant" purpose:

'sole purpose' is used in this Ruling to mean the only or the 'main or predominant or dominant' purpose of an institution as described in paragraph 27 of this Ruling. It has been used because the only purposes a charitable institution can have are charitable purposes or purposes incidental or ancillary to charitable purposes. It also helps avoid misunderstandings that can arise because of different usages (especially in a taxation context) of various terms that have been used by the courts to describe the required purpose.

Transitional period

There is no 'grandfathering' of the existing charitable status of entities under the ED and entities will need to find the resources to assess their charitable status on an ongoing basis.

There will also be a need for some charities to register with the ACNC as different sub-types to satisfy the new requirements.

In light of:

- the resource constraints facing most charities;
- the potential for duplicate compliance associated with other (delayed) NFP tax reform developments (including the deferred commencement of the proposed Unrelated Commercial Activities measures); and
- the potential outcomes arising from the NFP Tax Concession Working Group's review;

The proposed transitional period of 18 months for existing charities to make the necessary changes to amend their registration with the ACNC is not sufficient. We submit that a transitional period of at least three years would be far more appropriate.