AMENDMENTS TO PRIVATE ANCILLARY FUND GUIDELINES 2009 AND PUBLIC ANCILLARY FUND GUIDELINES 2011

SUBMISSION TO TREASURY IN RESPONSE TO THE EXPOSURE DRAFT DATED 22 DECEMBER, 201

This submission is responding only to the proposed change in the Exposure Draft, to Guideline 19.1 of the Private Ancillary Fund (PAF) Guidelines 2009, which relates to minimum annual distribution requirements for PAFs.

I am writing this Submission on behalf of a PAF called Hangid Foundation, being one of the directors. Our Foundation was only recently established but the whole family participates in the giving decisions and we are very passionate about philanthropy.

Hangid Foundation is very concerned about the proposal in the Exposure Draft that the minimum distribution requirement at the moment would be lower than the current 5% (the "Proposed Amendment") and I am writing on behalf of the Foundation to strongly oppose any change to the current minimum distribution of 5% of the total value of a PAF corpus. This is for three reasons:

1. Lowering the distribution requirement will mean that less funds will be given to DGR1's. In the current economic climate, more charity is needed not less.
2. Any PAF receiving sound investment advice will be receiving returns well in excess of 5% of the value of their corpus. So there is no reason for the current change.
3. If PAFs taking investment advice, are able to achieve over 5% in growth, then the Proposed Amendment has the effect of rewarding PAFs for making bad investment decisions.

These reasons are all elaborated further below.

1. More Charity is Needed not Less

The JB Were Report issued in December, 2015, entitled Australian Giving Trends, Signs of Life (see http://www.jbwere.com.au/content/dam/jbwere/documents/JBWere%20Report_Australian%20Giving%20Trends_Dec%202015_FINAL.pdf) indicates that the major recipient of PAF giving is welfare being 30% of last year's PAF giving. The actual amount of this giving isn't stated in the report but conservatively, if the total PAF corpus value (according to this Report) is $4billion and PAFs are currently giving 30% of their 5% annual distributions to welfare then this equates to around $60M.

These funds are utilised by organisations that are filling financial gaps that Government can't currently fund. So philanthropy is desperately needed for welfare.

If the proposed amendment is introduced, the $60M sum will immediately drop, as PAFs will now be permitted to gift 2% of their corpus instead of 5%. This will reduce the amount of all philanthropic giving by PAFs to all recipients including welfare.

If the Proposed Amendment could be justified, then this drop in available gifts would be understandable. However for the reasons explained in Section 2 below, the changes cannot be justified. So there is no justification for facilitating a drop in philanthropic funds that are vitally needed by those less fortunate in the community as well as for all other recipients of philanthropic funds from PAFs.

2. Financial Returns Above 5%

For the purpose of this Submission, I spoke to three leading PAF advisors. I didn't seek their consent to quote their responses for this Submission but I am happy to contact them to seek their consent if the Tax Office wished to follow up the conversations I had.

All of them indicated that their clients would all be currently receiving well over 5% growth in their corpus. They also indicated that as a result, they didn't think there was a need to change the percentage of minimum distribution. The strategies from each advisor to achieve this growth are listed below:

Advisor 1 – One third of the corpus in shares, one third of the corpus in property and one third of the corpus in cash.

Advisor 2 – One quarter of the corpus in shares, one quarter of the corpus in property, one quarter of the corpus in secured lending or hybrid investments and one quarter of the corpus in cash.

Advisor 3 – One quarter of the corpus in shares, one quarter of the corpus in property, one quarter of the corpus in alternative investments and one quarter of the corpus in cash.

One advisor indicated that if these type of investment strategies weren't deployed, a PAF could potentially be in breach of the PAF Investment Guidelines.

Hangid Foundation also earns above 5% in growth a year from our PAF.

The Explanatory Statement that was released with the Exposure Draft, stated that :

The minimum annual distribution rate is being amended to provide greater flexibility in unexpected economic conditions.

Clearly the Tax Office needs to take such events into account. However, I respectfully suggest that not only is the proposed change not needed at the moment based on the growth that is reasonably attainable in the current investment market but it is the wrong change.

A more equitable way of addressing the risk of market change is to change the proposed definition for distributions from the "lesser of" to the "greater of". This would mean that PAFs would be giving away all of their annual growth and in a year of poor investment returns, the greater amount could become the average RBA cash rate in that year.

Rewarding Bad Investment Decisions

If there are leading PAF financial advisers that are all able to achieve greater than 5% growth and Hangid Foundation is able to achieve 5% growth, why is the Proposed Amendment needed?

Furthermore, why does the law need to change to accommodate PAFs that may not be abiding by the PAF Investment Guidelines as their investments haven't been effective? Isn't this just rewarding bad investment decisions???

Conclusion

For the reasons described above, Hangid Foundation strongly opposes the Proposed Amendment and considers that no change is needed to the PAF Guidelines dealing with annual minimum PAF distribution.

If the Tax Office considers there is nevertheless a need to future proof the minimum distribution definition, then the word "lesser" should be replaced with the word "greater" and this would achieve the required outcome in a much more effective, justifiable and equitable way.

Roz Kaldor-Aroni
Director of Hangid Foundation
12 February, 2016