Neumann & Turnour LAWYERS

Submission on behalf of the Public Trustee of Queensland to Treasury Consultation on Public Ancillary Funds

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N&T Lawyers Pty Ltd trading as Neumann & Turnour Lawyers ACN 010 739 670 ABN 11 955 351 885 | **www.ntlawyers.com.au**
Level 2 345 Ann Street Brisbane Queensland Australia | Post: GPO Box 649 Brisbane 4001 | DX: 938 Brisbane
Telephone: (07) 3837 3600 | International: +617 3837 3600 | Facsimile: (07) 3211 3686 – General | Facsimile: (07) 3211 4171 – Family Law
A member of the Southern Cross Legal Alliance with associated legal firms in Sydney Melbourne Perth Darwin Auckland and Christchurch

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Introduction

Public Trustee of Queensland as trustee for Queensland Community Foundation

The Public Trustee of Queensland (PTQ) is a Statutory Corporation. The PTQ is the trustee of the Queensland Community Foundation (QCF) a public ancillary fund with approximately 190 sub-funds and about $70 million in assets. The QCF was established in 1997 to facilitate philanthropy by allowing donors to create a perpetual source of funds for either charitable purposes or designated charities. Since then, gifts have been made and have been received from Wills of donors which have indicated a preference (whether binding or non-binding) that funds be applied to the objects of a particular charity or to a particular charity by name. One of the attractions of the QCF is that all administration costs are borne by the PTQ and two other sponsors, so that there are no administration costs deducted from sub-funds. The donors to sub-funds intentions vary but as a general proposition it is expected that the donations will be invested with income distributed perpetually to DGRs that are either:

1. pursuing particular charitable purposes,
2. charities in particular regions, or
3. named; that is to designated charities, provided (implicitly) that they continue to pursue the same purpose and the entity remains a DGR.

Many, if not most, of the gifts to QCF are testamentary and are received pursuant to Wills drawn that (understandably) have not contemplated the Public Ancillary Fund Guidelines.

Both the PTQ and the QCF have separate Australian Business numbers (ABNs).

Overview

This submission:

1. Raises a threshold issue about whether the exemptions intended for public trustees actually apply to public trustees in their capacity as trustee;

2. Comments upon specific matters arising from the proposed changes; and

3. Makes some general observations that might be of assistance on broader policy issues.

With the exception of comments on portability to public ancillary funds, the submission is confined to comment upon proposed changes to the public ancillary fund guidelines. No comment is offered on private ancillary fund matters specifically. Some of the general comments may apply to both.

The PTQ in its own right or as trustee – a threshold issue

As a matter of law, the PTQ whether acting in his or her own capacity or as trustee of a trust, is the relevant legal entity. Both for taxation purposes and also under the *Australian Charities Not for Profits Commission Act 2012* a 'tax entity' as distinct from a 'legal entity' concept is

introduced. The tax concept of an entity distinguishes a trust from the trustee. These guidelines do not clarify whether it is a public trustee as a legal entity or a public trustee as a tax entity that is exempt from the operation of guidelines. Chief Justice French of the High Court in a lecture given at Melbourne University identified some of the difficulties arising from this distinction between an 'entity' for tax purposes and a legal 'entity'.[1] This may well be one of those situations. It is submitted that for the purposes of clarity the new guidelines should make it clear that the public trustee specific provisions, apply to a public trustee as a legal entity operating as trustee of any trust as well as a public trustee acting in its own right. Of course it is almost certainly going to be the case that it will be a public trustee acting as trustee that will need the protection of the exemptions afforded public trustees under the proposed new guidelines. It is submitted this should be made clear in the guidelines to avoid doubt.

Specific matters raised by the proposed amendments

The 4% rule

The 4% rule promulgated as regulations in Public Ancillary Fund Guidelines 2011 has been deeply problematic because the PTQ has taken a fairly conservative approach to investment and has historically distributed all income. This has meant that the capacity to meet both the 4% rule in times of low income return and also meet the terms of the trust have been worrisome. The PTQ therefore welcomes this proposed substantive change.

The PTQ is aware that there may be pressure from some in the philanthropic sector to maintain the current fixed distribution rules. It is respectfully submitted that each charitable trust is different and it is not for some in the sector, albeit well meaning, to oblige the government to leave others in the sector either potentially in breach of their trusts, or the law. The PTQ therefore encourages the Assistant Treasurer to resist any pressure for return to the 4% rule.

Portability from private ancillary funds to public ancillary funds

The PTQ submits that the new Guidelines should permit portability from private ancillary funds to public ancillary funds. It was the announced intention of the government and is good public policy. There is not any legal impediment to this, provided the correct procedure is followed.

On 28 May 2015 Josh Freidenberg MP, then Assistant Treasurer, in a joint media release with Scott Morrison MP, then Minister for Social Services, announced that private ancillary funds would be able to transfer their assets to other ancillary funds. There was no qualification that the transfer would only be to other private ancillary funds.[2]

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[1] Robert French AC (2 May 2015) *Harold Ford Memorial Lecture Trusts and Statutes* http://www.hcourt.gov.au/assets/publications/speeches/current-justices/frenchcj/frenchcj20May2015.pdf accessed 10 February 2016

[2] The Hon Josh Frydenberg MP (28 May 2015) *Measures to boost philanthropy in Australia* Joint media release with The Hon Scott Morrison MP Minister For Social Services at http://jaf.ministers.treasury.gov.au/media-release/026-2015/ accessed 9 February 2016.

Some private ancillary funds may wish to roll their assets into a sub-fund of QCF. This may occur where the founders of the private ancillary fund have grown older, no longer wish to be responsible for the day-to-day running of the fund, and do not have others to run the fund, or prefer the PTQ to act as trustee. At present the PTQ is aware of at least one private ancillary fund waiting for the promulgation of the proposed amendments to transfer its funds into the QCF. It is good public policy to enable this to occur.

Transfers between ancillary funds were addressed in *the Income Tax Assessment Act (1997)* s.426- 170 in the following terms:

> **426-170 Ancillary funds must not provide funds to other ancillary funds**
> An *ancillary fund must not provide money, property or benefits to another ancillary fund unless permitted to do so by the *public ancillary fund guidelines or the *private ancillary fund guidelines (whichever are applicable).

It follows that there is not any legal impediment to the authorisation of such transfers provided they are included in the new guidelines – in fact the legislation anticipates it.

The PTQ therefore submits that the announcement of Josh Friedenberg should be carried into effect so that transfers from private ancillary funds to QCF can occur.

The lawfulness of binding nominations

It is the submission of the PTQ that the Guidelines should support rather than hinder the carrying into effect of the charitable intention of donors including the capacity to make binding nominations if:

1. that is permitted generally as a matter of trust law; and
2. the binding is to the effect that the beneficiary is a DGR.

To the extent that the guidelines attempt to set out that the PTQ cannot accept funds earmarked for particular charities, the PTQ submits that the Guidelines go too far. It is submitted that it is a matter for the PTQ as trustee, (where necessary with the assistance of the Court) to determine if a separate trust is created by a particular gift and its terms. If the PTQ forms the view a gift can be received as trustee of QCF on any particular basis that must be passed on to a particular designated charity, then it is submitted that this is a matter for the PTQ.

Provided the PTQ complies with the law of charities and the tax legislation, there is not any public policy objective achieved by further regulations being added. The current Guidelines and Taxation Ruling 2011/4 indicate the acceptance of gifts by a Public Ancillary Fund with conditions that bind the trustee's discretion, might create a separate trust for taxation purposes. Those documents, when read together, indicate that the Commissioner will consider that a gift to a Public Ancillary Fund on conditions, is capable of being a separate trust and thus, would require its own separate registration as a charitable trust and application for income tax exempt status.

The 2016 Guidelines amend Guideline 44 of the 2011 Guidelines by adding an additional note:

Note 2: Due to the public nature of the fund, it is good practice for a trustee to review, amongst other things, the purpose(s) of the fund and any non-binding preferences indicated by donors before making distributions.

The PTQ submits the following in respect of that note:

1. In Queensland (at least) it may not be possible for donors to express "non-binding" preferences when they make gifts to the QCF.

2. The reason for the ATO's current positon in respect to "binding preferences" might stem from the case of *Re Australian Elizabethan Theatre Trust (1991) 102 ALR 681*. That case should not be applied to any Ancillary Fund for the reasons outlined below and therefore gifts made subject to (binding) preferences to public ancillary funds should be expressly permitted or at least not be expressly prohibited.

3. Ancillary funds should be free to administer (within the one ancillary fund) gifts of income and capital to many specified (named) charities without offending any revenue law.

Our client understands the *Elizabethan Theatre case* as authority for the principal that a trust with tax exempt status cannot accept donations that bind it to perform non-charitable purposes, so that the result is that non-charitable purposes are achieved through a tax exempt DGR trust. All ancillary funds are required to distribute to entities with DGR status. If that rule is followed, the mischief observed in the *Elizabethan Theatre case* could not eventuate in any ancillary fund.

The Guidelines should be flexible enough to enable the PTQ to determine whether gifts under Wills dating back to 1997 can be received into the QCF or constitute a separate fund, and it is submitted that this is best achieved by leaving the lawfulness of binding nominations to the general law. PTQ takes the view that ancillary funds were created to facilitate such giving.

In Queensland (at least) any person interested in the due administration of a charitable trust can apply to the Court under section 106 of the *Trusts Act 1973* for a direction that monies given to the QCF be administered in a particular way. We take the view that, as a matter of law, it is not clear whether a charity that was a subject of a non-binding preference expressed by a donor, could obtain one of those directions compelling the Public Trustee to administer funds in the QCF in a particular manner, at any given time. The law relating to such matters is complex and while the PTQ considers that any preference expressed by a donor to the QCF does not create a separate trust obligation, there may well be obligations (inferior to those of a trust relationship) that still apply to the Trustee of the QCF.

For these reasons, the PTQ submits that:

1. In Queensland, at least, it may not be possible for donors to express "non-binding" preferences when they make gifts to the Queensland Community Foundation;

2. “binding preferences” ought to be allowed in relation to any ancillary fund; and

3. Ancillary funds should be free to administer (within the one ancillary fund) gifts of income and capital to specified (named) charities without offending any revenue law;

4. If the Guidelines are to attempt to set out the scope of trustees’ discretions in relation to binding and non-binding preferences, then they need to take cognizance of the law in each State and Territory and consider whether there may be fiduciary or contractual obligations that fall short of a trust that could limit a trustee’s discretion; and

5. Guideline 44 needs to be amended further to give these recommended changes effect.

On this point then, it is submitted that the determination of when a separate trust arises, should be left to the general law in relation to binding and non-binding nomination. Provided the binding nomination is to the effect that the funds must be paid to a DGR that is not another ancillary fund, there is no policy object achieved by further regulations.

Broader policy issues

It follows from the above that there are some broader policy implications. It may be helpful to develop these into principles.

The philanthropy environment is maturing and with it the regulation environment is emerging as distinct from taxation. Second, there is a trend towards reduction rather than increase of red-tape.

The guidelines were formulated before the establishment of the ACNC. The establishment of the ACNC has matured the regulatory environment (relating to philanthropy and charities) such that one may now question whether detailed regulatory guidelines need to be published by the Assistant Treasurer. The function of the ACNC is, in essence, to provide a register, and to take regulatory responsibility for the charities and not-for-profits sector. Most public and private ancillary funds will be charities but some may be another form of not-for-profit. The question should therefore be asked: what if any *regulatory* function can and should be transferred to the ACNC and what, if any, should not? On its face, the Guidelines address almost if not identical subject matter as the Governance Standards promulgated as Regulations to the ACNC Act. The difference is arguably that the Guidelines address issues in a detailed and prescriptive way what the Governance Standards address in a principled way. This raises three issues for consideration:

First, should supervision of public ancillary funds pass to the ACNC? The PTQ can see some benefit in reporting to only one entity and complying with the requirements of only one regulator.

Second, following from the prior point, there may be benefit in operating under only one set of regulations/guidelines rather than ACNC Regulations and the Guidelines. That would lead to the parts of the Guidelines not already adequately addressed in the Governance Standards, being

promulgated as Regulations to that Act? This may reduce duplication and also potential conflict between the Guidelines and the ACNC Regulations. Guideline 11 is an example of a replication of a Governance Standard that could be abolished by such integration. There is a potential for conflict between the Governance Standards and the Guidelines and if there is, then which will prevail? Areas where this could arise include in relation to 'auditing' and future 'in Australia' limitations. One set of rules in one place applying to all public ancillary funds may be an aspiration worth pursuing - particularly as both are under the same Minister. (Although only charities are regulated by the ACNC at the moment, the non-charity public ancillary funds could be a logical first extension to include other not-for-profits.)

Third, the division of tax from regulation allows the tax laws to function as tax laws rather than carry regulatory functions.

With Compliments

Dr Matthew Turnour