



THE TAX INSTITUTE

2 May 2013

Manager
Philanthropy and Exemptions Unit
Indirect Philanthropy and Resource Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

Attn: Ms Maria Purnell

By email: charities@treasury.gov.au

Dear Ms Purnell,

A Statutory Definition of Charity

The Tax Institute is pleased to have the opportunity to make a submission to the Treasury in relation to the *A Statutory Definition of Charity Exposure Draft (Exposure Draft)*.

We believe that the proposed definition is an improvement on earlier attempts to provide a statutory definition¹ of “charity”. Given the significant number of tax concessions available for charitable and other non-profit entities at the Commonwealth level, clarity and certainty of the definition of charity is extremely important so that charitable entities can determine whether the relevant tax concessions are available to them. As we explain later in this submission, we have a number of suggestions for further improving the statutory definition.

Summary

Our submission addresses some concerns that The Tax Institute has with the Exposure Draft and suggests some alternate drafting to improve the statutory definition of charity. In summary, our submissions consist of:

¹ Eg *Charities Bill 2003* – Exposure Draft

- Suggestions for amendments to the Exposure Draft;
- Observations about certain comments in the Explanatory Memorandum concerning commercial activities that conflict with current case law; and
- Suggestions for organising the provisions in a more logical order.

Discussion

1. Suggested amendments to the Exposure Draft

a) Overall construction of the provisions in the Exposure Draft

The Tax Institute requests that Treasury clarify whether it is intended that the common law will continue to play a role in the construction and interpretation of the provisions contained in the Exposure Draft or whether the terms of the Exposure Draft are to be construed according to their own terms and the Explanatory Memorandum (**EM**).

The Factsheet² provided by Treasury states that the purpose of the Exposure Draft is to provide clarity and certainty for charities and the public on the definitions of “charity” and “charitable purpose” and not change the charitable status of existing charities or affect their tax treatment.

Whether this occurs, however, will depend on how a court interprets the provisions. As an example, what is a court to make of provisions such as subsections 6(1)(b) and 6(5)? Statements in the EM (e.g. paragraph 1.19) are not adequate to settle the question. Is it intended that the statute resolve the concerns with the treatment of government entities (discussed below)?

It is critical for parties who will rely on this Exposure Draft to know its intended place in the current legal landscape. If it is intended that the provisions of the Exposure Draft should not amend the common law except where expressly stated otherwise, this should be made clear by Treasury on the face of the Exposure Draft. If it is intended that the provisions are to supplant the common law, this should be made clear by Treasury on the face of the Exposure Draft.

b) Section 5

Note 1 to paragraph (b) in the definition of “charity” indicates that it is necessary to have regard to the entity’s governing rules, activities and other relevant matters in determining whether an entity is a charity. In our view, these matters are core criteria

² *Treasury’s Not-for-Profit Reform Factsheet: Statutory Definition of Charity*

for determining whether an entity is a charity. We recommend that this note form part of the operative provisions rather than remaining as a note in the legislation.

c) Section 6

(i) Section 6(1)(b)

We suggest the inclusion of the statement at section 6(1)(b) that “the benefit is a universal or common good” is unclear and may be unduly restrictive. Some explanation of the term “universal or common good” is included in subsection 6(5). However, this appears to simply substitute one unclear and undefined term (“universal or common good”) for another (“real overall value to the public”). Further, no explanation for the terminology is provided in the EM. As the terms “universal”, “common good” and “real overall value” are not defined for the purposes of the Exposure Draft, they would take their ordinary meaning.

It is unclear what these terms add to the determination of whether a purpose is for the public benefit. In particular, terminology such as “universal” suggests that there must be an absolute consensus on the “goodness” of the benefit which may be impossible to achieve in practice. Further, given the breadth of the terms “universal” and “common”, we suggest that it would be impractical, and virtually impossible, for any charity to satisfy the threshold that the benefit they provide is for the “universal or common good”.

(ii) Section 6(3)

Throughout section 6, reference is made to “benefit”. However, in section 6(3), reference is made to “possible benefit” (and “possible detriment”). Reference to any possible benefit makes this subsection very broad-reaching. On the face of the legislation, there is seemingly no allowance for the provision of even the most insignificant amount of private benefit to be provided to any of the various parties listed at subsection 6(3)(a) in determining whether the purposes of the entity are for the public benefit overall. Consequently, provision of even the most minor benefit unintentionally may be detrimental overall to this determination.

Comments made in the EM with respect to private benefits imply that if private benefits that are minor or incidental are conferred by the entity, this should not be detrimental to the determination of whether the purposes of the entity are for the public benefit. It is preferable if this limitation is expressed within the provision rather than being drawn from the EM.

We have similar concerns with respect to the reference to “possible detriment”. In particular, we query what the expression “a member of the general public” contained in

section 6(3)(b) is meant to capture. This seems to be an exceptionally, perhaps overly, narrow requirement.

Paragraphs 1.49 and 1.50 of the EM refer to this section and discuss the possible detriment that may occur. However, The Tax Institute queries whether, simply because one member of the public may suffer possible detriment, this should impact negatively on determining whether an entity's purposes are for the public benefit or not.

Inclusion of such an overall broad-reaching provision imposes an unduly high and unrealistic burden on an entity to ensure that they do not provide any possible benefit at all to any of the parties mentioned at subsection 6(3)(a) nor cause any possible detriment to even one single member of the public.

d) Section 7

We refer to the inclusion of the expression, "in the absence of evidence to the contrary" in respect of the presumption of public benefit which applies to certain charitable purposes listed in section 7.

The EM refers to certain entities, such as taxation authorities, who may challenge the presumption of public benefit of those entities whose charitable purposes would otherwise be presumed to be for the public benefit pursuant to section 7. However, it is not clear who bears the onus of proving that there is no evidence contrary to the presumption of public benefit. Does this onus fall with the entity which is relying on this presumption? Does this onus fall on the Australian Charities and Not-For-Profits Commission when making a determination regarding the status of the entity and whether it will register (or deregister) it as a charity?

We also query, for example, whether the Exposure Draft effectively negates the special treatment afforded by the common law concept of charity to poor relations/members/employees trusts, as considered by the House of Lords in *Dingle v Turner* [1972] UKHL 2. The ATO accepted the authority of *Dingle v Turner* in TR 2011/4. While a trust for the relief of poverty will get the benefit of section 7 of the Exposure Draft, this will only be so if there is no evidence to the contrary. Such evidence would presumably relate to the issues to be decided under section 6. If that is so, the very terms of these trusts may potentially be relevant contrary evidence counteracting the presumption of public benefit.

We request Treasury include some guidance on these issues in the EM.

e) Section 12

Section 12 is not clearly worded and may cause confusion regarding what determinations are required to be made of the “fund”, the “entity” and the “government entity”.

Further, the use of the defined term "government entity" in this context does not appear appropriate because it is being used to achieve different aims elsewhere. In particular, that term is used in paragraph (d) of the definition of “charity” in section 5 to ensure such an entity cannot be a "charity", but it is not otherwise used in relation to the definition of charitable purposes. This suggests that the common law consideration of whether a fund, authority or institution is too closely connected to government to be charitable still prevails. If this is correct, nothing in the common law would limit consideration to those organisations defined to be a "government entity". It is therefore possible for an organisation to not be a "government entity" but still be too closely connected to government to be charitable, such as an entity established under a State or Territory law but not prescribed under section 4(2). This may give rise to anomalous outcomes.

It is therefore suggested that a broader definition of organisations connected with government is required for the purposes of section 12. Alternatively, if the previous common law consideration of this point is to no longer apply, this should be clarified.

We have extracted section 12 at Appendix A and made some suggestions in mark-up to this provision. We have also suggested some alternate wording for section 12 which Treasury may use to rework the provision and prepare a clearer provision.

f) Sections 7, 11 and 13 – New and Inconsistent terminology

The Tax Institute notes that inconsistent terminology is used between section 7 and section 11. Section 11(a) introduces a charitable purpose of "advancing social or public welfare" but does not use the terminology “relief of poverty, illness or the needs of the aged” familiar from the *Statute of Elizabeth*³ and the common law. However, those familiar terms are used in section 7 and the EM which also make some relevant remarks on this point. For instance:

- Note 1 included in section 7 states that the purposes noted in section 7 are included in section 11. An example is given that the purpose of advancing social or public welfare includes the purpose of relieving poverty.

³ Preamble to the *Statute of Charitable Uses* 1601

- Per paragraph 1.84 of the EM, the purpose of relieving illness is encompassed in the purpose of advancing health. Per paragraph 1.89, the purpose of relieving the needs of the aged falls under the charitable purpose of “advancing social or public welfare”.

Hence, there is some inconsistent use of terminology between section 7 and section 11. We refer to the five purposes stated in section 7 of which two are expressly restated (advancing education and religion) and three (relieving the needs of the aged, relieving illness and relieving poverty) are not, while the EM includes nearly a page of examples of matters that could fall within the meaning of the term "purpose of advancing social or public welfare".

Section 13 clarifies some aspects of this purpose to a limited extent by ensuring it extends to include the purpose of supporting and protecting children and young people and certain disaster relief purposes.

As one of the aims of enacting a statutory definition is to clarify the common law without changing it, The Tax Institute suggests that it would be preferable for the legislation to include expansive definitions which nevertheless clearly include the historically familiar terms.

It may be useful if section 13 also expressly referred to the purposes of relieving the needs of the aged, relieving illness and relieving poverty (and, potentially, other purposes mentioned in the EM) as being within the meaning of a purpose of advancing social or public welfare. This would make it clear on the face of the legislation that these three purposes at least are in fact included in the charitable purposes as defined in section 11, rather than having to rely on (inoperative) Note 1 in section 7 and the EM.

2. Explanatory memorandum – commercial activities

Comments appear at paragraphs 1.36 and 1.37 of the EM to the effect that where business operations or commercial activities become an end in themselves, the entity may no longer have solely charitable purposes.

This particular comment conflicts with the principle which emanates from *FCT v Word Investments Ltd*⁴ which, as noted at paragraph 1.16 of the EM, is that

activities undertaken by an entity need not be intrinsically charitable for the entity to be a charity.

⁴ [2008] HCA 55

At paragraph 24 of the High Court judgement in *Word Investments*, the High Court rejected the notion of commercial activities being an end in themselves and therefore a “purpose” of the entity:

It is therefore necessary to reject the Commissioner's arguments so far as they submitted that Word [Investments] had a "commercial object of profit from the conduct of its business" which was "an end in itself" and was not merely incidental or ancillary to Word's religious purposes. Word endeavoured to make a profit, but only in aid of its charitable purposes. To point to the goal of profit and isolate it as the relevant purpose is to create a false dichotomy between characterisation of an institution as commercial and characterisation of it as charitable.

Therefore we do not understand why Treasury has included the statement contained in paragraph 1.37 suggesting that if a charitable entity undertakes commercial activities, this may cause the charitable entity to have purposes other than charitable purposes. The conclusion which may follow is that the entity is no longer charitable. Based on the decision in *Word Investments*, the suggestion being made is contrary to the common law position. We request that Treasury consider removing these comments from the EM.

For completeness, we note the *Word Investments* decision is the subject of the *Better Targeting of Not-for-profit tax concessions* measure Treasury is currently working on.

3. Layout of the provisions

The Tax Institute questions the layout of the Exposure Draft and the ordering of provisions, including the need to breakdown the Exposure Draft into Parts.

We suggest the following ordering of the provisions may make more sense logically for someone trying to work through the definitional and operative provisions (references are to the current draft section numbers):

- i) Section 1 – Short title
- ii) Section 2 – Commencement
- iii) Section 3 – Definitions
- iv) Section 4 – Government entity
- v) Section 5 – Definition of charity
- vi) Section 11 – Definition of charitable purpose
- vii) Section 13 – Purpose of advancing social or public welfare
- viii) Section 6 – Purposes for the public benefit
- ix) Section 7 – Certain purposes presumed to be for the public benefit
- x) Section 9 - When public benefit test does not apply

- xi) Section 8 – Purposes of native title holding entities that are directed to the benefit of Indigenous persons who are related
- xii) Section 10 – Disqualifying purpose
- xiii) Section 12 – Funding charity-like government entities
- xiv) Section 14 – Cy pres schemes

If you would like to discuss any of the above, please contact either me or Tax Counsel, Stephanie Caredes, on 02 8223 0011.

Yours sincerely

A handwritten signature in black ink that reads "M. Flynn" followed by a long horizontal flourish.

Michael Flynn
Vice President