

NDS comments to the Australian Treasury on the 2015 Tax Review

## Overview

NDS appreciates the opportunity to provide comments on the review of taxation.

NDS’s purpose is to promote quality service provision and life opportunities for people with disability. This submission will identify the taxation arrangements that facilitate this purpose within a fair tax system that adapts to the changing needs of the whole community. Specifically, we have responded to the questions in Chapter 7 of the *Re:Think* Tax Discussion Paper which is about tax in the not-for-profit (NFP) sector.

Retaining tax concessions for NFP disability organisations will play a key role in ensuring a viable future disability sector. This is in the public interest because the NFP component of the disability sector is critical to the success of the National Disability Insurance Scheme (NDIS) which in turn, will impact the social and economic wellbeing of Australia.

NFP disability organisations are at the forefront of building inclusive communities, which is a cornerstone of the NDIS. Through collaboration across local communities, local government, and allied sectors with common causes, the NFP disability sector has become a rich source of social capital. It recruits volunteers, builds community engagement, develops skills and social networks and enhances civil society.

It is difficult to precisely calculate the value-add contributions of the NFP sector but we do know that in many cases they cannot be efficiently contracted for and will not be provided by the for-profit sector. Furthermore, an effective NDIS market relies on the availability of diverse consumer options, including NFP disability organisations.

## Are the current tax arrangements for the NFP sector appropriate? Why or why not?

Current tax concessions are necessary to help NFP disability organisations maximise their charitable purpose and to enhance both the social and economic fabric of Australian society. These concessions include: the income tax exemption; higher GST registration threshold; capped exemptions from (or rebates of) fringe benefit tax (FBT); and the ability to receive tax deductible gifts.

Any gain in tax revenue from removing tax concessions in the NFP disability sector will reduce the resources that the NFP disability sector has to direct towards building inclusive communities and effective support networks and through this reducing the need for crisis services. Overtime this will likely increase the cost of crisis services in the health, justice, income support, housing, child protection and disability sectors.

Part of the added value of the whole NFP sector was calculated by the Productivity Commission in 2010 to include 4.6 million volunteers (a wage equivalent value of $15b)[[1]](#footnote-1). We are not sure exactly how much volunteering occurs in the NFP disability sector but if it is just 10% of all volunteering then that is $1.5b added value. Forgoing tax revenue from the NFP disability sector comprises both a great return on the investment, in addition to ensuring support is available to some of the most disadvantaged people in Australia.

NDS would be concerned by any proposal to replace tax concessions with direct funding. Attempting to itemise and contract for positive externalities arising from NFP organisations is fraught. Firstly, it is not practical to calculate an appropriate and fair quantum of funds. Secondly, the outcome focused nature of NFP missions in combination with the flexibility of non-contract funds allows organisations to be more responsive to changing and emerging needs and to build communities and support individuals. This added value does not easily lend itself to pre-identified services identified in contracts. Finally, current arrangements for tax concessions are legislated and provide greater certainty and stability for the sector than a direct funding approach would.

It is also important to note that tax should be applied to private wealth. Whereas, NFP disability organisations reinvest any surplus funds into activities associated with their charitable purpose—there is no accumulation of private wealth.

NDS recommends that the Government:

1. **Retain the FBT concessions to help NFP disability organisations attract an effective workforce**

Demographic trends and service sector reforms such as the NDIS will increase the demand for workers in the disability, aged-care and health sectors which all draw on similar worker catchments. This pressure combined with the relatively low pay rates for workers in the disability NFP sector contributes to significant retention and recruitment challenges. It is not possible at current funding levels, for example, to pay managers salaries that are competitive with the private sector or government disability sector.

The FBT exemptions/rebates that facilitate salary packaging, reduce the disincentives around low pay rates by increasing the ‘take home’ benefit of remuneration. NFP disability providers are clear that these employee tax concessions have been crucial in the attraction and retention of their staff and any reduction would add to the increasing workforce pressures and related wage negotiations.

1. **Retain income tax concessions so that NFP disability organisations can leverage capital and reinvest surplus for charitable purposes**

NFP disability organisations cannot easily attract equity/risk funding. Within this limitation, the impost of an income tax would further reduce the capital available to develop their services. This is a major issue with the advent of the NDIS which will require significant investment in new business systems to transform a sector which receives block-funding in advance to one which operates on payment in arrears. There is also a need for service development to support increased participation by people with disability in all facets of society. This development requires research and pilot projects which include direct investment from providers.

The dynamic and diverse market required to make the NDIS successful needs NFP disability providers to apply commercial principles and practices, create a surplus and reinvest this in producing optimal social outcomes. It is therefore important that NFP disability providers maintain a tax exempt status for income earned through unrelated commercial activities that are then applied to their charitable purpose.

NDS asserts that it is the purpose rather than the nature of the activity that should determine whether it should be taxed. This principle was affirmed by the High Court in 2008 in the Word Investment case, where it found that a charity’s activity of making a profit was not an end in itself but incidental to a charitable purpose. Moreover, if an income tax is imposed it would coerce organisations to avoid a surplus, which would undermine their effectiveness and charitable purpose.

## To what extent do the tax arrangements for the NFP sector raise particular concerns about competitive advantage compared to the tax arrangements for for-profit organisations?

Tax concessions do not give NFP disability organisations a competitive advantage over other organisations. Tax concessions do enable NFP disability organisations to fairly compete within increasingly open human service markets.

In 2010 the Productivity Commission investigated the effect on competitive neutrality of various NFP tax benefits[[2]](#footnote-2). They found that on balance income tax exemptions are not significantly distortionary as NFPs have an incentive to maximise the returns on their commercial activities that they then invest in their community purpose. The Commission did identify concerns about concessions on input taxes (including FBT) related to hospitals and gaming. These concerns are not relevant to the disability sector.

NDS urges the Treasury to make use of the 2010 Productivity Commission research in determining the answer to this question as the conditions it was informed by have not changed significantly. NDS argues that developments that are occurring in the wider policy environment make NFP disability sector tax concessions even more important for future competitive human service markets. This is true for the NDIS and is evident in the detailed analysis presented in the recent harper competition policy review[[3]](#footnote-3).

NDS recommends that the Government:

1. **Take heed of the findings in the Harper Competition Policy Review which require governments to conserve the value of NFPs in new human service markets**

NDS is broadly comfortable with the proposal to increase consumer choice in human services and through this create more competitive market structures. The NDIS is a leading example of this. However, as recommended by the competition policy review this must be done with caution. Governments must retain a stewardship function; carefully commission human services with a clear focus on outcomes; and encourage diversity of providers, while taking care not to crowd out community and volunteer services.

Governments must be careful when establishing new markets such as the NDIS market. Significant information asymmetry combined with historic underfunding in the disability sector may put NFP disability providers at a disadvantage when competing with large for-profit entrants to the NDIS market. These new entrants can more easily access capital and invest in new NDIS-suitable systems and marketing. The risk is that some good NFP providers will not survive the transition which may prevent a suitably diverse market providing choice to service users.

## What, if any, administrative arrangements could be simplified that would result in similar outcomes, but with reduced compliance costs?

The announcement in the 2015 Federal Budget of a cap on exempt benefits for Meal Entertainment and Venue Hire was unsurprising. NDS does not oppose a cap, but believes the announced cap of $5,000 *grossed up* is too low and that the benefit would be more efficiently provided as an increase to the FBT exemption cap. The administration required to manage the exempt benefit of $5,000 grossed up, against the actual financial benefit received by an employee, is now disproportionate and may mean that organisations no longer provide this benefit. If this occurs, it would erode staff take-home pay.

NDS recommends that the Government:

1. **Retain the value of the exempt benefits for Meal Entertainment and Venue Hire and reduce compliance costs by raising the FBT exemption cap.**

While some use of the Meal Entertainment Allowance is extravagant, advice provided to NDS indicates that most usage by community services is within a modest band of $4,800 to $5,500 a year (actual expenditure). In recent years, more organisations are making the benefit available to their employees as a method to attract and retain staff in a low-paid sector where demand for services (and therefore workers) is growing. To retain the value of the benefit, prevent its misuse and reduce administration and compliance costs, NDS recommends that the value of the Meal Entertainment Allowance should be added to the current FBT exemption $30,000 cap, increasing it to around $40,000 grossed up value per employee.

## What, if any, changes could be made to the current tax arrangements for the NFP sector that would enable the sector to deliver benefits to the Australian community more efficiently or effectively?

The building workforce pressure for the disability sector could partly be addressed through enhancing FBT concessions.

NDS recommends that the Government:

1. **Index the FBT concessions to help NFP disability organisations address increasing pressure to attract an effective workforce**

The cap on FBT must be regularly adjusted with inflation. The real value of the $30k limit (grossed up nominal value per employee) continues to erode, despite a commitment at the time of its introduction in 2001 to provide regular adjustment. We suggest that initially, any savings from the new cap on exempt benefits for Meal Entertainment and Venue Hire be reinvested in the sector through raising the FBT cap, and this should be followed by yearly indexation.

1. **Calculate the Fee-Help (HECS) repayments on the salary not the grossed up amount that includes FBT gains.**

Currently the Australian Tax Office factors in the grossed up amount a salary (including an added take home benefit from FBT) to determine HECS repayment amounts. For example, if your salary is $66,000 per year but you gain $16000 FBT you have to make a payment on $80,000. This can partially defeat the purpose of offering FBT exemptions and attracting trained workers to the NFP disability sector.

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**Contact:** Dr Ken Baker

Chief Executive

National Disability Services

Ph: 02 6283 3200

Mob: 0409 606 240

[ken.baker@nds.org.au](mailto:ken.baker@nds.org.au)

**National Disability Services** is the peak industry body for non-government disability services. Its purpose is to promote and advance services for people with disability. Its Australia-wide membership includes 1100 non-government organisations, which support people with all forms of disability. Its members collectively provide the full range of disability services—from accommodation support, respite and therapy to community access and employment. NDS provides information and networking opportunities to its members and policy advice to State, Territory and Federal governments.

1. Productivity Commission 2010, *Contribution of the Not-for-Profit Sector*, Research Report, Canberra [↑](#footnote-ref-1)
2. Ibid (Chapter 8) [↑](#footnote-ref-2)
3. Harper, I. 2015. The Australian Government Competition Policy Review: Final Report, Canberra. [↑](#footnote-ref-3)