



MELBOURNE  
SYDNEY

**Partners**  
Mark M Leibler AC  
Henry D Lanzer AM  
Joseph Borensztajn AM  
Leon Zwiher  
Philip Chester  
Ross A Paterson  
Stephen L Sharp  
Kenneth A Gray  
Kevin F Frawley  
Zaven Mardirossian  
Jonathan M Wenig  
Paul Sokolowski  
Paul Rubenstein  
Peter M Seidel  
John Mitchell  
Ben Mahoney  
Jonathan Miner  
John Mengolian  
Caroline Goulden  
Matthew Lees  
Genevieve Sexton  
Jeremy Leibler  
Nathan Briner  
Jonathan Caplan  
Justin Vaatstra  
Clint Harding  
Susanna Ford  
Tyronne McCarthy  
Teresa Ward  
Christine Fleer  
Jeremy Lanzer  
Bridget Little  
Gia Cari  
Jason van Grieken  
Elyse Hilton  
Jonathan Ortner  
Stephen Lloyd  
Scott Phillips  
Gavin Hammerschlag  
Shaun Cartoon  
Damien Cuddihy  
Dorian Henneron  
Rebecca Zwiher  
**Consultant**  
Jane C Sheridan  
**Special Counsel**  
Sam Dollard  
Laila De Melo  
Emily Simmons  
Bridgid Cowling  
Rosalie Cattermole  
**Senior Associates**  
Liam Thomson  
Bianna Youngson  
Kaitlin Lowdon  
Stephanie Campbell  
Claire Stubbe  
Briely Trollope  
Laura Cochrane  
Rachel Soh  
Greg Judd  
Ben Friis-O'Toole  
Ely Bishop  
Raphael Leibler  
Gabriel Sakkal  
Mark Macrae  
David Monteith  
Rebekah French  
Gisella D'Costa  
Lisa Garson  
Vidushee Deora  
Luke Jedynak  
Emily Korda  
Chris Murphy  
Michael Reppe  
Anna Sapountsis  
Jessica Thrower  
John Birrell  
Rob Deev  
Caitlin Edwards  
Jessica Elliott  
Simone Gould  
Alexandra Harrison-Ichlov  
Andrew Low  
Claire Southwell  
Luise Squire  
Ari Bendet

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**By E-mail**

charitiesconsultation@treasury.gov.au

Director  
Not-for-profit Unit  
Individuals and Indirect Tax Division  
Treasury  
Langton Cres  
Parkes ACT 2600

Your Ref

File No. 01-1920726

**Partner**  
Joey Borensztajn AM  
Direct 61 3 9229 9639  
jborensztajn@abl.com.au

**Lawyer**  
Jessica Wills  
Direct 61 3 9229 9880  
jwills@abl.com.au

Dear Sir/Madam

**Submission in relation to *Distribution Guidelines for ancillary funds***

**Introduction**

- 1 Thank you for the opportunity to provide a submission in relation to Treasury's consultation on possible policy changes regarding distribution guidelines for ancillary funds (**Distribution Consultation**).
- 2 Arnold Bloch Leibler (**ABL**) has an extensive charity law practice. We advise a broad range of charitable and not-for-profit organisations regarding, for example, governance, constitutional, and commercial issues. We also advise on philanthropy and charitable giving, including on establishing special purpose philanthropic entities, private and public ancillary funds and charitable trusts. We are actively engaged in developing the legal landscape for the charity and not-for-profit sector.

**Issues for discussion**

**Issue 1: Accumulating funds to support large projects**

- 3 While we recognise that relief from the requirement to satisfy minimum annual distribution requirements in service of a longer-term accumulation strategy may benefit many ancillary funds, this issue is not one directly relevant to our client base.
- 4 Accordingly, we have no substantive comments on this issue for discussion or the related prompt questions, but otherwise welcome the flexibility accumulation concessions would grant to many ancillary funds.

**Issue 2: Flexibility in transferring assets between ancillary funds**

- 5 This submission wholly endorses creating flexibility for ancillary funds to transfer assets between themselves. We see this flexibility as having significant positive impact for many of our clients, donors and recipients alike, and especially item 1 deductible gift recipients (**item 1 DGRs**) connected to schools, sporting clubs and community organisations, as well as museums, for the following key reasons:

- (a) **(aids strategic accumulation)** by permitting private ancillary funds (**PAFs**) to make distributions to public ancillary funds (**PuAFs**), in particular those PuAFs established to centralise donations from a diverse donor base and strategically fund a group of item 1 DGRs over an extended period, PAFs could make distributions which meaningfully contribute to the long-term financial plan of a group.

Earlier sections of the Distribution Consultation discuss accumulation of funding to support large projects, and the importance of facilitating ways in which a PuAF could strategically maintain its corpus to consolidate a higher value targeted impact distribution for a specific project in place of small incremental distributions made simply to comply with minimum annual distribution thresholds. Creating flexibility between ancillary funds to make distributions to one another goes hand in hand with enabling higher value targeted impact distributions for a specific project.

The imperative of a PuAF in this context – supporting a group of item 1 DGRs - is to consolidate donations and make calculated distributions for specific projects or purposes, enabling the greatest amount of flexibility for the group to decide how best and most impactfully to allocate funding. This also avoids duplicative administration costs for those recipient item 1 DGRs.

This intimate understanding of the operation and needs of the group as a whole, rather than individual entities, is not information a donor is privy to. Without the flexibility to distribute funds to a PuAF in this context, PAFs are denied the opportunity to benefit from and participate in the strategic planning of the broader group and the many efficiencies of utilising a PuAF as the umbrella conduit for an item 1 DGR 'group'.

- (b) **(provides vital flexibility)** ancillary funds by their implicit nature are conduit funders to item 1 DGRs that grant donors a tax deduction in anticipation of the distribution of their donation to the ultimate recipient item 1 DGRs.

A key motivator for establishing an ancillary fund is that a donor may be provided with a tax deduction for their donation in the short-term, but the ancillary fund is provided with immense flexibility to determine when and where to direct that donation. Enabling ancillary funds to transfer assets in certain situations, in particular from PAFs to PuAFs, merely builds on this defining feature of an ancillary fund.

- (c) **(enables sophisticated investment)** by reason of the requirements for a PuAF to:

- (i) solicit donations from the public; and
- (ii) operate under the governance of a board the majority of which comprises persons responsible to the public,

PuAFs are well suited to attract and manage a large corpus and develop sophisticated large-scale investment and accumulation policies which harness the diverse capabilities of their board members. The necessary time and resources invested to develop these complex administrative and operational systems are not accessible to all ancillary funds (in particular small PAFs) nor are they reasonable expenses (both in terms of time and resources) when considered relative to a small revenue PAF.

Accordingly, PuAFs often utilise sophisticated infrastructure to increase the efficiency and effectiveness of their distributions and PAFs able to make distributions to PuAFs could benefit in maximising the impact of their

distributions. As mentioned above, this also cuts down on duplicate administrative costs across multiple item 1 DGRs eroding donor contributions.

### Transfers to count towards minimum annual distribution

- 6 In relation to the examples provided below, we consider that:
- (a) ancillary fund to ancillary fund transfers should count towards satisfaction of the transferor ancillary fund's minimum annual distribution requirement;
  - (b) onwards distribution of funds received from an ancillary fund by the transferee ancillary fund to the ultimate item 1 DGR beneficiary should not count towards satisfaction of the transferee ancillary fund's minimum annual distribution requirement (to avoid double counting); and
  - (c) a 4–5-year cycle in which to make onwards distribution from the transferee ancillary fund to the ultimate item 1 DGR would be appropriate, if not a greater period in certain circumstances, so as not to fetter the accumulation and flexibility benefits.

### Sector examples

- 7 Example 1: **(School)** ABL acts for a School which acts as trustee for the following entities:
- (a) School Building Fund – endorsed as an item 1 DGR;
  - (b) Scholarship Fund – endorsed as an item 1 DGR;
  - (c) Public Library – endorsed as an item 1 DGR; and
  - (d) Public Ancillary Fund – endorsed as an item 2 deductible gift recipient.

Indeed, ABL acts for many schools which adopt this type of structure, comprising some or all of the aforementioned item 1 DGRs.

In particular, the PuAF here was established to facilitate long-term strategic support for each of the item 1 DGRs which serve purposes beneficial to the students at the School, including establishing endowment fund.

Fundraising initiatives by the School routinely direct donors to make donations to the PuAF so the School has maximum flexibility to allocate funding for specific initiatives over an extended period of time depending on short and long-term needs.

Currently this PuAF is unable to accept donations from PAF donors, who must make distributions directly to item 1 DGRs. Of note, in 2021 approximately 40% of donations to the School group of item 1 DGR entities were from PAFs. Permitting these PAF donors to distribute directly to the PuAF would provide the extensive advantages set out in paragraph 5 above to the School, and in this case in particular permit the PuAF full flexibility to allocate funding strategically amongst the various item 1 DGR entities on a needs basis now and in future and hold a component for endowment. Of note, ultimately all relevant funds will flow from the PuAF to School group item 1 DGRs, so the net impact is the same.

- 8 Example 2: **(Public Museum)** ABL acts for both a Public Museum (endorsed as an item 1 DGR) and a PuAF established for the singular purpose of providing funding to the Public Museum. Indeed, ABL acts for at least 3 Public Museums and PuAFs which operate in this way.

The PuAF collects donations which form an endowment fund for the current and future funding and operations of Public Museum, one that is invested strategically to maximise corpus and distributed as and when required by the Public Museum for ongoing operations and specific projects.

Of note, on average over the last 5 years approximately 24.5% of donations received are from PAFs (and accordingly receipted by the Public Museum). Permitting PAF donors to distribute directly to the PuAF would provide the extensive advantages set out in paragraph 5 above, and in this case in particular permit the PuAF to serve as a true endowment fund for the Public Museum.

In our experience, the control and resources of a PuAF which funds a Public Museum make the PuAF the ideal holder, investor and manager of the relevant corpus. In this context, permitting the PuAF to receive distributions from donor PAFs gives the PuAF a desirable amount of flexibility to manage funding independently of the Public Museum, providing a long-term and somewhat independent perspective on how to best serve the interests of the Public Museum.

- 9 Example 3: (**Community Organisation**) ABL acts for a PuAF established to support a range of charitable institutions (predominantly Public Benevolent Institutions) operating in New South Wales.

The PuAF acts as a central strategic planner and fundraiser for these various organisations which creates considerable administrative efficiencies for the item 1 DGRs which receive the ultimate distributions.

Given the significant market reputation of the PuAF, donors without insight into the operations of the not-for-profit sector trust that when they make donations to the PuAF they are contributing to a longstanding credible philanthropic effort.

Of note, while in previous years (2010 – 2015) PAF donations totalled less than \$1m and approximately 10% of total donations received, in recent years this has dramatically increased to approximately \$4m and 30-35% of donations being 'raised' from PAFs and accordingly receipted by the recipient item 1 DGRs rather than the PuAF. Permitting PAF donors to distribute directly to the PuAF would provide the extensive advantages set out in paragraph 5 above.

- 10 Example 4: (**Sporting Club**) ABL acts for the philanthropic arm of a number of AFL clubs, which may comprise Public Benevolent Institutions, Harm Prevention Charities and other item 1 DGRs established to support community initiatives from year to year.

Again, a PuAF is established in these contexts to facilitate long-term calculated support for each of the related club item 1 DGRs and centralise donations from extremely large donor pools comprising thousands of team supporters and corporates. The AFL clubs note that the number of large donors making donations via PAFs is increasing year on year.

Given the size of the donor pool and significant community reach of these clubs, the PuAFs utilise significant resources to structure long-term fundraising initiatives as well as develop strategic plans for the club's philanthropy and community impact. Permitting PAF donors to distribute directly to a PuAF in these circumstances would provide the extensive advantages set out in paragraph 5 above.

**Questions**

- (a) *(Question 7) Is there a concern if a PAF transfers assets to a PuAF given the latter has a lower minimum distribution rate?*

No. In all examples provided above funds received will ultimately, in the short or long term, be used and applied by the relevant PuAF for that purpose. In any case, in our experience most of our clients routinely exceed the minimum annual distribution thresholds year on year.

- (b) *(Question 8) To address the risk of churning of funds between ancillary funds with different accounting periods, should the existing prohibition on transferring assets if any have been received from another ancillary fund with the two previous years apply to such transfers?*

If this question intends to raise a concern about churning arising via multiple ancillary fund to ancillary fund transfers, we agree that this should be generally prohibited. As clear in the examples provided above, we envisage singular PAF to PuAF transfers before distribution to the ultimate item 1 DGR recipient being the most relevant and beneficial ancillary fund transfer for our clients and should not be subject to a two-year limit.

- (c) *(Question 9) Should any ancillary fund be able to transfer assets to any other ancillary fund, or should transfers be limited, for example a PAF may transfer to a PuAF but not the other way around?*

Based on the above, we are most interested in obtaining flexibility for PAF to PuAF transfers, but in some instances PAF to PAF transfers should also be permitted (i.e. for example, family divisions).

- (d) *(Question 9.1) Should the existing prohibition on moving assets contributed, either directly or indirectly, by the public from a PuAF to a PAF apply to these transfers?*

Based on the examples we have provided, we do not see this prohibition as being overly restrictive on the actions of most ancillary funds. With that said, we do have one client (and related enquiries being considered by the ATO at present) who is facing difficulty due to this prohibition, and removal of the prohibition in that context would be appropriate. Perhaps this is best dealt with on a case-by-case basis.

- (e) *(Question 10) Should a fund require the Commissioner's consent before transferring assets?*

Assuming the Distribution Guidance issued by the Treasury includes clear prescriptive instructions on permissible transfers, requiring Commissioner consent prior to each ancillary fund to ancillary fund transfer would be administratively burdensome, particularly in relation to annual giving which applies in relation to examples 1, 2 3 and 4 above.

- (f) *(Question 11) Who should be required to ensure the receiving fund distributes an amount equivalent to the value of the transferred assets: the giving fund or the receiving fund?*

The receiving fund.

- (g) *(Question 12) Would the benefits to receiving funds of receiving additional resources be outweighed by the costs of administering the transferred assets?*

The sector examples we have provided above contemplate receipt of distributions from PAFs by large-corporus PuAFs with sophisticated administration processes already in place which are able to manage these funds and related conditions applying to these funds. In these circumstances, the benefit to receiving funds from PAFs would certainly outweigh the costs of administering those funds.

- (h) *(Question 13) What consequences should apply if the receiving fund does not distribute to type 1 DGRs an amount equivalent to the value of the transferred assets? For example, should an administrative penalty be imposed on the trustee of the fund?*

We agree that an administrative penalty should be imposed and is appropriate in the circumstances.

- (i) *(Question 14) Should a fund require the Commissioner's consent before transferring assets? Should the receiving fund require consent?*

Assuming the Distribution Guidance issued by the Treasury includes clear prescriptive instructions on permissible transfers, requiring Commissioner consent prior to each ancillary fund to ancillary fund transfer would be administratively burdensome.

Depending on what conditions (if any) are imposed on the recipient ancillary fund as to treatment of an ancillary fund distribution, it may be worthwhile considering whether the recipient fund needs to consent to receipt of distributions from ancillary funds at all, either specifically in relation to each distribution or generally in relation to distributions from PuAFs or PAFs or both.

## Conclusion

- 11 In summary, we welcome the proposals set out in the Distribution Consultation and take this opportunity to thank the Government for giving us the opportunity to provide feedback on the proposals. In particular, we see the possibility of creating flexibility for ancillary funds to transfer assets between themselves having immense beneficial impact on our clients and the broader not-for-profit sector.

If you would like to discuss this submission further, please contact Joey Borensztajn AM or Jessica Wills on **03 9229 9639**.

We consent to this submission being published on the Treasury website.

Yours sincerely



**Joey Borensztajn AM**  
Partner



**Jessica Wills**  
Lawyer