Law Council
OF AUSTRALIA

Legal Practice Section

Deductible Gift Recipient Reforms

The Treasury

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About the Law Council of Australia

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The Law Council advises governments, courts and federal agencies on ways in which the law and the justice system can be improved for the benefit of the community. The Law Council also represents the Australian legal profession overseas, and maintains close relationships with legal professional bodies throughout the world.

The Law Council was established in 1933, and represents 16 Australian State and Territory law societies and bar associations and the Law Firms Australia, which are known collectively as the Council's Constituent Bodies. The Law Council's Constituent Bodies are:

- Australian Capital Territory Bar Association
- Australian Capital Territory Law Society
- Bar Association of Queensland Inc
- Law Institute of Victoria
- Law Society of New South Wales
- Law Society of South Australia
- Law Society of Tasmania
- Law Society Northern Territory
- Law Society of Western Australia
- New South Wales Bar Association
- Northern Territory Bar Association
- Queensland Law Society
- South Australian Bar Association
- Tasmanian Bar
- Law Firms Australia
- The Victorian Bar Inc
- Western Australian Bar Association

Through this representation, the Law Council effectively acts on behalf of more than 60,000 lawyers across Australia.

The Law Council is governed by a board of 23 Directors – one from each of the constituent bodies and six elected Executive members. The Directors meet quarterly to set objectives, policy and priorities for the Law Council. Between the meetings of Directors, policies and governance responsibility for the Law Council is exercised by the elected Executive members, led by the President who normally serves a 12 month term. The Council's six Executive members are nominated and elected by the board of Directors.

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The Secretariat serves the Law Council nationally and is based in Canberra.

About the Section

The Legal Practice Section of the Law Council of Australia was established in March 1980, initially as the 'Legal Practice Management Section', with a focus principally on legal practice management issues. In September 1986 the Section's name was changed to the 'General Practice Section', and its focus broadened to include areas of specialist practices including Superannuation, Property Law, and Consumer Law.

On 7 December 2002 the Section's name was again changed, to 'Legal Practice Section', to reflect the Section's focus on a broad range of areas of specialist legal practices, as well as practice management.

The Section's objectives are to:

- Contribute to the development of the legal profession;
- Maintain high standards in the legal profession;
- Offer assistance in the development of legal and management expertise in its members through training, conferences, publications, meetings, and other activities.
- Provide policy advice to the Law Council, and prepare submissions on behalf of the Law Council, in the areas relating to its specialist committees.

Members of the Section Executive are:

- Mr Philip Jackson SC, Chair
- Ms Maureen Peatman, Deputy Chair
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- Mr Mark Cerche
- Dr Leonie Kelleher OAM
- Mr Geoff Provis

Acknowledgement

The Law Council is grateful to the Charities and Not-for-profits Committee (**the Committee**) of its Legal Practice Section for preparing this submission.

The Committee was established in March 2016 and comprises leading practitioners in the not-for-profit area from around Australia:

The objectives of the Committee include:

- to engage with financial accountability and taxation laws and policies that affect NFP organisations;
- to promote the administration of justice and the development and improvement of laws and policies affecting NFP organisations; and
- to contribute to the implementation of the Law Council’s International Strategy.

Introduction

1. This submission is made by the Committee in response to the Treasury's Deductible Gift Recipient Reforms Consultation Paper (**Consultation Paper**). The Committee is comprised of lawyers and academics with specific expertise in the area of the law of charity. This submission is informed in part by the practical experience of its members in dealing with the Australian Charities and Not-for-profits Commission (**ACNC**) and the Australian Taxation Office (**ATO**) and the legislation that governs those bodies, on behalf of not-for-profit (**NFP**) clients.

2. At the outset, the Committee wishes to make some general comments about the proposed Deductible Gift Reforms (**DGR**) reforms:

   - As noted in the Law Council's submission of 7 August 2017 to Treasury on the DGR Reform Opportunities Discussion Paper (**2017 Submission**) (see **Annexure A**), the Law Council supports:
     - reform which will provide clarity and consistency in reporting and governance requirements;
     - the reduction of red tape and complexity;
     - access to clear understandable information and education; and,
     - transparency and accountability.
   - The reforms outlined in the Consultation Paper are generally consistent with those criteria and the Committee is therefore broadly supportive of the reforms. However, some important details of the design of the reforms require attention to better accord with the criteria.
   - In some areas there is also a lack of clarity about the precise details of the design and its administrative implementation and the Law Council would be particularly keen to discuss these areas if it would help to elaborate on our submissions below.
   - As noted in the 2017 Submission, there are likely to be issues given the differing meanings in ITAA97 of government agency and in the *Charities Act 2013* (Cth) (**Charities Act**) of government entity. If the definitions are not consistent, some entities may fall through the gaps – not meeting the definition of government agency under the ITAA97, but constituting a government entity under the Charities Act. Amending the definition of government agency is beyond scope. However, that may be a more widely effective reform than the alternative of providing an additional circumstance in which the Commissioner may provide an exemption (see paragraph 25 below).
   - The Law Council notes that transparency and accountability will be improved by including more entities on the ACNC's public register (as a result of many non-charity DGRs becoming registered charities). However, transparency and accountability would be best supported by providing (on the one register) similar information to the public on all DGRs, including specifically listed DGRs, DGRs granted an exemption under the proposed reforms and government entities. We strongly encourage Treasury to give this further consideration and to ensure that at least for all DGRs granted an exemption, such information is included on the ACNC's register.
   - While it is outside the scope of the Consultation Paper, requiring most non-government entity DGRs to be charities should reduce the impact of any future transition to the Not-for-profit Sector Tax Concession Working Group's

suggestion that all charities be made DGRs.[1] The Committee accordingly encourages Treasury to give further consideration to this recommendation.

3. The following summarises the Committee's more specific comments on the proposed reforms.

   (a) On the requirement for DGRs to register as charities:

   - Consultation Question 1: The eligibility criteria for the transition arrangements are clear, but the transition arrangements themselves need to be clarified. In particular, it is unclear by what precise date entities need to amend their governing documents and be fully compliant with the ACNC Act requirements. It is also unclear precisely what administrative approach will be adopted after that date.

   - Consultation Question 2: Twelve months should be a sufficient period for the transition, provided that entities are contacted and given support before 1 July 2019. That is because most member-based entities will need to use their AGM in the second-half of 2019 to gain member approval for amendments to governing documents.

   - Consultation Question 3: Yes, in the interests of reliability, the ACNC register should indicate whether transition entities have been reviewed by the ACNC.

   - Other issues – registration: The *Australian Charities and Not-for-profits Commission Act 2012* (Cth) (**ACNC Act**) allows registration or revocation of registration to be backdated. The tax legislation does the same for tax concessions such as DGR status or income tax exemption. The transition process needs to take better account of the possibility for backdating. For instance, some entities may discover that they ought to have been endorsed as income tax exempt and may need to seek backdated endorsement. Others may think that they can continue as DGRs as a result of transitioning to charity registration with the ACNC but may then subsequently find out that they have never been charities when the ACNC conducts a review.

   - Other issues – ACNC Act compliance: streamlined transition entities will be registered under the ACNC Act but may not yet have amended their governing documents to enable them to comply with the ACNC Act. The transition arrangements need to extend to this inability to comply during the transition period.

   (b) On the exemption from charity registration:

   - Consultation Question 4: Yes, the eligibility criteria for an exemption are relatively clear although the statements in relation to ancillary funds are not quite correct, as explained further below.

   - Consultation Question 5: The definition of government agency in the ITAA97 and of government entity in the Charities Act differ. Some entities

[1] Not-for-profit Sector Tax Concession Working Group, 'Fairer, simpler and more effective tax concessions for the not-for-profit sector' (Final Report, May 2013) <https://static.treasury.gov.au/uploads/sites/1/2017/06/NFP-Sector-WG-Final-Report.pdf >.

may fall through the gaps, such as some war memorials, libraries, museums and galleries.

- Consultation Question 6: The arrangements generally appear appropriate. However, the reference to 'sufficient internal controls and governance processes' is vague and should be replaced with a clearer requirement. As well, to avoid unnecessary regulatory duplication, we recommend a streamlined exemption process for ancillary fund DGRs which cannot qualify as charities because of the range of DGRs to which they are intended to on-donate.

- Consultation Question 7: An exemption should be able to be reviewed and varied such that if a necessitous circumstances fund was operated by an entity which could not register as a charity that the exemption would cease if the entity became eligible to be registered or if the fund itself became a separate entity eligible for registration with the ACNC.

(c) On abolishing public fund requirements:

- Consultation Question 8: Where a registered charity is a basic religious charity, it is not required to comply with the ACNC governance standards and so removing the degree of responsibility requirement may reduce governance standards for public funds that are or that are operated by basic religious charities. In addition, the Consultation Paper could be clearer that it is not proposing that there be a requirement for any management committee for a public fund (separate from the board or trustees of the charity that is or that operates the public fund) to comply with the ACNC governance standards, in addition to requiring that board to comply with the ACNC governance standards.

- Consultation Question 9: There are a number of issues with the proposed reform, including the interaction with gift accounts; the operation of multiple purpose funds within one public fund; the interaction with the purposes of the operating entity, where a public fund is operated by an entity; the time at which governing rules would need to be amended; the risk of creation of a separate trust rather than a fund; and some matters that require clarification.

- Given the issues with the proposed reform, the Committee suggests an alternative proposal that would achieve the original concept of abolishing public fund requirements, while better providing clarity and protecting integrity. The alternative proposal would involve each DGR category that currently requires a public fund to be amended to refer to a fund or institution rather than a public fund. The gift account requirements would then apply in the same way as they apply for all other DGR categories.

DGRs to Register as Charities

Question 1: Are the eligibility criteria for transition arrangements clear?

4. The eligibility criteria for the transition arrangements are clear, but the transition arrangements themselves need to be clarified. In particular, it is unclear by what precise date entities need to amend their governing documents and be fully compliant with the ACNC Act requirements. It is also unclear precisely what administrative approach will be adopted after that date.

5. The following seems implicit in the Consultation Paper and appears broadly consistent with achieving a transition period and with the ACNC's regulatory approach statement. However, if the following is intended, we recommend that it be stated expressly:

   - Despite the ACNC Act requirements, existing DGRs will not have to amend their governing documents before 1 July 2020.
   - The streamlined transition will involve the ACNC checking that the basic information is completed but the ACNC will not review the governing documents of streamlined transition entities before 1 July 2020.
   - In taking an 'educative approach', the ACNC will, as a matter of allocation of administrative resources, permit charities a short period beyond 2020 to finalise such amendments. It appears that period may be 2 years, but the precise period should ideally be stated. If there are any circumstances in which a grace period will not be provided (e.g. fraud, etc), these should be specified.

6. The information should also make it clear whether the ACNC will be conducting a review of all streamlined transition entities and, if so, the date by which those reviews will occur. At present, the consultation paper implies that reviews will occur by 1 July 2022.

7. The consequences of a negative review of a streamlined transition entity should also be clarified. In particular, the Committee recommends that the 'educative approach' above be applied. We also refer to our comments in paragraphs 18 to 21 on the revocation date.

Question 2: Is 12 months a sufficient transition period for providing the information to register or applying to the ATO for an exemption?

8. Twelve months should be a sufficient period provided the ATO and the ACNC intend to contact the entities affected and provide them with support *before* 1 July 2019.

9. If the transition period is limited to 12 months, it is imperative that the contact commence prior to 1 July 2019, because most incorporated entities and unincorporated associations are likely to present any necessary amendments to their governing documents to members at the annual general meeting. For most member-based entities, annual general meetings take place shortly after the end of the financial year. If preparations have not been made *before* the 2019 annual general meeting, the 2020 annual general meeting is likely to fall *after* the transition period has ended.

Question 3: Is it desirable for the ACNC register to indicate which entities on the register have not been reviewed?

10. Yes. In order for there to be integrity and reliability of the register, any entities which have not been reviewed by the ACNC (or the ATO prior to 2012) should have some indication of this fact. The indication should only be removed once the ACNC has done a full review, which the ACNC will hopefully complete within the two year period referred to in the consultation paper.

Other issues relating to charity registration – date of registration or revocation

11. The Consultation Paper is silent on the ability for registration or revocation of registration to be backdated.

Registration

12. Many of the affected entities will have assumed that they were income tax exempt through their DGR endorsement and will not have understood their potential liability for income tax as a result of not being a registered charity.

13. The information provided to entities should deal with this issue and note the ability of the ACNC to backdate the registration if all aspects, such as the governing documents and pursuit of the purposes, would mean that the entity was entitled to be registered as a charity since 2012 (or date of establishment, if later). Entities wishing to have their registration date backdated will need to subject themselves to a full review and not take advantage of the transitional arrangements. Alternatively, the ATO could state that it will not pursue any of these entities for unpaid taxes, at least until after the ACNC has conducted the full review (e.g. prior to 1 July 2022).

14. Once these entities are notified that they should have been registered as a charity in order to access income tax exemption they will be naturally very concerned as to their potential exposure to unpaid taxes, fines and penalties.

Revocation

15. The streamlined transition process requires entities to apply for charity registration by 30 June 2020. At some time after 30 June 2020, the ACNC may determine that an entity is not eligible to be registered as a charity. Potentially, the ACNC could backdate that decision to whatever day the entity applied under the streamlined process in the period 1 July 2019 to 30 June 2020.

16. The transition provisions should clarify that even if revocation is backdated to a day earlier than 30 June 2020, the entity retains its DGR status until the end of 30 June 2020.

17. Further, the transition obviously creates some uncertainty for donors. What if a donor makes a donation to an entity that is reviewed in January 2022 and determined never to have been a charity so that its registration is revoked from the date of application – say 1 July 2019? The ATO practice has generally been to permit deductions for unrelated third parties even where retrospective revocation results in an entity (retrospectively) not being a DGR at the time of the donation (see e.g. the minutes of the National Tax Liaison Group for 17 December 2010). It is suggested that certainty should be provided to donors to streamlined transition entities.

18. Such certainty should at least be provided at the level of an express statement from the ATO about the manner in which it intends to administer the transition. In keeping with the rule of law, it would, however, be preferable for such certainty to be provided in a binding form. The Commissioner's remedial power (*Taxation Administration Act 1953* (Cth) division 370 of schedule 1) seems suited to these circumstances and could permit the Commissioner to determine a modification to division 30 of the *Income Tax Assessment Act 1997* (Cth) (**ITAA97**) by way of making a legislative instrument.

Other issues relating to charity registration – compliance with the ACNC Act

19. Streamlined transition entities will be required to comply with all ACNC Act requirements as registered charities, albeit the consultation paper suggests that affected DGRs will not be required to report to the ACNC. If entities are truly to have until 30 June 2020 to get their affairs in order in terms of meeting the eligibility

requirements to be a charity and to maintain charity registration, ACNC Act requirements should not necessarily apply until 1 July 2020. For example, governance standards 4 and 5, in particular, may require an entity to amend the composition of its board/controllers or to amend its governing rules.

20. It is suggested that a transitional provision apply, akin to that in subdivision 45-D of the *Australian Charities and Not-for-profits Commission Regulation 2013* (Cth), so that governance and external conduct standards do not apply until 1 July 2020, where the entity is precluded from meeting those standards by its governing rules.

Exemption from Charity Registration

Question 4: Are the eligibility criteria for the exemption from charity registration clear?

21. Yes, the eligibility criteria for an exemption are relatively clear although the statements in relation to ancillary funds are not quite correct. Ancillary funds that are registered as charities may distribute to item 1 DGRs that are registered charities or that are government entities which would be charities if they were not government entities. There are also a number that were 'grandfathered' at the commencement of the Charities Act which are registered charities and able to make grants to any item 1 DGR.

22. Currently an ancillary fund can be registered as a charity if its purposes allow the fund to benefit item 1 DGRs that are registered charities or which are government entities that would be charitable if not a government entity. Therefore it is better to state that ancillary funds that wish to distribute to DGRs that are not charitable will need to apply for an exemption.

23. There is a typographical issue in table 4 circumstance 2 – the second paragraph should make it clear that the DGR was established to further charitable purposes. The reference to furthering the entity's 'not-for-profit purpose' is too vague.

24. In table 5 circumstance 3, the words 'cannot or' should be deleted.

Question 5: Are there circumstances that would not be captured under the proposed circumstances?

25. As identified in paragraph 2, the definition of government agency in the ITAA97 and of government entity in the Charities Act differ. Some entities may fall through the gaps, such as some war memorials, libraries, museums and galleries. If an existing DGR is a government entity for the purposes of the Charities Act, but not a government agency under the ITAA97 that should at least provide an additional circumstance in which the Commissioner may provide an exemption.

26. Otherwise, the Committee believes that all of the relevant circumstances have been covered with the Commissioner's discretion.

Question 6: Are the arrangements for the Commissioner's discretion appropriate and sufficient?

27. The arrangements generally appear appropriate. However, the makes the following additional comments:

- The reference to 'sufficient internal controls and governance processes' is relatively vague. To better accord with the rule of law, the Committee recommends creating a more certain requirement. This could be done while still maintaining flexibility to deal with differences in size and activities. The principles-based ACNC governance standards provide an example of such an approach.
- It is unclear precisely how the legislative instrument setting out additional compliance matters is to be made including whether the Commissioner will be empowered to make the instrument. The Committee also queries what the breadth of compliance matters is intended to be, and suggests that, it is relatively narrow, a legislative instrument may not be required.
- Exemption circumstance 4 contemplates ancillary fund DGRs with purposes (that preclude them from charity status) of providing funds to specifically listed DGRs, government entity DGRs and non-government, non-charity DGRs that have been granted an exemption. Given that extensive governance and reporting requirements are already in place for ancillary funds and that money can only be distributed to entities that have already been subject to vetting by government or that are themselves government entities, it is unclear why a second layer of vetting is required of the ancillary fund. To reduce unnecessary regulatory duplication obligations (another ACNC Act object), the Committee recommends that such ancillary fund DGRs be automatically entitled to an exemption from charity registration, or at least a streamlined exemption application process.

28. In relation to the reporting requirements, we suggest that the information provided should be made available to the public in a similar fashion to the information on the ACNC register. This would be consistent with the ACNC Act object of maintaining, protecting and enhancing public trust and confidence in the Australian not-for-profit sector and with the intention of the ACNC Act, as partially endorsed by the ACNC Legislation Review Panel, of applying this object to NFPs beyond charities, including ITAA97 division 30 non-charity NFPs.

29. We note that if a public fund may have multiple DGR categories, it may not be possible to break down the expenditure for administration attributable to each DGR category.

Question 7: Are there any circumstances where an exemption should be time limited?

30. An exemption should be able to be reviewed and varied such that if a necessitous circumstances fund was operated by an entity which could not register as a charity that the exemption would cease if the entity became eligible to be registered or if the fund itself became a separate entity eligible for registration with the ACNC.

Abolishing Public Fund Requirements

31. The government announcement of 5 December 2017 stated that 'public fund requirements will be abolished.[2] The Consultation Paper refers to the abolishment of *certain* public fund requirements:

[2] Hon Kelly O'Dwyer, Minister for Revenue and Financial Services (Cth), 'Reforming administration of tax deductible gift recipients' (Media Release, 5 December 2017) <http://kmo.ministers.treasury.gov.au/media-release/114-2017/>.

- a majority of responsible persons to manage the public fund is no longer required; and
- a half measure – a separate bank account is no longer required for each public fund but there must still be a separate bank account for one or multiple public funds.

32. The Committee supports the removal of these requirements but queries why the intended reform has been watered down. The Committee supports the abolition of the public fund requirements as previously announced. This can be achieved in a manner which will:

    - maintain integrity for tax deductible gifts;
    - provide consistency with other categories of DGRs which do not currently require a public fund, but which may nevertheless have multiple purposes. For example, DGR item 4.1.7 (an institution that would be a PBI, but for the fact that it also promotes the prevention or control of diseases in human beings or that it also promotes the prevention or the control of behaviour that is harmful or abusive to human beings);
    - provide consistency and clarity of the application of the gift account provisions in section 30-130 of the ITAA97;
    - clarify when endorsement for multiple DGR categories is permissible.
    - ensure separate trusts are not created rather than funds; and
    - remove confusion by use of the term 'fund' for institutions.

33. There are a number of issues with the proposed reforms set out in the Consultation Paper which have not been addressed and which respond to question 9 of the Consultation Paper. The Committee comments on these issues below and then sets out an alternate proposal.

34. In response to question 8 relating to abolishing the requirement for management by a committee with a degree of responsibility to the general community, see paragraphs 49-50, 53(d) and 54 below.

Issues with the proposed public fund reform

35. Public funds can be established and maintained by operating entities for the specific DGR purposes or established as trusts and seek DGR endorsement as a whole. The Consultation Paper appears to mainly address entities seeking endorsement for the operation of a public fund, and not where the public fund is the operating entity and the whole entity is endorsed as a DGR. Greater clarity is required between these two types of public fund, as there seems little reason to treat public funds endorsed as a DGR for the whole entity any differently from other categories of DGRs endorsed as a whole entity.

Fund or institution

36. Public funds which are endorsed as a whole (and do not sit within an operating entity) often operate as institutions as they may actively fundraise or provide support and assistance other than passively provide money to their beneficiaries, such as some necessitous circumstances funds or scholarship funds.

37. Items 2.1.8–2.1.9A refer to the fund conducting the activity of providing religious instruction or education in ethics. This activity is more like an institution than a fund.

38. There is some lack of clarity and consistency as to the use of the word ‘fund’ in these contexts. Given these institutions can be endorsed as public funds, perhaps the word 'fund' is no longer appropriate.

Public fund and gift account?

39. Section 30-130 of the ITAA97 requires a gift account to be established in certain circumstances. As all DGRs are required to be able to identify gifts and income generated from those gifts in the event of a winding up or revocation of DGR status (section 30-125(6) of the ITAA97), effectively all DGRs must have a gift account, even if they are not subject to section 30-130. The current laws and policy are not clear as to the interplay between gift accounts and public funds. Our understanding has been that where a public fund only receives gifts it will also be a gift account but where it receives income other than gifts or money received from those gifts, the entity must also have a gift account.

40. The reform proposal does not explain whether a public fund which receives money other than tax deductible gifts needs a gift account. The Consultation Paper assumes the public fund is only receiving tax deductible gifts:

> *… the entity can choose to either use a single public fund to solicit tax deductible donations … or establish a separate public fund for each general category.*

41. It is unclear how a public fund should set up its banking and accounting arrangements to satisfy section 30-130 or section 30-125(6) if it is receiving other income, particularly if it is a fund for multiple DGR categories.

42. It is unclear if there is a difference between a public fund and a gift account.

43. From a policy perspective regarding ensuring the integrity of tax deductible gifts, since, from 1 July 2019, all DGRs, other than government entities, must be charities or operated by charities, or obtain an exemption which will require adequate governance standards, why should some DGRs require gift accounts and some require public funds? We submit this distinction is no longer required and, further, is confusing and cumbersome, providing unnecessary regulation.

Multiple funds within one public fund?

44. The Consultation Paper proposes one public fund with multiple purposes (analogous to sub funds, which a number of public ancillary funds currently operate). This would require amendments to all the public fund DGR categories which currently require ‘a public fund maintained for the purpose of …’. Some categories currently require the public fund to be established and maintained *solely* for the stated purpose (e.g. items 2.1.8–2.1.10).

45. The Australian disaster relief fund, developed country disaster relief fund, and war memorial funds have a two-year limit on their ability to receive tax deductible funds which will need to be covered in the public fund governing documents so as to note DGR status may continue for some DGR categories but not others after the defined time limit.

46. It is not clear whether this option of one public fund with multiple DGR purposes is permitted where there is no operating entity. For example, the Committee queries whether a multi-purpose trust be established with no principal purpose but just a number of public fund categories. Currently this could only be done through a public

ancillary fund but a school, for example, may wish to establish one trust which holds the funds for the school building fund, scholarship fund and a necessitous circumstances fund or a disaster relief fund. The Consultation Paper makes it clear that a single public fund within the school as an operating entity could be established but can the public fund be in a separate trust – would the trust be considered the operating entity for the multiple public funds even though it had no other purpose or activity?

Purposes of the operating entity

47. The Consultation Paper incorrectly states that with respect to some DGR categories, an entity must pursue a principal purpose and they 'are generally unable to establish public funds that are unrelated to furthering their principal purposes'.

48. An example was given of Public Benevolent Institution (**PBIs**) and environmental institutions. The statement is true for PBIs, given the ACNC's interpretation that all the purposes of a PBI must be ancillary or incidental to their benevolent purpose. However for environmental entities, the other example given, there is no such restriction, and the purposes other than the principal purpose can be unrelated. This is the case for many other categories of DGRs.

Managing Committee

49. The Consultation Paper refers to a requirement to appoint a managing committee for the public fund. There is only a requirement to appoint a managing committee if the board of the entity does not have a majority of responsible persons. By removing the requirement for a majority of responsible persons, the board of the entity can manage the public fund.

50. The Consultation Paper lacks clarity as to whether there is an additional requirement for charities to establish a separate managing committee for a public fund and to ensure the committee members meet the ACNC governance standards. The Committee assume that this is not intended to be in the ITAA97 but Treasury is relying on the existing ACNC Act, in which case it should be clarified that ultimately the registered charity must ensure the board of the public fund (if it is a separate entity and endorsed as a whole) or the board of the operating entity of the public fund (whether or not there is a separate managing committee to the board) complies with the ACNC governance standards.

Governing rules required for endorsement

51. The Consultation Paper states:

> *… once the ATO has endorsed the entity, the entity can choose to either use a single public fund to solicit tax deductible donations under all the general DGR categories for which it has been endorsed; or establish a separate public fund for each general category. If an entity chooses to use a single public fund, the entity would update the governing document for its public fund to reflect the general categories it is endorsed under …*

52. However, as a matter of practice, in order to obtain endorsement for any DGR category, the ATO will require to see the governing documents for the public fund to ensure it contains the appropriate DGR purposes, not for profit clause, and dissolution clause. Therefore an entity would need to make the decision as to a

single public fund or multiple public funds prior to seeking endorsement from the ATO, rather than the order of events suggested in the consultation paper.

Table 7 – Public fund requirements

53. In relation to table 7 setting out the revised requirements we comment as follows.

(a) **Requirement 1** is in fact two requirements:

- the public must be invited to contribute; and
- the fund must operate on a not for profit basis.

It needs to be clarified whether the public must be invited to contribute to a public fund endorsed under multiple categories in general terms or specifically to each sub-fund set up for a different DGR category?

(b) The components set out in **requirement 2** raise the following issues:

- The rules could inadvertently establish a separate trust rather than a fund. Requiring the fund to have its own separate governing rules, which set out its specific purposes and include the dissolution clause could amount to the creation of a separate trust. Wording will need to be included to make it clear it is not intended to be a trust and the funds belong to the operating entity, or the ITAA could recognise that unless clearly intended to be a separate trust, public funds will not be regarded as trusts for tax purposes.
- It should not be a requirement for the fund's governing rules to be separate from the operating entity – this should be optional as it is currently (i.e. either separate or within the operating entity's governing rules). The Committee notes as well that where there is not an operating entity and the fund is being intentionally set up as a trust for endorsement as a whole, then the words 'separate to the entity' have no application.
- If there are to be multiple DGR purposes in one public fund, presumably there will need to be an appropriate dissolution clause for each DGR purpose.

(c) **Requirement 3** is also multiple requirements:

- account separately for donations made for each DGR purpose;
- deductible gifts to be kept separate from non-deductible funds;
- separate bank account for the fund and clear accounting procedures; and
- receipts issued in the name of the fund.

A fund for multiple DGR purposes must be able to separately account for donations made to each DGR purpose and be able to separately identify the gifts – which is the requirement of a gift account under s 30-130. Though not stated in the Consultation Paper, a single purpose public fund must also meet this requirement. The Consultation Paper assumes both that the public fund is being operated by another entity *and* that it will only receive gifts. As this is not

always the case, the Committee suggests that there needs to be an explanation of what is proposed in these other scenarios.

If the fund has multiple DGR purposes, requirement 3 suggests that there will be one name for the fund, not for separate DGR purposes (or sub funds) and this one name will be on the Australian Business Register (**ABR**) and receipts will be issued in the name of the fund. However, if donors are making a donation for a particular DGR purpose, they will want to know that purpose has DGR endorsement and that it has been recorded for that purpose by the entity, therefore each sub fund for a DGR category will need to have its own name, recorded on the ABR, and receipts should be made in the name of the sub fund.

There is a requirement to have a separate bank account for the fund but it is unclear why this is necessary and it is unclear whether the bank account can include income other than gifts raised for that DGR purpose. Requiring a separate bank account also heightens the risk (discussed above) that a public fund might be treated as a separate trust.

(d) **Requirement 4** requires the managing committee members to comply with the ACNC governance standards. Where a managing committee is established as a sub-committee of the board of a registered charity, the charity is not required to ensure they comply with the ACNC governance standards. The charity is required to ensure the board members comply with the ACNC governance standards only. It is unclear if it is intended that this requirement is to be an addition to the ACNC requirements so that a charity would need to ensure any sub-committee managing a public fund needs to meet the governance standards, in addition to the board of the charity.

54. Where a registered charity is a basic religious charity, it is not required to comply with the ACNC governance standards, or to provide certain information to the ACNC. Removing the requirement for management by a committee with a degree of responsibility to the general community may therefore reduce governance standards for public funds that are or that are operated by basic religious charities.

Example 1

55. The Committee notes the following issues with Example 1:

- Item 1.1.3 relating to a public fund for the purpose of providing money for hospitals must have already been established prior to 1963, under the special conditions.
- A single public fund is established but as the DGR purpose for each must be stated and each must have a separate dissolution clause. While there does not need to be multiple governing rules, there does need to be recognition in the governing rules of the separation of purposes and the need for separately identifying gifts and distributions with respect to the purposes – this should be explained.
- While there is a single public fund there will need to be two names to identify sub funds for the separate DGR purposes and endorsements and to enable separate receipting and accounting for integrity purposes and to satisfy donor concerns – this should be explained.
- The example does not refer to the bank account but the Committee assumes that a separate bank account will be required for the fund – this may be

difficult for the bank and donors where the donor wants to specify the name of the sub-fund rather than a generic name for a multi-purpose fund.

- The example refers to separately accounting for donations made to each DGR purpose – the interplay with section 30-130 of the ITAA97relating to gift accounts needs to be clarified.
- The last paragraph of the example refers to the 'governing board of the public fund'. However, the context of the example is a registered charity being the operating or sponsoring entity – this entity is required to ensure the board complies with the ACNC governance standards. There should not be a requirement for a separate governing board for the public fund.

Alternative Proposal

56. While the Committee strongly supports the proposal to abolish the public fund requirements in principle, there are a number of issues that need to be clarified. The Committee believes the original concept of abolishing the public fund requirements can be achieved while retaining integrity for tax deductible donations as follows.

57. Each of the categories which require a public fund should be amended to refer to a fund or institution. There is no need to distinguish these categories from any other category by the term 'public fund'.

58. The requirements for a gift account can apply. There is no reason to distinguish these DGR categories from those not requiring a public fund. If a gift account offers sufficient integrity for some DGR categories, then this requirement should be sufficient for all DGR categories.

59. As there is no requirement for a separate bank account for a gift account, it is not clear why that requirement is necessary for these categories of DGRs. At most the requirement for a separate bank account could apply only where the fund or institution is not endorsed as a DGR as a whole and a registered charity, so that the need for a separate bank account applies only where the fund or institution is operated by a registered charity. Though this may also be unnecessary, provided that the funds can be, and are, adequately tracked by the operating entity.

60. When the regulation of the DGRs which are currently maintained on registers are transferred to the ACNC, the public fund requirements for the registers other than the register of approved organisations for a developing country relief fund can be abolished by endorsing the whole entity as a DGR. The current way these entities are endorsed for the operation of a public fund is confusing and unnecessary given the operating entity and the public fund must have the same principal purposes. The DFAT approved organisations are different as the operating entity can have wider purposes than the public fund.

61. The gift account for an entity with multiple DGR purposes will need separate names for each DGR sub-fund and a separate listing on the ABR under that name and under the ABN of the operating entity.

62. A decision needs to be made as to whether an entity can be established with multiple DGR purposes and receive multiple DGR endorsements. Perhaps the multiple purpose gift fund should only apply where there is an operating entity with broader purposes to just the DGR purposes. For example, could an entity be established to award scholarships, relieve financial necessity of people in necessitous circumstances, provide disaster relief to Australians and developed countries and support public ambulance services? Currently in order to have one

trust for multiple categories, a public ancillary fund would need to be established and then separate entities for each of the different categories.

63. Basic religious charity DGRs do not have to comply with ACNC governance standards. Consideration should be given to retaining some management committee degree of responsibility requirements while this remains the case.

Other suggestions

64. It is a welcome move to enable multi-category DGRs and the Committee would encourage Treasury to consider broadening this aspect of reform.

65. It is also noted that the rationale for removing the responsible person requirement focuses on the difficulties faced in regional and rural Australia in finding appropriate 'responsible persons'. In light of this recognition, Treasury is also encouraged to remove this requirement from public ancillary funds which disadvantages community foundations in particular in rural and regional areas.

Contact

66. For further comment or clarification on any of the matters raised in this paper please contact Jennifer Batrouney QC, Chair, Charities and Not-for-profits Committee on (T) 03 9225 8528 or at (E) Jennifer_batrouney@vicbar.com.au.