



Australian Conservation Foundation

Submission on Draft Research Report
Contribution of the Not-for-Profit Sector
Productivity Commission (October 2009)
Australian Government

November 2009

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1. Background

ACF welcomes the opportunity to make this submission on the Draft Research Report of the Australian Government's Productivity Commission on the *Contribution of the Not-for-Profit Sector (Draft Report)*.

ACF is a national, community-based environmental organisation that has been a strong voice for the environment for over 40 years, promoting solutions through research, consultation, education and partnerships. We work with the community, business and government to protect, restore and sustain our environment.

Both through its own activities and involvement in sectoral representative bodies including the National Roundtable of Nonprofit Organisations (NRNO) ACF has a longstanding interest in the policy setting affecting the Not-for-Profit (NFP) Sector and has been a regular contributor to the debate on these issues.

ACF welcomes the Draft Report as a timely recognition of the importance and contribution of the NFP sector in Australia and as a significant contribution to the reform of a range of issues of critical importance to it. These reforms, in parallel with other current Government initiatives such as the National Compact, can do much to enhance the effectiveness and contribution of the sector.

2. Summary and outline of ACF submission

We note that in recent years the policy and regulatory setting for the NFP sector has been the subject of numerous inquiries, reviews and submissions with little in the way of substantive reforms to show for these efforts. Notably, less than a year ago, the Senate Standing Committee on Economics concluded a substantial review of policy and regulatory issues affecting the sector (**STEC Review**).¹ It is ACF's hope that policy choices made in response to the Draft Report will take the outcomes of these previous processes into account, noting the substantial resources that the sector has invested in them over time.

This submission does not address every point of substance raised by the Draft Report or reiterate in detail points that have been made on a number of occasions previously. Rather, this submission is focussed primarily upon those issues raised in

¹ Senate Standing Committee on Economics: *Disclosure regimes for charities and not-for-profit organisations* (December 2008). Report (**STEC Report**) available at http://www.aph.gov.au/Senate/committee/economics_ctte/charities_08/report/index.htm

the Draft Report of direct daily importance and concern to ACF as a medium sized and nationally focussed environment NFP. It also offers some observations on NFP financing based upon ACF's own experiences and those of other NFPs with which it enjoys a close working relationship. To summarise our response and recommendations:

Summary of Recommendations		
#	Topic	ACF Response
1.	Appropriate legal forms (DR 6.1)	ACF is supportive of a new Cth. incorporated association supported by a regulatory regime that borrows appropriately from existing State/Territory incorporated associations legislation and the Corporations Act. The approach should be proportionate and should facilitate efficient (and non-compulsory) migration to the new form.
2.	Reducing unnecessary compliance burdens (DR 6.2)	Draft Recommendation 3.3 should be amended to reflect the need for the COAG reform agenda to pursue a broader reform agenda. While fundraising regulation is a critical area, the agenda should also cover a broad range of tax and other regulatory schemes that are inconsistent, duplicative and/or disproportionately burdensome, including electoral laws.
3.	Statutory definition of charitable purposes (DR6.3)	ACF is strongly supportive of a statutory definition of charitable purposes. The definition must enshrine the legitimacy of non-partisan engagement by NFPs with government, policy and law reform processes and commercial activities conducted in support of charitable purposes. It should also allow charitable institutions or funds to confer "private benefit" in the context of community development or financing activities in recognised lower socio-economic areas.
4.	Consolidating Commonwealth regulation (DR 6.4)	ACF is strongly supportive of a new national Registrar for regulation of the sector.
5.	Simplifying tax endorsement (DR 7.1)	ACF is supportive of a single national application process with mutual recognition. ACF is generally supportive of tax concessions as a key vehicle for governmental support to the sector.
6.	Expansion of gift deductibility (DR 7.2)	ACF is strongly supportive of an expansion of DGR eligibility. Current categories of eligibility and also rules applicable to gift deductibility are unduly restrictive.
7.	Planned giving (DR 7.3)	ACF is strongly supportive of initiatives to promote a broader understanding of the benefits of planned philanthropic giving, including associated tax benefits.
8.	NFP access to capital (DR 7.4)	ACF endorses the establishment of a cross-sectoral working party to explore obstacles to, and opportunities for, enhanced access to capital by the sector.
9.	Government/sector compacts (DR 13.1)	ACF agrees that compacts between governments and the sector must be supported by concrete plans and monitoring and evaluative processes.
10.	Office for Not-for Profit Engagement (DR 13.1)	ACF strongly supports the establishment of a senior departmental resource to drive sector reform.

Our submission addresses and is structured around the following draft recommendations made in the Draft Report:

Recommendation in Draft Report	Para of ACF Submission	Topic
<i>Smarter regulation of the NFP Sector</i>		
6.1	3.2	Providing for appropriate legal forms
6.2	3.3	Reducing unnecessary compliance burdens
6.3	3.4	Statutory definition of charitable purposes
6.4	3.5	Consolidating Commonwealth regulation and improving transparency
<i>Realising funding opportunities for the sector</i>		
7.1	4.1	Simplifying processes for and improving effectiveness of tax endorsement
7.2	4.2	Scope of gift deductibility
7.3	4.3	Promotion and support of planned giving
7.4	4.4	NFP financing
<i>Building stronger, more effective relationships for the future</i>		
13.1	5.1	Government/sector compacts
13.2	5.2	Supporting effective relationships and driving change

3. Smarter regulation of the NFP sector

3.1. Overview

ACF shares the Productivity Commission’s overarching concern that the NFP sector is very poorly served by the current regulatory architecture.

Despite the scale of the NFP sector’s contribution to Australian society, both economically and more broadly, reform of the sector regulatory environment has consistently played second fiddle to reform efforts in other sectors.²

We agree that COAG’s “Principles of best practice regulation” reproduced in the Draft Report represent a useful framework for assessing the appropriateness and effectiveness of regulatory regimes.³ By most recent assessments, key planks of the NFP sector regulatory architecture perform poorly when measured against the criteria in this framework.

We agree there is an urgent need for reform at State and Commonwealth levels to address these shortcomings. ACF recommends that reform efforts should reflect the following three thematic priorities:

² “Economically significant” NFPs alone are estimated to have contributed ~\$43 billion to Australia’s GDP in FY2009-07. An imputed estimated additional \$14.6 billion was added by volunteers in the sector in FY2006-07. See ABS statistics quoted in the Draft Report; p.XXVI

³ Draft Report p. 6.7

- increased clarity, consistency and harmonisation across jurisdictions, including mutual recognition based upon single and conclusive assessments of status/eligibility in one jurisdiction;
- reducing numerous processes currently duplicated across separate regulatory regimes and regulators; and
- reducing or eliminating regulation where the demonstrated public interest benefit (or risk addressed) is not commensurate with the cost of compliance.

With this broader context in mind we have set out below our comments on specific reform recommendations made in the Draft Report.

3.2. Providing for appropriate legal forms

Draft Productivity Commission Recommendation 6.1

The Australian Government should establish a Commonwealth incorporated associations legal structure for not-for-profits. The new legal structure would assist not-for-profits, in particular those operating across state and territory boundaries, that do not wish to be companies limited by guarantee but wish to be incorporated at the Commonwealth level.

Australian governments should ensure that incorporation legislation is amended to allow not-for-profits to migrate from one form of legal entity to another and to migrate between jurisdictions. State and territory governments should continue to reduce unnecessary compliance requirements for incorporated associations.

3.2.1. ACF response to recommendation

ACF agrees in-principle with the recommendation to establish a new Commonwealth incorporated associations legal structure for NFPs. A new form of entity, when teamed with an appropriate legislative operating regime and a dedicated sector regulator, could address a number of shortcomings arising from the current choices of legal form available.

A company limited by guarantee will often not be an ideal option given the complexity and length of the *Corporations Act 2001* (Cth) (**Corporations Act**) and the inappropriateness of many of its provisions for a company that is not carried on for profit and does not have a share capital.⁴ On the other hand State and Territory incorporated associations legislation has lagged behind developments

⁴ The fact that a company limited by guarantee is regulated for many purposes under the Corporations Act as if it is a public company, poses compliance burdens and costs that can be disproportionate taking into account public interest concerns and resources available to smaller NFPs. See The Allen Consulting Group (2006) *Improving Not-For-Profit Law and Regulation: Options Paper*; Chapter 4; available at <http://www.allenconsult.com.au/publications/view.php?id=314>

in modern governance practices and lacks sufficient guidance on key issues such as duties and obligations of office holders that are more comprehensively dealt with in Chapter 2D of the Corporations Act. There is a need for a legal form that borrows appropriately from each of these regimes. The choice and forms of legal entity available to the sector and their key features need also to be better communicated to the sector.

While a new Commonwealth entity should be available for NFPs that wish to incorporate at the Federal level, given the management and administrative resources potentially involved, migration to this form should not be compulsory for existing NFPs.

ACF recommends that in borrowing appropriately from other models, the legislative regime supporting the new entity should:

- adopt a proportionate approach to regulation reflective of the level of management and financial resources available, including tiered reporting and other key obligations based upon size/resources;
- better reflect modern governance practices and requirements than does current State/Territory incorporated associations legislation, including more detailed guidance on the obligations and duties of management board members borrowing where appropriate from the Corporations Act; and
- not operate to preclude those NFPs having a “Federal” governance structure (eg. an advisory Council constituted on a proportional representation basis) to continue with such a structure, subject to there being an identified Board (or similar) vested with key statutory management responsibilities and duties.

ACF agrees that, in implementing a new Commonwealth entity, Commonwealth, State and Territory Governments should ensure that enabling legislation minimises transaction costs and facilitates efficient migration between forms. For example, an NFP wishing to migrate to the new Commonwealth entity should not be subject to Stamp Duty (or similar taxes) on any re-construction transactions required to migrate (eg. the transfer of assets and liabilities) to the new form.⁵ Similarly, these transactions should not give rise to capital gains or other tax liabilities.

⁵ While charities should be eligible for stamp duty exemptions, as discussed below, a process by which an application for exemption must be made by a charity on an ad hoc basis for each transaction in some States/Territories creates uncertainty as to whether relief will be granted and a significant administrative burden.

3.3. Reducing unnecessary compliance burdens

Draft Productivity Commission Recommendation 6.2

To promote confidence in the not-for-profit sector and reduce regulatory burden, Australian governments, initially through the COAG Business Regulation and Competition Working Group, should:

- *agree to and implement harmonised fundraising regulation and mutual recognition across Australia;*
- *support the development of a fundraising register for cross jurisdictional fundraising organisations, to be administered by the proposed national Registrar;*
- *endorse the adoption by all governments of the Standard Chart of Accounts for reporting by not-for-profits in receipt of government grants or service contracts;*
- *ensure that the Standard Business Reporting initiative be expanded to include reporting requirements by not-for-profits.*

3.3.1. ACF response to recommendation

There appears little controversy that regulation of the NFP sector in Australia is complex, lacks coordination between jurisdictions and imposes a substantial burden upon both the sector and regulators. ACF welcomes the Draft Report's finding that the current state of affairs requires the urgent attention of Governments at both Commonwealth and State and Territory level.

However, ACF believes that the scope of the reform agenda should not be limited to the points listed in Draft Recommendation 6.2 (acknowledging that the Draft Report calls for broader reform generally). While reform of fundraising regulations is a critical and urgent task, a significant burden is imposed on the sector on a daily basis by a number of other regulatory schemes – including Commonwealth, State and Territory electoral laws that are unnecessarily complex, duplicative or inconsistent. The schemes impacting most heavily upon ACF are discussed in further detail in paragraph 3.3.2 below.

ACF recommends that Recommendation 6.2 be amended to broaden the scope of the COAG Working Group remit to include a broader review of regulation of the sector, including Commonwealth, State and Territory electoral laws. The Office for Not-for-Profit Sector Engagement (see paragraph 5.2 below) should be tasked with driving a sector wide reform agenda as an urgent priority.

3.3.2. The scale of the problem

We have set out below examples of particular types of regulation that pose a disproportionate burden upon the NFP sector, particularly those operating nationally or across jurisdictional borders.

Assessment and consequences of charitable status/tax concessions

A 2007 study by the NRNO⁶ identified that:

- there are 15 Commonwealth Acts and 163 State and Territory Acts under which entitlement to a benefit or some legal outcome turns on the charitable purpose or status of an organisation;
- 19 Commonwealth, State and Territory governmental entities are regularly involved in determining the charitable status of organisations and a further 74 entities may be called on to make such determinations from time to time; and
- the processes for determining the charitable status of organisations vary significantly between government agencies with little coordination among agencies within and among jurisdictions, and a high degree of inconsistency and duplication.

For NFPs operating nationally, differing tests for and consequences of, charitable status and different regulators create substantial administrative and management work and uncertainty. For example, an organisation employing staff or dealing with real property in different jurisdictions is faced with different rules, processes and forms applicable to the fundamental question of charitable status and therefore exemption from taxes. These include payroll tax, stamp duty and land tax –Recognition of charitable purpose in one jurisdiction is no guarantee of recognition in another.

ACF agrees with observations made both in the Draft Report and by numerous commentators that tax concession categories, processes and entitlements are unnecessarily complex and burdensome and often discriminate based upon unclear policy objectives. These categories and processes should be simplified with approaches to entitlements based upon sound policy rationale.⁷

While the establishment of a “one-stop shop” for Commonwealth regulation and a new statutory definition of charitable purpose would make a substantial contribution to reform of the sector, meaningful reform will also require a systematic review of legislation at Commonwealth, State and Territory level to implement a coherent approach and to remove inconsistencies and duplications. ACF recommends that the new Office for Not-for-Profit Sector Engagement (see paragraph 5.2 below) be tasked with driving this reform agenda as an urgent priority.

Fundraising laws and NFP disclosure

⁶ NRNO (December 2007) *The assessment of charitable status in Australia: Current practice and recommendations for improvement*.

⁷ Draft Report p.6.34.

As has been acknowledged in the Draft Report, the inconsistency of State and Territory charitable fundraising laws poses considerable challenges particularly for those NFPs wishing to fundraise across jurisdictions and to utilise modern fundraising techniques, including online tools.

In its submission to the Productivity Commission, The Fundraising Institute Australia succinctly summarised the problem as follows:

“The regulatory burdens faced by nonprofit organisations operating across jurisdictions are significant, particularly in fundraising. Due to the varying requirements of state and territory legislation and regulation, it is not possible for a national organisation to run a single national fundraising campaign. In order to comply with various jurisdictions’ regulation, national campaigns must be tailored for each state or territory. This presents a significant drain on resources and capacity for national organisations, which adversely impacts service delivery and operational effectiveness.”⁸

In ACF’s experience, the key areas of inconsistency across the eight State and Territory jurisdictions that pose the greatest practical difficulties, include different:

- tests of charitable purpose and therefore coverage under the relevant State/Territory fundraising regime;
- registration and authorisation renewal requirements, for example some jurisdictions require annual renewals while others adopt longer time periods;
- fundraising authorisation terms and conditions that govern the type and methods of fundraising activities;
- requirements applicable to the engagement by NFPs of commercial fundraising service providers, including inconsistent regimes for regulatory approval of service provider relationships and fee disclosure requirements; and
- fundraising and other periodic reporting requirements.

ACF agrees in-principle with the proposal to establish a national register of authorised fundraisers. However in ACF’s view, meaningful reform would also involve at least national regulatory harmonisation but ideally a single National Fundraising Act (based upon a referral of powers from states and territories to the Commonwealth). In addition to substantially reducing administrative burdens, this approach would reflect the reality that many in the sector

⁸ Fundraising Institute Australia Submission to the Productivity Commission (May 2009); reproduced in Draft Report; p.6.27

undertake cross-jurisdictional fundraising campaigns and use methods (such as internet fundraising) that can pose difficult jurisdictional questions.⁹

From the perspective of donors and grant makers, a number of commentators have identified the limited utility of existing laws on the disclosure of fundraising costs by NFPs.¹⁰ ACF is supportive of measures that would improve the usefulness of reporting by NFPs to their donors and other stakeholders.

However measures to prescribe new standards must be framed in a way that acknowledges:

- the diversity of fundraising sources and methods across the sector. For example, an organisation receiving a significant portion of its funds from Governments and other large grant makers may have lower fundraising costs than an organisation highly dependent upon expensive methods such as face to face recruitment and telemarketing;
- that fundraising strategies may be based upon timing and return on investment assumptions that do align with applicable reporting cycles. For example substantial costs may be invested “up-front” in a fundraising campaign expected to yield results over many years. Costs associated with establishing the campaign may appear high in early reporting years;
- the diversity in organisational outcomes or “outputs” across the sector. For example, not all NFPs are engaged in activities commonly referred to as “service delivery” (eg. treating the ill or providing housing or other human services). While in some cases these types of outcome may be partly amenable to some form of ratio based reporting, for many organisations meaningfully assessing “social returns on investment” can be a more nuanced exercise more suited to narrative based reporting on achievements against mission and purpose than financial ratios;¹¹ and
- that as is the case in any other context, undertaking quality work in the NFP sector requires adequate “administrative” and other support.

While the establishment of uniform accounting standards may assist with questions such as how to account for various costs, it may not adequately address some or all of the issues outlined above. In short, a “one size fits all approach” is unlikely to yield improvements in the quality of material available to all donors and other stakeholders.

⁹ See STEC Report p.98

¹⁰ See for example The Allen Consulting Group (2006) op cit

¹¹ See evidence given by Professor Myles McGregor-Lowndes to the STEC Review. STEC Report p.109

Commonwealth and State/Territory Electoral Laws

For many NFPs, contributing to sound public policy in the furtherance of their charitable purposes is an important part of the organisation's activities. To accomplish their goals, NFPs may find themselves commenting on issues that arise in an election context, and throughout the political cycle they may comment on or refer to the policies of governments, political parties or candidates.

In some cases, the expression of views on what are deemed to be "political" or "electoral" matters may trigger legal obligations under the Commonwealth *Electoral Act 1918* and equivalent separate legislation in each State and Territory. These obligations are triggered because the Act extends beyond disclosure and reporting requirements applicable to political parties and candidates to cover the activities of broad sections of civil society in Australia.

NFPs have three key compliance obligations under these laws:

- inclusion of *authorisation statements* on certain publications that contain "electoral matter" (terminology and precise tests differ between jurisdictions);
- *disclosure of "political expenditure"* if such expenditure exceeds a (relatively low) prescribed threshold that differs between jurisdictions; and
- *disclosure of gifts* exceeding a prescribed threshold (that varies between jurisdictions) that are used to enable such "political expenditure".

Although efforts have been made to harmonise laws nationally, as is the case with laws and regulations on a range of other issues, NFPs are faced with different compliance obligations in each of the eight State and Territory jurisdictions and at Commonwealth level.

As the ACF Paper attached to this Submission highlights, the compliance obligations imposed by these laws are complex and in several respects uncertain.¹² Furthermore, as highlighted by a Bill currently before the Senate that would significantly increase both the compliance burden and penalties for non-compliance, they are subject to frequent change.¹³

ACF agrees with conclusions reached in a Paper recently published by The Centre for Independent Studies that the policy rationale and public interest benefit associated with subjecting the NFP sector to these reporting obligations (originally intended to cover direct participants in the political process ie.

¹² Australian Conservation Foundation (September 2009) *How would 2009 Electoral Act reforms affect charities?* (See the Attachment to this Submission). This Paper covers Commonwealth Electoral Act compliance obligations only. Similar requirements are imposed by equivalent State and Territory laws.

¹³ *Commonwealth Electoral Amendment (Political Donations and Other Measures) Bill 2009*

political parties and candidates) is unclear.¹⁴ This is particularly the case given that NFPs (unlike parties and candidates) are not elected to positions of power as a result of the electoral process. At best the complexity of these laws present substantial compliance challenges for even relatively well resourced NFPs. At worst they potentially undermine effective democracy by discouraging public participation in its key processes, for example by discouraging donations to NFPs because the identity of donors must be publicly disclosed.

In ACF's view, this regulatory regime insofar as it applies to NFPs pursuing non-partisan advocacy activities in support of a charitable purpose does not provide a public interest benefit remotely commensurate with the resources required to comply with it. It is neither "smart" nor proportionate regulation of the sector.

ACF recommends that the Office for Not-For-Profit Sector Engagement (see paragraph 5.2 below) undertake a cost/benefit review of the coverage of the NFP sector's non-partisan charitable advocacy activities under Commonwealth, State and Territory electoral laws.

3.4. Statutory definition of charitable purposes

Draft Productivity Commission Recommendation 6.3

The Australian Government should adopt a statutory definition of charitable purposes in accordance with the recommendations of the 2001 Inquiry into the definition of charities and other organisations.

3.4.1. ACF response to draft recommendation

ACF is strongly supportive of a statutory definition of charitable purpose that reflects contemporary community perceptions of public benefit and the role of civil society in modern society.

ACF is generally supportive of the recommendations of the 2001 Inquiry¹⁵ noting that, in implementation, the statutory definition must recognise the legitimacy of:

- a broad range of non-partisan engagement with governments, policy and decision makers by organisations in furtherance of their charitable purposes. Activities recognised as legitimately in support of a charitable purpose should include promoting or opposing changes to laws, presenting views on issues during elections, participating in government processes (eg. submissions to parliamentary inquiries and other processes) and analysing policies of governments and political parties;

¹⁴ The Centre for Independent Studies (July 2009) *Diminishing Democracy: The Threat Posed by Political Expenditure Laws*; Available at <http://www.cis.org.au/>

¹⁵ See Recommendations of the *Report of the Inquiry into the Definition of Charities and Related Organisations* (2001) and the STEC Report Chapter 8

- commercial activities undertaken in support of recognised charitable purposes. For many NFPs, particularly those who receive little or no Government funding, being able to undertake “commercial” revenue raising activities, is critical to their viability; and
- “private” or “business like” benefits when conferred in the course of community development or financing activities eg. in a recognised low socio-economic region or community.

3.4.2. Further comments

Of arguably greater concern to many NFPs than the compliance burden posed by the broader sector regulatory regime, is the fundamental uncertainty created by reliance upon centuries old law on the threshold question of what purposes and activities are legitimately “charitable”.

Despite the issue of helpful guidance by the Australian Taxation Office (ATO) in 2005,¹⁶ the law remains unnecessarily complex and uncertain and does not reflect 21st century community values. The judiciary has regularly noted the unsatisfactory nature of the situation.¹⁷

“Political” activity

The uncertainty is particularly acute for organisations wishing to engage with governments in non-partisan furtherance of their charitable purposes. This is because the common law has been slow to categorically endorse such activities as legitimate, finding that purposes considered “political” or advocating a change in law or policy are not charitable. The unnecessary complexity and fundamental uncertainty of the law in this area is illustrated by the recent decision of the Full Court of the Federal Court in the *Aid/Watch* case.¹⁸

Non-partisan activities such as promoting or opposing changes to the law, presenting views on issues during elections, participating in government processes (eg. submissions to parliamentary inquiries and other processes) and analysing the policies of governments and political parties are broadly recognised by the community as essential to healthy democratic processes. They are a vital part of charities’ work in addressing not only societal symptoms such

¹⁶ See Taxation Ruling 2005/21 available at:

<http://law.ato.gov.au/atolaw/view.htm?docid=TXR/TR200521/NAT/ATO/00001>

¹⁷ See recently, comments of the Full Court of the Federal Court in *Commissioner of Taxation v Aid/Watch Incorporated* [2009] FCAF 128 at paragraph 9 and of the Administrative Appeals Tribunal of Australia in the same matter [2008] AATA 652

¹⁸ *Commissioner of Taxation v Aid/Watch Incorporated* op cit. Special leave of the High Court has been sought to appeal this decision.

as distress, inequality and environmental degradation but also the underlying causes and ultimate solutions. In the words of one organisation:

“From the perspective of the St Vincent de Paul Society, we would see advocacy as absolutely non-negotiable. It is integral to our charitable purpose. This is not something that we have invented in recent years; it goes to the heart of our founding. In Paris in 1833, our founder made very explicit the principle that we were not simply to give assistance to the poor but to seek out and understand the structures that give rise to poverty and inequality, and to actively advocate to change those structures.”¹⁹

By way of example in an environmental context, the health of wetlands and rivers in the Murray Darling Basin (MDB) area is acknowledged by broad sections of the community as a significant issue of concern. Successfully addressing the symptoms (such as biodiversity loss, loss of social amenities etc) requires a thorough examination of the causes, for example in this context over-allocation of water entitlements in catchment areas. In the process of facilitating solutions that acknowledge different competing interests, environment NFPs such as ACF have been able to make a valuable and broadly recognised contribution to the inter-governmental policy response. ACF and others would simply be unable to participate in these processes if laws applicable to charitable purpose prohibited activities such as commenting upon policy and regulatory issues such as targeted land and water reform, governance structures for the MDB and governmental budgetary allocations for measures including structural adjustment, investment in water saving irrigation infrastructure and water entitlement buy-backs etc.²⁰

“Commercial” activities in support of charitable purpose

The continuing lack of certainty around the extent to which charities are able to undertake commercial activities in support of their charitable activities is also an issue of concern to the sector. For many NFPs, particularly those who receive little or no Government funding, being able to undertake commercial revenue raising activities is critical to their viability.

While the recent decision of the High Court in the *Word Investments* case has provided some welcome clarity on this issue, legislative recognition that commercial activities undertaken in support of charitable purposes is essential.²¹

Conferral of “private” or business like benefits

As outlined in paragraphs 4.2 and 5.2 below, the current NFP policy, regulatory and tax setting is not generally conducive to innovative community development

¹⁹ Dr John Falzon, CEO St Vincent de Paul Society, evidence given to the STEC Review, STEC Report p.84

²⁰ For more information on ACF’s Healthy Rivers Campaign see http://www.acfonline.org.au/default.asp?section_id=17

²¹ *Commissioner of Taxation v Word Investments Ltd* (2008) HCA 55

and social financing approaches. One aspect of this is that the current definition of “charitable purpose” lacks clarity on the extent to which “private” or “business like” benefits can be conferred by an organisation pursuing charitable objectives.²²

ACF recommends that the conferral of such benefits should be permitted when undertaken in support of a recognised community development purpose. For example assistance to, or financing of, a community or individually owned business initiative in a recognised lower socio-economic region or community.²³

3.5. Consolidating Commonwealth regulation and improving transparency

Draft Productivity Commission Recommendation 6.4

The Australian Government should establish a one-stop shop for Commonwealth regulation by consolidating various regulatory functions into a new national Registrar for Community and Charitable Purpose Organisations with the following key functions to promote confidence in the not-for-profit sector:

- *register and regulate Commonwealth incorporated associations, companies limited by guarantee and Indigenous corporations;*
- *register and endorse not-for-profits for commonwealth tax concession status*
- *registration of cross-jurisdictional fundraising by not-for-profit organisations*
- *a single reporting portal for public record corporate and financial information, proportionate to the size and scope of functions of not-for-profit organisations*
- *provision of appropriate governance education*
- *complaints handling*

3.5.1. ACF response to draft recommendation

In the interests of consistent and clear regulation, reduced compliance burdens and effective use of public funds, ACF is generally supportive of these recommendations. ACF is strongly supportive of a regulator vested with dedicated oversight of the sector and of investment in educational resources for the sector.

However the measures outlined in the Recommendation will not alone achieve necessary outcomes without parallel review and reform of the layers of regulation at Commonwealth, State and Territory level (some of which are discussed in paragraph 3.3 above) that pose practical difficulties for NFP organisations large and small on a daily basis. ACF recommends that the new Office for Not-for-Profit Sector Engagement (see paragraph 5.2 below) be tasked with driving this reform agenda as an urgent priority.

²² See the discussion on these issues in TR 2005/21; paragraph 3.1

²³ We have discussed the policy setting for social investment and finance further in paragraph 4.4 below.

As discussed in paragraph 3.3.2 above, any new reporting initiatives or standards for the sector should recognise and acknowledge that a “one-size-fits-all” approach is inappropriate for the sector.

Finally, ACF recommends a wording change to the Draft Recommendation to insert the words “support and” prior to the words “promote confidence in”.

4. Realising funding opportunities for the sector

4.1. Simplifying processes for/improving effectiveness of tax endorsement

Draft Productivity Commission Recommendation 7.1

Australian Governments should recognise the tax concession status endorsement of not-for-profits at the Commonwealth level, and explore the scope for a single national application process for organisations for tax status endorsement, or mutual recognition of endorsement, across all jurisdictions.

4.1.1. ACF response to draft recommendation

ACF is supportive of simplified processes and a single national application process (with mutual recognition).

As a general point, ACF supports the overall system of tax concessions for NFPs and considers it an efficient way to foster development of the sector. In terms of government grants as a potential substitute for tax concessions, ACF views tax concessions as a preferential alternative to grant funding because tax concessions:

- better facilitate NFPs pursuing activities that are independent of the agenda of government, including acting as an independent check and balance upon and source of accountability for governments; and
- can offer lower compliance burdens than grant funding conditions (although as outlined in this Submission and the Draft Report, there is substantial scope for improvement in application and compliance processes associated with current tax concessions).

4.2. Scope of gift deductibility

Draft Productivity Commission Recommendation 7.2

Subject to considerations of affordability, the Australian Government should widen the scope for gift deductibility to include all charitable institutions and charitable funds as endorsed by the proposed national Registrar.

Gift deductibility should continue to be available to other eligible categories which fall outside this scope, such as cultural and environmental organisations endorsed by the proposed national Registrar.

4.2.1. ACF response to draft recommendation

ACF agrees that the scope of gift deductibility should be widened to include all charitable institutions and funds.

4.2.2. Further comments

General

For many NFPs, DGR status is critical to accessing capital. Moreover, statistics referred to in the Draft Report evidencing rapid growth in philanthropic gifts claimed as tax deductions (approximately doubling during the period 2000-01 to 2006-07), highlight the increasing appeal of this to donors as a vehicle for NFP financing.²⁴

ACF shares concerns raised in the Draft Report (and by a number of other commentators over recent years) that the rules and categories for DGR eligibility are unduly narrow and restrictive. Furthermore, detailed rules applicable to gift deductibility can be unnecessarily strict in the application. Rules around the “conferral of benefaction” and the receipt by donors of “material benefit” in exchange for donations can create difficult compliance issues for unwitting donors and NFPs lacking resources to obtain legal advice on subtle differences that can mean the difference between compliance and breach.²⁵

Financing community development – regulatory obstacles

The impact that the restrictive DGR categories have on the broader sector and in particular upon the advancement of social and community welfare has been the subject of broad criticism and is acknowledged in the Draft Report.²⁶

One example we wish to highlight is the negative impact the restrictions place upon organisations that receive little or no government funding and wish to support community development activities. For example, despite the significant socio-economic disadvantage that persists in many Indigenous communities, an organisation wishing to contribute to development activities in those communities is not eligible for DGR endorsement under current criteria on the basis of a community development purpose alone. Furthermore, current rules applicable to income tax exempt endorsed funds operate to prevent funding

²⁴ ATO Data in McGregor-Lowndes M and Newton C (2009) *An Examination of Tax-Deductible Donations Made by Individual Australian Taxpayers in 2006-07*, Working Paper no. CPNS 45, quoted in Draft Report pp.7.17-7.18; available at <http://www.bus.qut.edu.au/research/cpns/publications/>

²⁵ See Taxation Ruling TR 2005/13 *Income tax: tax deductible gifts – what is a gift*; available at: <http://law.ato.gov.au/atoLaw/view.htm?docid=TXR/TR200513/NAT/ATO/00001>

²⁶ Draft Report p.7.22

being used for purposes that confer “private benefits”.²⁷ There is also the lack of clarity (referred to in paragraph 3.4 above) about the extent to which activities that confer “private benefits” can be undertaken within the confines of the general common law definition of “charitable purpose”. As we have outlined, any statutory definition of “charitable purpose” should permit such benefit where supportive of a community development purpose in recognised lower socio-economic regions.

In our view, the regulatory setting should encourage rather than hinder organisations wishing to support the development of local economies (and through this, socio-economic outcomes) in these regions by using innovative financing and/or capacity building approaches in support of individual or community owned for-profit enterprises.

ACF recommends that the joint working party referred to in Draft Recommendation 7.4 be tasked to consider the application of existing laws (including DGR eligibility and those applicable to income tax exempt funds and charitable institutions) in a community development and community finance context with a view to these better facilitating these approaches.

4.3. Promotion and support for planned giving

Draft Productivity Commission Recommendation 7.3

To encourage cost-effective giving, the Australian Government should explore options to promote and support planned giving, especially payroll giving and bequests. Options include increasing the awareness of the tax benefits of giving, and financial assistance and advice to smaller organisations to establish planned giving programs.

4.3.1. ACF response to draft recommendation

ACF is strongly supportive of stronger promotion of both planned giving programs and the tax benefits of philanthropic giving.

4.4. Enhanced access to capital

Draft Productivity Commission Recommendation 7.4

The Australian Government should establish a joint working party made up of representatives of the not-for-profit sector, business, philanthropic and other government to explore obstacles to not-for-profits raising capital and evaluate appropriate options to enhance access to capital by the sector.

4.4.1. ACF response to draft recommendation

²⁷ See Australian Taxation Office NAT 10652 -12.2005 Instructions for Endorsement as a tax concession charity or income tax exempt fund. Available at: http://www.ato.gov.au/content/downloads/n10652-12-2005_proof06.pdf

ACF is strongly supportive of a joint working party approach to evaluating constraints to, and opportunities for, sector financing.

As we have outlined in paragraph 4.2 above, we believe that there are several regulatory/tax impediments to NFP participation in community development programs and financing. In addition to a reform agenda focussed upon removing these impediments, we agree with the Draft Report's conclusions that this agenda should also focus upon how NFP's access to capital can be proactively stimulated, including through an examination of measures adopted in other countries.

4.4.2. Further comments

Whether or not governments participate directly in capitalising NFPs (eg. through matching grants), ACF believes that government has a critical role in creating an enabling environment for seed and growth capital to support social enterprise ventures (both "NFP" and for-profit) not effectively served by traditional government programs or private sector investment.

As the Draft Report has highlighted, debt funding on conventional terms is often unavailable or prohibitively expensive or risky for key stakeholders such as Board members asked to guarantee obligations. Moreover, corporate vehicles currently available to the NFP sector do not facilitate equity capital raising while key regulatory parameters applicable to for-profit vehicles lack the flexibility necessary to adapt to a context in which investment returns are viewed through a different and broader prism than traditional approaches.

In ACF's view Australian governments can and should explore ways in which the policy setting and regulatory environment can foster investment in initiatives that generate social or environmental returns, if not profits in the conventional sense. We agree that the following approaches referred to in the Draft Report are worthy of detailed consideration by the joint working party/new Office for Not-for-Profit sector engagement:

- **New form of "community"/"low profit"/"blended value" incorporated entity:** we agree that the inability of NFPs to directly raise equity finance significantly diminishes the range of capital raising options. Approaches such as **(i)** a cap on earnings distributions; **(ii)** tiered capital structures to better facilitate "gap" financing; and **(iii)** asset locks to protect community benefit; may all be worthy of examination with a view to developing models that better facilitate social investment because they more accurately reflect the

objectives and risk profile of participants, are flexible and have relatively low transaction costs.²⁸

- **Stimulating Community Development Financial Institutions (CDFIs):** the success of overseas examples such as ShoreBank Pacific highlight the critical role that CDFIs can play as an intermediary between social enterprises having a demand for finance and capital markets. This role can span a broad spectrum of activities from business plan related advice to principal lending, debt packaging (eg. securitisation) and other pooled investment products. ACF believes that the growing appetite among the investment community for socially responsible investments (for example in areas such as ecosystem services) will generate increasing demand for CDFIs able to play these roles. We agree that governments should examine how the existing policy/regulatory setting (including prudential and financial services regulation and tax laws) and new initiatives such as competitive funding allocations and government “products” (eg. guarantees) can stimulate the development of CDFIs in Australia.²⁹

In addition we also recommend that broader fiscal approaches to stimulating social investment also be examined. The United States Treasury Department’s *New Market Tax Credit Scheme* permits taxpayers to receive a credit against Federal income taxes for making qualified equity investments in designated Community Development Entities (including CDFIs). This scheme (which has to date invested US\$21 billion in social enterprise projects including social housing and sustainable forestry initiatives) is worthy of examination in an Australian context.³⁰

5. **Building stronger, more effective relationships for the future**

5.1. Government/Sector Compacts

Draft Productivity Commission Recommendation 13.1

Compacts between Australian governments and the sector must be supported by well documented plans of action, including at agency level, if appropriate, and supported by practical measures including monitoring and evaluative processes that give concrete expression to the proposed relationship.

5.1.1. ACF response to draft recommendation

²⁸ See the discussion of the L3C Company (Vermont and Michigan, USA) and Community Interest Company (UK) at p.7.42 and 9.5 of the Draft Report. See also <http://www.blendedvalue.org/>

²⁹ As the Draft Report indicates, the *Community Reinvestment Act* has been highly effective in stimulating social investment in the USA. Existing CDFIs in Australia include Bendigo-Adelaide Bank’s joint venture Community Sector Banking Pty Ltd

³⁰ See http://www.cdfifund.gov/what_we_do/programs_id.asp?programID=5

ACF agrees with this Draft Recommendation. Plans of action and monitoring and evaluative processes are critical to ensure these processes deliver upon their promise. ACF has provided more detailed comments on the developing National Compact to the Department of Families, Housing, Community Services and Indigenous Affairs in the context of the consultation process for that initiative.³¹

5.2. Supporting effective relationships and driving change

Draft Productivity Commission Recommendation 13.2

The Australian Government should establish an Office for Not-For-Profit Sector Engagement within the Prime Minister's portfolio, for an initial term of five years.

The Office would support the Australian Government in its efforts to:

- *implement sector regulatory and other reform and the implementation of the Government's proposed compact with the not-for-profit sector*
- *promote the development and implementation of the proposed Information Development Plan*
- *initially fund and oversee the establishment of the proposed Centre for Community Service Effectiveness*
- *implement the proposed contracting reforms in government funded services*
- *act as a catalyst for the promotion and funding by government agencies of social innovation programs*
- *facilitate stronger community and business collaboration.*

The Office should, through the relevant Minister, report publicly on an annual basis on its achievements.

5.2.1. ACF response to draft recommendation

ACF is strongly supportive of a dedicated and senior departmental resource to drive the reform agenda – at Commonwealth and State and Territory level - so urgently needed by the NFP sector. ACF recommends that the Office be given a broad remit reflective of the scale of reform required and the breadth of the recommendations arising out of the Productivity Commission and other recent review processes.

ACF welcomes the opportunity to make this submission on the Draft Report and would be pleased to discuss this further. Please direct any inquiries to:

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Attachment: Australian Conservation Foundation (September 2009) *How would proposed Commonwealth Electoral Act reforms affect charities?*

³¹ See <http://www.facsia.gov.au/sa/communities/overview/Pages/default.aspx>

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