



9 December 2021

Individuals and Indirect Tax Division
The Treasury
Langton Cres
Parkes ACT 2600

Submitted by Email

Dear Sir/Madam,

Remake of the *Public Ancillary Fund Guidelines 2011*

Philanthropy Australia appreciates the opportunity to make this submission regarding the draft *Taxation Administration (Public Ancillary Fund) Guidelines 2022* (Draft Guidelines).

In doing so, we wish to convey our serious concerns about elements of the proposed changes, specifically in relation the new eligibility requirements for Responsible Persons.

We do not support these changes, and if they were included in the final version of the Guidelines, we would have no choice but to actively oppose their introduction.

Given our sincere wish to continue to work constructively with the Australian Government and the Treasury to enhance the taxation and regulatory framework for giving in Australia, our strong preference is that the issues in the Draft Guidelines be promptly addressed, so as to smooth the process for their introduction.

Further detail about our concerns is provided below.

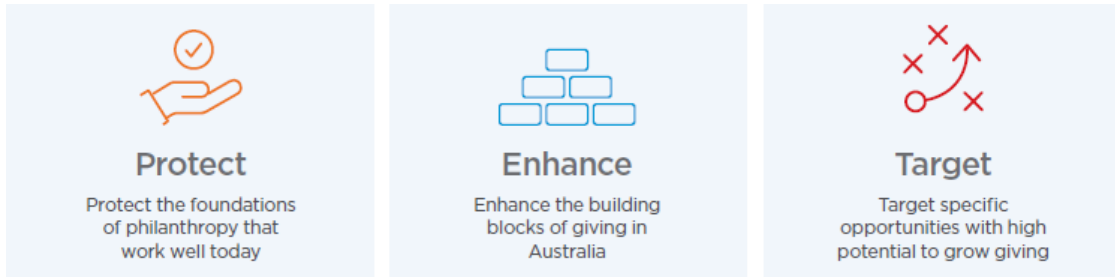
Philanthropy Australia's Focus on Public Ancillary Funds

As the peak body for philanthropy in Australia, our vision is 'a generous and inclusive Australia' and our purpose is 'to inspire more and better philanthropy'.

Our membership includes numerous organisations that use a Public Ancillary Fund (PuAF) structure to facilitate and promote philanthropy, such as community foundations, philanthropic service providers, corporates and wealth management firms. We therefore take a strong interest in the design of the taxation and regulatory framework that applies to philanthropy, including PuAFs.

Our response to the Draft Guidelines is based on engagement with Philanthropy Australia members and also reflects the strategic priorities set out in the *Blueprint to Grow Structured Giving*¹ launched earlier this year, namely the need to protect existing frameworks which work effectively and support giving in Australia.

¹ See: <https://www.philanthropy.org.au/tools-resources/a-blueprint-to-grow-structured-giving/>



We believe that the proposed new eligibility requirements for Responsible Persons represent a substantive change to the existing regulatory framework for PuAFs, which would seriously undermine the viability of PuAFs and the key role they play fostering Australia's culture of giving.

Highly Concerning Changes to Eligibility Requirements for Responsible Persons

A Major Change with Harmful Impacts

A majority of the individuals involved in the decision-making of a PuAF, namely the directors of a PuAF trustee, must be Responsible Persons.

Although the Draft Guidelines do not change this requirement, they do introduce a new substantive change to the eligibility requirements for Responsible Persons, by way of Clause 12(8) of the Draft Guidelines extracted below.

- (8) The *responsible person* cannot be:
- (a) a donor to the fund who has contributed more than [\$10,000] (in total); or
 - (b) a founder of the fund; or
 - (c) a *relative of an individual covered by paragraph (a) or (b); or
 - (d) an *associate of an individual covered by paragraph (a) or (b); or
 - (e) except with the consent of the Commissioner, by written notice, an employee or *agent of an individual covered paragraph (a) or (b).

Although the Draft Explanatory Statement states that this is intended to 'ensure that at least one independent person is involved in the decision-making of each public ancillary fund', as currently drafted the eligibility requirements would impact all Responsible Persons of a PuAF.

It is our understanding that this broader application of the requirement reflects the current policy intent, which is a source of major concern to Philanthropy Australia.

It is often difficult for PuAFs to attract directors who meet the existing requirements and ensure that a majority of directors are Responsible Persons. This is particularly the case with smaller PuAFs that operate in rural and regional areas.

Furthermore, across a range of different types of PuAFs, it is common for these directors to also donate to the PuAF, in many cases exceeding a total amount of \$10,000. The relatives and associates of founders and/or donors may also wish to assist with the governance of PuAFs by taking on the responsibilities of being a director.

In the case of corporate foundations which are structured as a PuAF, founders, associates and employees may also wish to contribute in this way.



Such individuals should not be penalised for their giving or other types of contributions, which is the what the proposed change effectively would do. In doing so, the change also means that PuAFs cannot benefit from the expertise and skills of such individuals, many of whom have extensive governance experience in a diverse range of contexts.

These regulations should not hinder engagement by people who are seeking to actively benefit the community through both their financial resources and their expertise, skills and experience.

Based on consultations with our members, the change would:

- Result in many directors of PuAFs becoming ineligible to be Responsible Persons, and in effect, directors of the PuAF
- Make it much harder to attract new directors who meet the proposed new eligibility requirements, given that such directors are often drawn from the pool of individuals who support the work of the PuAF, including by making donations to it and/or contributing their expertise and skills
- Cause immense governance instability and disruption, distracting PuAFs from their core focus of facilitating and promoting giving for public benefit
- Make it impossible to engage donors in the process of stewarding funds for public benefit, despite those donors having considerable experience and expertise in governance

In the case of some of our member organisations, half of the Responsible Persons of certain PuAFs would become ineligible because of the proposed change. The impacts of this change would therefore be highly detrimental and cause immense instability across the philanthropic sector. At a time that we are looking to grow philanthropy at both a local and national levels, these changes would represent an attack on champions of philanthropy, both individuals and organisations, when their work and contributions should instead be actively encouraged and supported.

A Major Change with No Policy Rationale

We note that no policy rationale has been provided to justify this change, and Philanthropy Australia is not aware of any governance issues which would necessitate this change.

As you may be aware, we are represented on the Australian Taxation Office's (ATO) Not-for-profit Stewardship Group, and we appreciate the commitment shown by the ATO to the effective and proportionate regulation of PuAFs. No relevant regulatory risks have been brought to the attention of this forum that would justify the proposed change.

Although the Draft Explanatory Statement states that the 'provision has been updated to provide greater consistency with similar restrictions applying to responsible persons in the model trust deed', no such restrictions are included in the model deed.

Finally, it is noted that PuAFs, along with Private Ancillary Funds (PAFs), are the most regulated form of charitable entity in Australia. Numerous safeguards already exist to address conflicts of interest, preclude the receipt of private benefits and prevent uncommercial transactions being entered into. These include Clauses 18(3) and 22 of the Draft Guidelines, provisions in the model deed, the requirements in the Australian Charities and Not-for-profits Commission (ACNC) Governance



Standards, and the duties and obligations applying under trust law. In addition, a comprehensive reporting framework for PuAFs exists, to enable oversight of compliance with these requirements.

Recommendation

Based on the points set out above, Philanthropy Australia strongly recommends that the Clause 12(8) of the Draft Guidelines be removed.

Other Significant Matters Requiring Attention

Although the new eligibility requirements for Responsible Persons are the most concerning aspect of the Draft Guidelines, Philanthropy Australia believes that a number of other significant matters also need to be addressed, in order to avoid problematic and possibly unintended consequences.

Clause 22(3) – Reinstating the Word ‘Material’ Before ‘Benefit’

Clause 22(3) of the Draft Guidelines differs from Clause 42 of the existing Guidelines, due to the removal of the word ‘material’ before ‘benefit’. It is not apparent why immaterial benefits should be captured by this Clause, given that by their very nature such benefits are not of any substantive significance.

The absence of the term ‘material’ before ‘benefit’ arguably means actions such as providing directors of a PuAF with sandwiches during a board meeting would represent a benefit that is in breach of the Draft Guidelines. Public recognition of a PuAF by a grantee, following a grant made by the trustee, may be considered a ‘benefit’, and therefore also result in a breach the Draft Guidelines.

Taxation Ruling TR 2005/13, *Income tax: Tax deductible gifts - what is a gift*², focuses on ‘material benefits’, and it is submitted that the Draft Guidelines should do the same. Such an approach also makes sense in terms of the regulatory framework for PuAFs being risk-based and proportionate.

Recommendation

In Clause 22(3) of the Draft Guidelines, the word ‘material’ should be included before ‘benefits’.

Clauses 27(1) (b) and (c) – Including a Reference to Sub-funds In Order to Not Restrict Portability

Portability is an important element of the regulatory framework for PuAFs and also PAFs. In the case of PuAFs, it allows ‘sub-funds’ to be transferred from one PuAF to another PuAF or to a PAF. It also allows for the reverse. This improves flexibility and supports the use of sub-funds as a vehicle for structured giving in Australia, which in turn helps grow our culture of giving.

For example, some donors may establish a sub-fund within a PuAF, and then wish to establish a PAF, and can request that funds contributed to the sub-fund be transferred to the PAF (subject to discretion of the PuAF trustee and the other conditions in place under the existing Guidelines).

² See: <https://www.ato.gov.au/law/view/document?DocID=TXR/TR200513/NAT/ATO/00001>



Alternatively, donors which have established a PAF may find that it is not an effective way to structure their giving, and therefore may wish to wind it up and transfer its assets into a sub-fund within a PuAF.

As currently drafted, Clause 27(1)(c) would mean that where a PuAF has received any assets from any other ancillary fund within the last two years, it cannot transfer the assets of a sub-fund out of it during that period.

This would be a severe limitation that would hinder the operation of existing portability arrangements. It would introduce significant red tape that precludes transferring sub-funds out of a PuAF and also would create a major disincentive to allow sub-funds to be transferred into the PuAF (or created, where a PAF's assets are being transferred into the PuAF for the purposes of creating a sub-fund), given the consequences that would flow from this.

Therefore, the Clause needs to be re-drafted to address this issue, possibly using the following wording:

(c) none of the assets of the public ancillary fund have been received from another ancillary fund during the 2 previous financial years (or where a sub-fund is being transferred, none of the assets allocated to that sub-fund have been received from another ancillary fund during the 2 previous financial years)

There is also an issue with the current drafting of Clause 27(1)(b), which would preclude transferring the assets of a sub-fund out of a PuAF where the PuAF as a whole has not yet met the minimum distribution, even if the donor requesting the transfer has already recommended grants from that sub-fund that meet the minimum distribution and these grants have been made by the trustee of the PuAF.

This could result in considerable delays to transferring the assets of a sub-fund, but without any apparent policy rationale that justifies the delay.

For example, towards the beginning of a financial year, a donor may recommend grants be made from a sub-fund, representing 4% of the assets allocated against the sub-fund at the end of the previous financial year, which turn are made by the trustee of the PuAF. But the PuAF as a whole may take until much later in the financial year to meet its overall minimum distribution. In such a situation, the transfer of the sub-fund will not be able to take place until much later in the financial year.

Decisions regarding portability are at the discretion of the trustee of a PuAF and require the agreement of the Commissioner of Taxation. However, in order to address unnecessary complications arising from how the Clause is currently drafted, a reference should be included which allows transferring the assets of a sub-fund out of a PuAF where grants equal to the minimum distribution have been made from assets allocated against that sub-fund.



Recommendation

In Clauses 27(1) (b) and (c) of the Draft Guidelines, the wording should be amended to ensure that portability is not adversely impacted and can occur in a timely manner.

Conclusion

Philanthropy Australia thanks the Treasury for the opportunity to make this submission. We have raised some significant issues in our submission, and we sincerely hope that these matters can be promptly resolved, so that the proposed *Taxation Administration (Public Ancillary Fund) Guidelines 2022* contribute to growing Australia's culture of giving, rather than having the opposite effect.

Although we accept that broader policy changes are outside of the scope of this consultation process, Philanthropy Australia does again wish to reiterate the need for two related policy changes:

- Addressing current barriers which preclude granting from ancillary funds to other ancillary funds, which means that PuAFs are cut off from the growing pool of funds held within PAFs
- Creating a new DGR category for community foundations, to help further unlock the potential of community philanthropy in Australia and address the major limitations imposed by the current structuring options available for community foundations

We would welcome the opportunity to discuss the matters in this submission further, and are very happy to assist with the more detailed aspects of addressing them. In this regard, please do not hesitate to contact Philanthropy Australia's Director of Policy, Government Relations and Research, Sam Rosevear (sam@philanthropy.org.au, 1300 511 500).

Yours Sincerely,

A handwritten signature in blue ink, appearing to read "Jack Heath".

Jack Heath

CEO

Philanthropy Australia