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LAWYERS

Neumann & Turnour Submission on 'In Australia' Requirements

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1. INTRODUCTION

Neumann and Turnour Lawyers is a Brisbane based law firm which specialises in the area of Not for Profit ("NFP") law. We provide advice to an extensive number of not for profit organisations, particularly charities.

We write in response to the *Tax Laws Amendment (Special Conditions for Not-for-Profit Concessions) Bill 2012* which proposes to reform and standardise the 'in Australia' requirements for exempt entities and deductible gift recipients found within the Income Tax Assessment Act 1997 (ITAA).

For the purposes of illustration, we address the effect of the proposed reforms upon those entities within the NFP sector that are conducting overseas aid relief within what is commonly referred to as an 'auspicing' model. Due to the various charitable endorsements employed within such an arrangement, adopting a focus on such a model enables this submission to illustrate the practical effect of the proposed amendments on a range of charitable entities.

Typically an auspicing model entails an entity which operates a Developing Country Relief Fund (DCRF) under Division 30-80 of the *Income Tax Assessment Act 1997* (Cth) (ITAA) entering into contractual engagements with other charities for the purpose of 'auspicing' those separate charities for the conduct of fundraising. Under that model, the resultant funds are paid to the Developing Country Relief Fund, and then expended in the conduct of various overseas aid development projects. Charities engaging with an entity operating a DCRF under an auspicing model are typically themselves charities, and either:

1. Operate a Public Ancillary Fund which raises donations and then pay those donations to the DCRF; or
2. Do not operate a Public Ancillary Fund, but operate to raise donations which are paid directly by donors to the DCRF.

Whilst it is evident that certain of our prior submissions on the previous April 2012 Exposure Draft have been incorporated in the draft Bill, we remain concerned about the potential effects of the Bill as set out herein.

2. PROPOSED AMENDMENTS TO SECTION 50-50 ITAA

A. Tracing of funds given by an Exempt Entity to another Exempt Entity

Subsection 50-50(4), which requires an exempt entity to ensure that any money, property or benefits it provides to another entity are used 'in Australia', will be highly problematic in operation. When the practical application of such a section is considered, several questions arise that demonstrate the difficulty of its implementation:

1. What is the cut-off-date for ensuring the funds are used in Australia by the recipient? Conceivably, donor entities could be forced to track fund use by recipient entities for years after the date of a gift.

2. As the giving entity has no control over the operations of the recipient, how can the giving entity possibly affirm that the funds will be used in Australia? The comments of Lord Justice Oliver in *Inland Revenue Commissioners v Helen Slater Charitable Trust* [1981] 3 W.L.R. 377, 382 (Court of Appeal), are salient in this regard:

> The Crown's proposition is a startling one; it involves this, that the trustees of a grant-making charity, although they may discharge themselves as a matter of law by making a grant to another properly constituted charity, are obliged, if they wish to claim exemption under the subsections, to inquire into the application of the funds given and to demonstrate to the Revenue **how those funds have been dealt with by other trustees over whom they have no control and for whose actions they are not answerable. Anything more inconvenient would be difficult to imagine**....(emphasis added)

3. If it is determined at a later date that at the date of the supply of funds the recipient entity was recorded as exempt but was not entitled to that exemption at the time of the supply, will the giving entity be entitled to rely on the knowledge it held at the time of the supply, or will it be exposed to the loss of its exemption?

4. The Bill states that existing prescribed entities will be 'grandfathered' and that organisations may be prescribed under Regulation as satisfying 50-50(2) (see 50-51(2)(d)). What is the application of the 50-50(4) where the supplier gives to an prescribed entity that expends the funds outside of Australia? Would organisations fundraising under an auspicing model lose endorsement as an exempt entity for their operations within Australia where they give to another exempt entity that is a prescribed institution under Regulation?

'Provide' vs 'give'

The Bill encompasses the *providing of money, property or benefits*, as compared with the 'giving' of money or property proposed in the April 2012 Exposure Draft. This change renders the clause extremely expansive in operation. What are 'benefits'? Are supplies made under a routine contractual engagement (such as information technology contractors or office equipment service providers) to be taken into account? The April Exposure Draft confined the necessary consideration to *gifts* made to non-exempt entities, and was more workable in this regard.

Proposed solution

The simplest means of resolving these uncertainties is to remove subsection 50-50(4) entirely. However, if the subsection is to remain, the Bill must provide a positive deeming clause in order to remove this uncertainty. Drafting that will address this is as follows, to be inserted as new 50-51(3):

> "(3) An entity satisfies the conditions in subsection (2) (about operating and pursuing its purposes in Australia) to the extent that it provides money or property or benefits to another entity that is an *exempt entity at the date of the provision."

Furthermore, should an exempt entity give to a Developing Country Relief Fund, there is currently no provision in the Bill which states that the donor entity would be deemed to satisfy the 'in Australia' requirements to the extent that the donor's operations comprise that giving. An appropriate further subsection to address this would be new 50-51(4):

"(4) An entity satisfies the conditions in subsection (2) (about operating and pursuing its purposes in Australia) to the extent that it provides money, property or benefits to a fund, authority or institution that is a deductible gift recipient."

B. Regulatory Power

Proposed subsection 50-50(5) provides that the use of certain amounts (including gifts and government grants) may be disregarded, provided that the entity satisfies the precondition that it 'complies with the conditions (if any) prescribed in the regulations for the purposes of this subsection'. The Explanatory Memorandum provides some direction as to these conditions, at paragraph 1.138; however, no certainty is offered. Access to the disregarding provision in 50-50(5) (and the equivalent existing provision, s 50-75) is critical for entities seeking to maintain exempt status where operating an auspicing model.

We are concerned about the potential effect of the delegated legislation further anticipated by the Bill. To leave the conditions unstated in the legislation is to introduce significant uncertainty for the sector. It also delegates the ability to the executive government to effectively frustrate the ability to rely upon 50-50(5). Without sufficient clarity within the legislation itself, the net effect of that delegated power may be the effective frustration of Australia's contribution to overseas development through such private sector engagements. The proposed conditions should therefore be stated in the Bill itself and opportunity should be granted for the making of submissions upon those conditions.

3. PROPOSED AMENDMENTS TO 30-18 ITAA 1997

A. Tracing of funds given by DGR to a non-DGR

The requirements in proposed section 30-18(3) that require an entity to trace funds are unworkable for the reasons stated in our submissions in respect of s 50-50(4) above.

B. Gifts made by a Public Ancillary Fund to a Developing Country Relief Fund

International Affairs Deductible Gift Recipients are exempt from the 'in Australia' requirements under proposed 30-18(5). The 'in Australia' test for Public Ancillary Funds is stated in proposed 30-18(1):

(1) Subject to subsections (4) and (5), a fund, authority or institution satisfies the conditions in this section if:

(a) it is established in Australia; and

(b) it operates solely in Australia; and

(c) it pursues its purposes solely in Australia.

Where a Public Ancillary Fund's operations principally encompass the giving of funds to a Developing Country Relief Fund (DCRF), the requirement that the entirety of the Public Ancillary Funds' operations be taken into account under 30-18(1) may require that the activity of giving to a DCRF is also to be taken into account.

Whilst the DCRF is exempt from the requirements that it operate solely in Australia, the Public Ancillary Fund is not. This introduces the possible interpretation that the overseas use of the funds by the DCRF is to be taken into account in determining the nature of the operations of the Public Ancillary Fund.

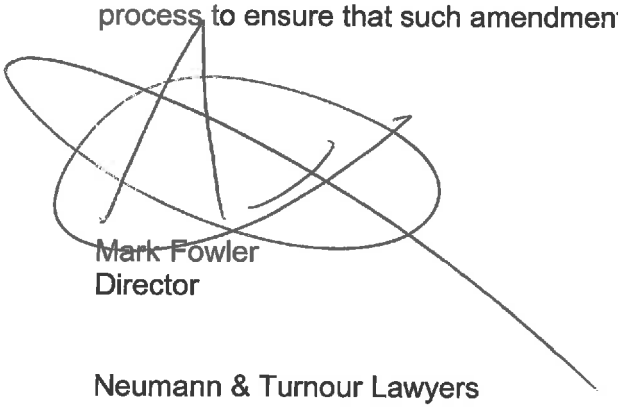
Again, we are of the opinion that a specific legislative presumption must be introduced to remove this possibility. We consider that the following additional sub-section 30-18(8) is required:

> "(8) A fund, authority or institution satisfies the conditions in subsection (1) (about operating and pursuing its purposes in Australia) to the extent that it provides money, property or benefits to a fund, authority or institution covered by section 30-80 (international affairs deductible gift recipients)."

C. CONCLUSION

By way of conclusion, we thank the Committee for the opportunity to make submissions in respect of the standardisation of the special conditions for tax concession entities. For the avoidance of doubt, our submissions should not be considered to express a satisfaction with the proposed amendments. In our opinion, the existing legislative framework is the preferred position.

The current legislation has enabled significant contributions to Australia's overseas aid efforts by organisations conducting auspicing arrangements similar to that described herein. Should any further amendments be proposed, it is requested that the specific engagement of organisations conducting such auspicing arrangements be sought in the consultation process to ensure that such amendments do not inadvertently detract from those operations.



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