Submission to The Hon. Joe Hockey, Treasurer

Submission in response to the Re:think - Tax discussion paper

Better tax system, better Australia

May 2015

Introduction

This submission briefly outlines some of the key issues for Australia's charity and not-for-profit sector in response to the Re:think Tax Discussion paper.

This Community Council for Australia (CCA) submission has been prepared with CCA members (see listing of CCA members, Attachment A) as well as other key organisations working in the broader not-for-profit sector. It is important to note that this submission does not over-ride any policy positions that may be outlined in any individual submissions from CCA members.

CCA has held preliminary consultations with members of the Tax White Paper Task Force and consulted with a broad range of stakeholders in framing this submission.

The fundamental principle of achieving a better Australia through having a better tax system is one CCA strongly embraces. The tax system is not just about an economic exchange, it is part of the fabric of our communities. The provision of tax concessions to charity and not-for-profit organisations has been an important contributing factor in building a strong and resilient Australian community.

CCA appreciates this opportunity to be part of the national conversation and provide input into this area of taxation policy and its impact on charities and not-for-profits.

The Community Council for Australia

The Community Council for Australia is an independent non-political member based organisation dedicated to building flourishing communities by enhancing the extraordinary work undertaken by the charities and not-for-profit sector in Australia. CCA seeks to change the way governments, communities and not-for-profits relate to one another. It does so by providing a national voice and facilitation for sector leaders to act on common and shared issues affecting the contribution, performance and viability of NFPs in Australia. This includes:

- promoting the values of the sector and the need for reform
- influencing and shaping relevant policy agendas
- improving the way people invest in the sector
- measuring and reporting success in a way that clearly articulates value
- building collaboration and sector efficiency
- informing, educating, and assisting organisations to build sustainable futures
- providing a catalyst and mechanism for the sector to work in partnership with government, business and the broader Australian community to achieve positive change.

Our success will drive a more sustainable and effective charities and not-for-profit sector in Australia making an increased contribution to the well-being and resilience of all our communities.

Current situation – the context

The not-for-profit sector

The charities and not-for-profit sector turns over more than $105 billion annually, contributes over $55 billion to GDP per annum, and employs over one million staff (or eight per cent of all employees in Australia). The sector holds over $175 billion in assets, and across the last decade, sector growth has continued at approximately 7% a year, greater than any other industry group.

These figures tell only a small part of the story. The real value of the sector is that these are the organisations at the heart of our communities; building social connection, nurturing spiritual and cultural expression, and enhancing the productivity of all Australians.

The importance of the sector is now being internationally recognised with many governments putting in place measures to increase NFP productivity. Smaller government and bigger community is a common theme, driven in part by savings, but also by a commitment to greater civic engagement and productivity within the NFP sector. The sector itself is beginning to work on productivity as a core issue.

The recent history of the NFP sector is framed by growth and reform, but there are a number of new issues emerging. The level of individual philanthropic giving has levelled out from the high in 2008. The ongoing increase in revenue available to governments is effectively stalling in real terms against a backdrop of increasing demands and higher community expectations. Competition within the sector is increasing, although not always to the benefit of the community.

There have been no less than 15 major reviews, reports and inquiries into the regulation and contribution of the charities and not-for-profit sector since 1995. There are currently a range of initiatives seeking to promote social enterprise; reduce compliance costs for NFP organisations; encourage a diversification of financing options to build a more sustainable funding base; streamline and refine the regulation of NFPs and charities; establish less bureaucratic reporting requirements while building community transparency; increase philanthropy and improve relationships between government and the NFP sector. CCA supports these activities.

The Australian Charities and Not-for-profits Commission (ACNC) is now an effective national regulator. It is the first time the NFP sector has had an independent regulator dedicated to serving their needs and the needs of the community. The ACNC is a positive step towards reducing red tape, supporting transparency, building community trust and enhancing the role of the sector.

The inability of governments to streamline their own regulatory processes, their tendering processes, contract management and programs monitoring has consistently been identified as a major barrier to improving productivity in the not-for-profit sector in Australia. The lack of certainty in the government regulatory environment, funding and contracting processes also undermines performance and ongoing investment in improving outcomes. For the sector to be more effective, these issues must be addressed.

Given the size of the sector and its critical role in our community, the Federal Government can achieve real economic and social benefits if it chooses to strategically invest in strengthening our communities and our NFPs by improving the way it taxes and regulates the sector.

Overview of key issues

1. The purpose of the Australian taxation system

The title of the Tax White Paper is "*Better tax system, better Australia*". CCA believes that all Australians want to live in flourishing communities. While it is important to have a fair, efficient and effective taxation system, the way we tax also has a direct impact on many of the relationships between citizens and within our communities. Our tax system influences the availability of housing and employment, the quality of our education, health care and support services. A good tax system helps create opportunity and promotes public benefit. It supports investment in innovation and creativity, while increasing productivity.

Focusing on economic principles that treat each individual as an economic unit for the sake of developing and implementing an economically sound taxation system will not enable the taxation system to realise its potential to contribute to a better Australia.

CCA supports a national conversation about taxation, but the focus of this conversation should be about the kind of Australia we want to live in rather than simply what taxes we want to pay. Any proposed changes should be meaningfully canvassed with those it will impact on – keeping in mind the fundamental principle of all good interventions – first do no harm.

2. Concessions and public benefit

In the context of considering the Australian taxation system, it is important to note the fundamental difference between a commercial and a not-for-profit organisation is purpose. All charities and not-for-profits are driven by a purpose that has to be about providing a real public benefit. Most commercial entities are primarily about making money.

The fact that a charitable organisation engages in commercial activities does not make them commercial. A local charity in a rural city may run a car wash or car park for the weekend football game as a way of underwriting their charitable purpose. If the organisation engages in promotion of their car park it does not make them an advertising agency, nor does running a car park make them a for-profit business if all the money they raise is directed to their charitable purpose. This small scale, local commercial activity for a charitable purpose is typical of the majority of commercial activities by charities and not-for-profits.

Any suggestion that such activities should be taxed in the same way as commercial activities, ignoring their purpose, would create major problems for charities and not-for-profits, and more importantly, for the communities they serve.

As the tax discussion paper points out, concessions to the charities and not-for-profit sector provides at least $5 billion in tax concessions through various exemptions including FBT, GST, income tax and imputation credit exemptions and concessions.

While the rationale for concessions varies, the fundamental principle informing these concessions is that the purpose of charities and not-for-profits is to provide a public benefit and serve their communities, often in situations where there is market failure and high community need. There is also an acknowledgement that the transfer costs of collecting taxes and then redistributing this revenue back to communities through government bureaucracies represents a significant cost. CCA has considered each of the main concessions separately below:

2a) Deductible gift recipient status (DGR)

CCA has consistently argued that the current system of determining which charities or benevolent organisations should be able to offer tax deductibility to donors is a broken and dysfunctional process. The involvement of five different registers (Australian Charities and Not-for-profit Commission, environmental, harm prevention, international development, art and culture) as well as the Australian Tax Office is complex enough, but the blurring of categories and eligibility makes no sense whatsoever.

Many organisations find the system very complex to understand. The application process is demanding, the time taken to process applications is often more than a year, it can be very costly paying for legal and other experts, and often requires rewording of foundation documents through Annual General Meetings.

It is important to note that application for DGR status rarely changes what organisations actually do, only how they describe it.

The ACNC is working and has the respect of both the charities sector and other regulators. It is time the ACNC took a central role in making recommendations to the ATO regarding DGR eligibility.

As noted in the section below on inequity in the charities and not-for-profit sector, a lot of work and consultation has already occurred in relation to how DGR could work better. The findings of previous inquiries and working parties need to be revisited to enable real reform of DGR in Australia.

2b) Fringe Benefit Tax (FBT)

FBT concessions have been important to many charities, Public Benevolent Institutions (PBIs) and not-for-profits (NFPs) in both attracting and retaining quality staff. For many organisations, this concession has enabled benefits such as a subsidised vehicles or accommodation assistance to be partially underwritten as a component of employee benefits. Where the FBT concessions and exemptions are used in this way, it is often a very important component of employee remuneration. Many in the sector would like to see it increased to enable charities to compete more equitably in employment markets with better resourced government agencies and commercial organisations. For some employees, the FBT exemptions can add 10% to their annual salary package making work in the charitable sector more attractive. At the same time, there are many organisations eligible to access this concession where it is not utilised.

The recent decision to cap meals and entertainment concessions adds increased complexity and compliance costs to what is already an administratively difficult and time consuming system.

CCA understands FBT exemptions are under active consideration for reform. In any change to FBT exemptions, it will be important to acknowledge the importance of this exemption for many organisations and employees in the charities and NFP sector. Options such as income tax rebates and payments to employers to replace FBT exemptions need to be carefully worked through with the sector.

Any changes to FBT concessions and exemptions will also need a significant transition plan allowing time for adjustments to be made in the way employees are compensated in situations where employee benefits are to be reduced.

Regardless of what changes are implemented, it will be very important to maintain the level of support for the sector that current FBT exemptions provide.

2c) Income tax

The basis of income tax exemption is that any income earned by charities and not-for-profits is used for public benefit. Any suggestion that the income producing activities of charities should be subject to income tax is equating income generated for public benefit to income generating private wealth.

In the case of the very large clubs where income is largely derived from hospitality and gaming, the very broad application of the mutuality principle is an area where further consideration may be warranted, especially given the amount of income which is exempt from tax relative to the level of public benefit provided.

2d) GST

GST exemptions offer a tangible benefit for many organisations in the charities and not-for-profit sector. The rationale is clear (public benefit). Administrative and compliance costs are negligible and application of the GST exemption is equitable across different forms of charities and not-for-profits.

GST exemptions available to charities and not-for-profits work well and do not require any review.

2e) Refundable franking credits

Reforms to the dividend imputation system to make imputation credits refundable for some taxpayers were introduced in 2000, creating refundable franking credits. The availability of refundable franking credits does not impose any significant administrative and compliance costs, and addresses distortions which the Industry Commission identified in its 1995 report into Charitable Organisations. They provide over $500 million each year to support charities to deliver public benefit. For some trusts and foundations and charities with significant investments, a significant proportion of all their income is derived through this concession. Any changes which limit or remove the availability of refundable franking credits would have a major negative impact on charities and the important work they do.

There is no rationale to review or consider changes to this important concession.

3. Supporting philanthropy

CCA supports measures to encourage philanthropy in Australia. There are ways to both improve and expand support for citizen involvement in donating and supporting charities.

CCA has repeatedly called for reforms to the pre-tax workplace giving program introduced under the Howard government. At present less than 5% of employees participate in these programs. The potential, as shown by overseas experience, is much higher. CCA believes providing options such as opt out programs (where employees are signed up unless they opt out) and tax incentives for employer matching of workplace giving both have the potential to not only increase workplace giving, but also benefit workplace and communities through increased civic engagement.

4. Housing and taxes

In almost every area of human endeavour, access to stable and safe accommodation is a pre-requisite to realising potential and growing productivity. In Australia, access to affordable housing is clearly a major issue. The tax system has a direct impact on the housing market through negative gearing, land tax, and stamp duties.

CCA believes it is important to consider the impact of all taxation on the housing market, and particularly the most vulnerable or those who cannot afford to participate in what amounts to Australia's most important and widely used wealth ladder – home ownership.

The current tax arrangements do not promote access to appropriate housing across our communities. For example, it seems to be an illogical approach to impose a massive tax on people if they want to sell their existing house and buy another. Stamp duties effectively create a barrier to mobility in the housing market (particularly for those who might otherwise might downsize) serving no real benefit other than to provide revenue to State and Territory governments.

CCA supports a comprehensive review of current taxation arrangements in relation to the impact of existing taxation provisions on housing in Australia.

5. Employment and taxes

The benefit of participation in the employment market cannot be overstated, especially for people more likely to be marginalised. Encouraging employment, even on a part time basis, should be a goal for the taxation system.

CCA believe there is scope to incentivise employment in areas where there is a need (particularly rural and remote communities) for new job creation or for population groups that often face barriers to full employment participation (unskilled youth, disability, mental health etc.).

In considering workplace participation, it is important to acknowledge the vital role played by over five million volunteers in Australia's charities and not-for-profits. For some volunteers, providing tax deductibility for expenses involved in volunteering may be an important enabling concession.

CCA would support a more comprehensive review of current taxation arrangements in relation to the impact of taxation on employment and volunteer participation in Australia.

6. Access to capital

The lack of access to capital with the charities and not-for-profit sector has a very strong negative impact on productivity and effectiveness across the sector. CCA strongly believes there needs to be a freeing up of capital to support the not-for-profit sector.

Unfortunately many banks and other financial institutions have difficulty engaging with or underwriting the not-for-profit sector as risks are not always as easy to identify and quantify, and these risks are often compounded by uncertainty.

Concepts such as impact investing are in some ways only just beginning in Australia. New approaches in this area include government backed social development investment and social bonds, but we still have a long way to go if increased capital is to be made more readily available to address social needs. CCA is part of Impact Investment Australia, working through the G8 and other local and global initiatives to facilitate greater social impact investment based on a more outcomes driven model. CCA has also argued for an NFP bank underwritten by the dead money accounts (unclaimed Superannuation etc.) that could invest in generating increased social benefit.

CCA has identified a number of areas our members believe are important in improving the productivity and competitiveness of the Australian not-for-profit sector through diversifying the sources of capital including reviewing the structural barriers to appropriate investment such as regulations, taxation, legislation and standard definitions that restrict new investment and leveraging of existing capacity within not-for-profit organisations.

A number of developed countries have adopted beneficent taxation regimes to redirect capital into impact investing. The following material drawn from the G8 Social Impact Investing Taskforce (2014) document provides some indications of the kind of regulatory environments that can support the introduction of social impact financing at a larger scale.

In the US, Federal New Markets Tax Credits and the Community Reinvestment Act were designed to increase the flow of capital to poorer parts of the US. Since 2000 over $31.1 billion in new market tax credit transactions have been reported. In 2013 $55 billion was channelled from banks to poorer communities through social investment under the Community Reinvestment Act.

In 2014, the UK Government announced Social Investment tax relief. Individuals can deduct 30% of the cost of their eligible social investment from their income tax liability and may defer capital gains tax charges. These tax concessions can apply to social impact bonds (SIBs), shares or debt investments in eligible social sector organisations. In March 2015, the UK Government announced seven new SIB investment schemes that aim to support social entrepreneurs and help to reform public services (Smith 2015).

In France, every employee is given the choice of including impact investments in their pension savings through ‘fonds d’investissement solidaires dits 90/10’. Assets under management in social investment have grown from €478 million to €3.7 billion in 2014.

Freeing up capital and providing incentives for investment into socially beneficial activities would significantly increase access to capital for charities and not-for-profits. The benefits of such changes would be very significant for the sector, but also provide real benefits to governments and communities.

7. Competitive neutrality

The issue of competitive neutrality has been the subject of various sector reviews and inquiries since 1995. The Inquiry into the Definition of Charity (2000) made the point very clearly that commercial activities should not be used to deny charitable status (recommendation 18).

One of the most telling reasons for making this recommendation was that a commercial organisation and charity involved in the same activity are doing so for two very distinct purposes. The charity is seeking to provide a public benefit and the commercial organisation is seeking to increase the wealth of individual owners.

Perhaps even more importantly from a purely commercial perspective, the Inquiry found that the advantages enjoyed by the charity in terms of tax and other concessions are more than offset by the difficulty most charities experience in attracting capital and investment (see above). The Henry Tax Review in 2008 made the same findings – the commercial benefits of tax and other concessions are negated by public benefit and uneven access to capital.

8. An uneven playing field within the charities and not-for-profit sector

There is no right or prescribed size for a charity or not-for-profit organisation. As a semi competitive market seeking to serve their communities, there are clearly advantages and disadvantages associated with size, scale, replicability and responsiveness to local needs that impact on the viability and effectiveness of each organisation.

While individual organisational factors are one issue that creates an uneven playing field, the taxation environment also provides advantages and disadvantages to different organisations, often without a clear rationale. As the Henry Taxation Review and the Productivity Commission have highlighted, the current taxation and concessions regime applied to charities and not-for-profit organisations is in real need of reform.

There are major issues with the inconsistency of concessions across various charities and not-for-profits. Two organisations doing exactly the same work with very similar governance structures and operations can have entirely different tax status. One organisation may have access to Deductible Gift Recipient (DGR) status and substantial Fringe Benefits Tax (FBT) concessions, while the almost identical agency may not enjoy the same concessions.

The inconsistency in application of concessions has substantial implications beyond cost structures as attracting investment from philanthropy and other sources is often dependent upon being able to offer the offsets that come with charitable and DGR status. An experienced and knowledgeable Not-for-Profit Tax Concessions Working Group was established by the Treasurer in late 2012 to consider these issues. After a period of public and private consultations, this Working Group delivered a final report in May including some revenue neutral initiatives that CCA supports – see here: http://www.treasury.gov.au/~/media/Treasury/Access%20to%20Information/Disclosure%20Log/2014/1447/Downloads/PDF/NFP%20Sector%20WG%20Final%20Report.ashx

CCA believes this report is another that should be taken off the shelf, dusted off, and used to inform real reform and provide concessions that will benefit civil society and the broader community.

In considering taxation policy it is important to address some of the inconsistencies that create advantages and disadvantages within the charities and not-for-profit sector.

Conclusion

This submission reflects the findings from a long history of inquiries and detailed consideration by numerous groups into the benefit of charitable and not-for-profit tax concessions to the Australian community. While most of the current charity and not-for-profit tax concessions should be retained, we can improve the tax system by streamlining classifications and concessional arrangements, improving access to capital, creating greater certainty in government funding, streamlining government processes and associated administration, empowering consumers; ending pointless duplication and multiple assessments of eligibility for government concessions. Changes in these areas will benefit all Australians.

It is hoped the review of Australian taxation will take the issues raised in this submission into account to ensure the government and community maximise their investment in charities and not-for-profits. A better tax system can play a vital role in ensuring we live in the Australia we want, and encourage a stronger less encumbered charities and not-for-profit sector to flourish.

Current Membership – Community Council for Australia *Attachment A*

Organisation	CEO/Director
2realise	Rowena Stulajter
Access Australia's National Infertility Network	Sandra Dill
Australian Charities Fund	Jenny Geddes
Australian Council for International Development	Marc Purcell
Australian Healthcare and Hospitals Association	Alison Verhoeven
Australian Indigenous Leadership Centre	Rachelle Towart
Australian Institute of Superannuation Trustees	Tom Garcia
Australian Major Performing Arts Group	Bethwyn Serow
Australian Women Donors Network	Julie Reilly
Canberra Men's Centre Inc	Greg Aldridge
beyondblue	Georgie Harman
Charities Aid Foundation	Lisa Grinham
Church Communities Australia	Chris Voll
Churches of Christ Community Care VIC & TAS	Paul Arnott
Community Broadcasting Association of Australia	Jon Bisset
Community Colleges Australia	Kate Davidson
Compass Housing Co Ltd	Greg Budworth
Connecting Up Australia	Anne Gawen
Drug Arm Australasia	**Dr Dennis Young (Director)**
e.motion21	Cate Sayers
ethicaljobs.com.au	Michael Cebon (Associate Member)
Family Life Services Australia	Jo Cavanagh
Foresters Community Finance	Ashley Hood
Foundation for Alcohol Research and Education	Michael Thorn
Foundation for Young Australians	Jan Owen
Fundraising Institute of Australia	Rob Edwards
Good Beginnings Australia	**Jayne Meyer-Tucker (Director)**
HammondCare	Stephen Judd

Hillsong Church	**George Aghajanian (Director)**
Justice Connect	Fiona McLeay
Lifeline Australia	**Jane Hayden (Director)**
Life Without Barriers	**Claire Robbs (Director)**
Maroba Lodge Ltd	Viv Allanson
Missions Interlink	Pam Thyer
Mission Australia	Catherine Yeomans
Musica Viva Australia	**Mary Jo Capps (Director)**
Opportunity International Australia	Robert Dunn
Our Community	Denis Moriarty (Associate Member)
Philanthropy Australia	Chris Wootton
Port Phillip Housing Association	Karen Barnett
PowerHousing Australia	Julie Quaass
Pro Bono Australia	Karen Mahlab (Associate Member)
Relationships Australia	Alison Brook
RSPCA Australia	**Heather Neil (Director)**
SANE	Jack Heath
SARRAH	Rod Wellington
Save the Children	**Paul Ronalds (Director)**
St John Ambulance Australia	Peter LeCornu
Social Ventures Australia	Michael Traill
The Benevolent Society	Joanne Toohey
The Centre for Social Impact	Andrew Young
The Reach Foundation	Sarah Davies
The Smith Family	**Lisa O’Brien (Director)**
The Ted Noffs Foundation	Wesley Noffs
Variety Australia	Neil Wykes
Volunteering Australia	**Brett Williamson (Director)**
Wesley Mission	**Rev Keith Garner (Director)**
World Vision Australia	**Rev Tim Costello (Chair)**
YMCA Australia	Ron Mell
Youth Off The Streets	Fr Chris Riley
YWCA Australia	Dr Caroline Lambert