Australian Government
Department of Communications, Information Technology and the Arts

our reference

Consultation on the Definition of a Charity
The Board of Taxation
C/- The Treasury
Langton Crescent
PARKES ACT 2600

SUBMISSION ON THE CHARITIES BILL 2003

The Department of Communications, Information Technology and the Arts (DCITA) welcomes the opportunity to respond to the Board of Taxation's invitation, as part of its public consultation process, to make a submission on the workability of the draft legislative definition of charities and the implications for the not-for-profit cultural sector.

This submission addresses issues relating to the Charities Bill 2003. It also considers issues relating to the legislative frameworks in tax law and administrative mechanisms that provide for concessional treatment of the not-for-profit cultural sector, since these are pertinent to the clarity and workability of the definition of "charity" on which you are seeking comment.

Introduction

The Australian Government's cultural objectives are to:

- promote access to, participation in and enjoyment of cultural activities by the public at large;
- foster creativity, diversity and excellence in the arts;
- encourage the viability of cultural organisations;
- protect the intellectual property and moral rights of creators; and
- facilitate Australia's cultural export performance.

A key strategy to achieving these objectives is to assist the not-for-profit cultural sector via the following mechanisms: funding at arm's length through peer assessment processes; direct grants to cultural organisations to deliver specific benefits to the community, including in regional areas; and the direct establishment and maintenance of cultural institutions to provide products and services. Indirect tax expenditures through various tax concessions available to the broader not-for-profit sector are a very important additional avenue of support to cultural organisations and institutions.

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Charities Bill 2003

Inclusion of culture as a specific category of charity

DCITA welcomes the "advancement of culture" as a specific category in the legislative definition as it gives express recognition to the established role of not-for-profit cultural endeavour as part of the charitable sector. (The cultural sector has in the past come under the general category of *other purposes beneficial to the community*.)

Disqualifying purposes

DCITA is concerned that Section 8 as it stands could potentially be very restrictive and discriminatory and seriously inhibit the legitimate operations of charitable organisations.

Section 8(1) states that "the purpose of engaging in activities that are unlawful is a ***disqualifying purpose"***. The Explanatory Memorandum states that "the disqualifying purpose of engaging in illegal activities parallels the requirement that a charity does not engage in activities constituting a serious offence" (clause 1.52). The Bill defines *serious offence* as "an offence against a law of the Commonwealth, of a State or a Territory, that may be dealt with as an indictable offence (even if it may, in some circumstances, be dealt with as a summary offence)".

While on face value this clause would appear reasonable, there is the potential for an organisation's charitable status to be revoked based on the actions of one person within the organisation and prior to a court hearing or trial. Furthermore, there is nothing in the legislation to indicate that it would not be applied to past indictable offences within a charitable organisation.

In the USA, regulations known as *Intermediate Sanction Regulations* have been issued to cover charitable organisations and persons who hold certain powers, responsibilities or interests and are in a position to exercise substantial influence over the affairs of a charitable organisation. The Intermediate Sanction Regulations are designed to provide a roadmap for organisations, particularly in the area of entitlement of officials to various benefits and to ensure compliance by the charity and officials with the rules applying to benefits and with other applicable laws. A paper by the Director of Exempt Organizations, Internal Revenue Service[1] suggests that legislative history indicates that, in most instances, the imposition of the intermediate sanction will be in lieu of revocation of an organisation's charitable status. This model would be worth exploring further, as it would appear to provide a more effective approach for dealing with the "engaging in unlawful activities" by a charity or a person(s) within the charitable community.

[1] 'Easier Compliance is Goal of New Intermediate Sanction Regulations', by Steven T. Miller

The intent of Section 8(2) would appear to be to clarify that the purposes of advocating a political party or cause; supporting a candidate for political office; and/or attempting to change the law or government policy are not in themselves charitable purposes. The clause as it currently reads could, and indeed is, raising alarm within the charitable sector (including cultural organisations) that engaging in these activities could jeopardise their charitable status. It is recommended that this clause be reworded to more clearly enunciate the intent and allay concerns where these activities are ancillary or incidental to an entity's charitable purpose.

Government function versus charitable purpose

Over time the relationship between government and the community sector has changed, as has responsibility for delivery of services, resulting in a blurring of the distinction between the two. This is causing increasing uncertainty within the not-for-profit sector, particularly for the purpose of determining access to tax concessions, where it is not clearly obvious whether an entity is carrying out a 'government function' or engaged in a 'charitable purpose'.

This is a significant issue within the cultural sector. By way of example, DCITA administers two tax incentive programs, the Register of Cultural Organisations (ROCO) and the Cultural Gifts Program (CGP) which encourage donations to cultural entities with Deductible Gift Recipient (DGR) status. The close to 400 public art galleries, museums and libraries participating in the CGP, with the exception of a few, are government owned and controlled. ROCO has some 900 participant entities, of which some 28 have been established as statutory authorities and around a further 20 have some degree of government control.

While DCITA is aware of the distinction between DGR and charitable status, it is not well understood within the not-for-profit cultural sector or the general community. DGR status provides approved charities and government entities (eg, the national and state public collecting institutions) with direct access to tax deductibility for donations. Charitable status relates mainly to income tax exemption as a charity and does not include government entities since they are considered to be part of the function of government. This has led to an anomaly in the income tax law that presents an impediment to DGRs that are not "charities" attracting disbursements from charitable funds (ie, ancillary funds, philanthropic trusts and prescribed private funds), since charitable funds will not be exempt from income tax under Division 50 of the *Income Tax Assessment Act 1997* unless they distribute solely to another charitable fund, foundation or institution. That is, distributions to a government entity that is a DGR will not constitute a distribution to a "charity".

The relationship between government and the not-for-profit sector is likely to continue to change and will be influenced by initiatives such as the Prime Minister's Community Business Partnership which is actively working to encourage greater collaboration between government, business and community leaders in delivering community outcomes. It would be clearer and more workable now and in the future if entities that have all the characteristics of a charity and would be deemed to be engaged in charitable activities, except for the fact that they are government controlled, were classified as charities for the purpose of tax law and access to tax concessions.

In the event that the current definition of charity is retained, DCITA recommends that the Board pursue amendment of Division 50 to address the existing anomaly relating to disbursements to DGRs, to ensure consistent access to philanthropic support by all DGRs including those classified as government entities.

Concept of altruism as an additional requirement to enhance the public benefit element of a charity

The *Report of the Inquiry into the Definition of Charities and Related Organisations* (the Report) recommended that that the public benefit test should be strengthened by also requiring the dominant purpose of a charitable entity to be altruistic. The terms of reference identify this issue as one on which the Board of Taxation is seeking input.

Section 7 of the Charities Bill 2003 defines the public benefit element of a charitable purpose and upholds the common law approach that 'public benefit' is an essential condition for determining charitable purpose. It is considered that the public benefit test defined in Section 7 is sufficient in ensuring involvement by the public and that charitable activity is of benefit to the public, without the need for an additional test to explicitly embrace the concept of altruism. The Report noted that the Inquiry Committee did not consider that altruism needed defining beyond its ordinary dictionary meaning, being 'unselfish concern for the welfare of others' or 'regard for others as a principle for action'. The 'altruism' test may be difficult to apply in an objective way and could potentially deny charitable status to organisations who otherwise meet the public benefit test, with adverse implications for the charitable sector and the community.

Public benevolent institutions as a subset of charity

As noted in the Report, the term Public Benevolent Institution (PBI) appears only in revenue Acts to limit some tax concessions to a subset of charity. These tax concessions include income tax exemption as a charity and more comprehensive fringe benefits tax concessions than are available to other charities and related organisations.

PBI has never been legislatively defined and it is noted that there have been no steps taken in the Charities Bill 2003 to do so. The distinction between PBIs and other charities is not readily understood, as noted in the Report, and this is certainly the case within the not-for-profit cultural sector.

Other common law countries such as the United States of America, Canada and the United Kingdom adopt the approach of a single concept or category of charity, with taxation concessions applying equally to all charities. It is suggested that the notion of a PBI is becoming outmoded and less relevant in today's society. For instance, there is increased recognition that a charitable purpose can have impacts and benefits on the community beyond that particular charitable purpose/activity. For example, there is greater government recognition that the arts are an important part of the charitable sector and the community, providing intellectual and emotional stimulation, offering commentary on all aspects of society and challenging citizens to find new ways of looking at life. In addition, the benefits of cultural activities are increasingly being recognised as playing an important role in engaging those at risk of social exclusion and promoting community cohesion.

It is proposed that a single category of charity would overcome the existing complexity and confusion surrounding the concept and understanding of charity within the not-for-profit sector and the broader community and be more appropriate in today's society and adaptable to the changing role of charities in the future.

Summary

The cultural sector in Australia is predominantly not-for-profit and dependent on a mix of earned income, government and philanthropic or sponsorship support. DGR status is of particular importance to the sector, as income from donations has become increasingly important to the survival of not-for-profit cultural organisations.

The Charities Bill 2003 expressly acknowledges not-for-profit cultural activity as part of the charitable sector. The recommendations made in this submission are aimed at strengthening recognition of the not-for-profit cultural sector as an important component of charitable endeavour, by affording it the same status and treatment, including taxation concessions, as other charities. It is believed that this approach would also reduce the administrative burden for government and charities and provide greater clarity for the not-for-profit sector and the general public on what constitutes a charity.

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