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The Commissioners
The Productivity Commission

9 February 2024

Dear Sir/Madam

PRODUCTIVITY COMMISSION DRAFT REPORT - PHILANTHROPY - BDO SUBMISSION

BDO refers to the invitation by the Productivity Commission to provide comments on the Productivity Commission's Draft Report on Philanthropy. BDO is pleased to provide feedback and comments in relation to the call for submissions. Our detailed comments are outlined in the appendix below.

BDO is a firm of Chartered Accounts that provides Tax, Audit and various advisory and consulting services to a large variety of clients in various sectors, including charities and other not for profit organisations. Also please note that BDO established the BDO Foundation Trust as a Public Ancillary Fund in 2018 to connect the firm and its employees with key community issues.

Should you have any questions or wish to discuss any of the comments made in our submission, please contact Russell Postle via email: russell.postle@bdo.com.au or phone on 0419 703 581.

Yours sincerely

Lance Cunningham
BDO National Tax Technical Leader

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PRODUCTIVITY COMMISSION DRAFT REPORT - PHILANTHROPY - BDO SUBMISSION

**Draft finding 3.1****Rising income and wealth are the major reasons behind rising tax-deductible donations**

Tax-deductible donations by individuals made directly to charities have increased in value, but fewer people are making such donations. From 2000-01 to 2020-21, tax-deductible donations tripled (in real terms) despite the number of taxpayers increasing by only 38%. The available evidence indicates that this coincided with individuals' financial capacity to donate increasing.

The Australian Government also made policy changes that provided additional or more flexible financial incentives to give, which likely also played a role in increasing giving. Giving into private and public ancillary funds has grown in value (from \$692 million in 2011-12 to \$2.4 billion in 2020-21). The relative importance of private ancillary funds has also grown from 15% to 27% of individual giving.

This commentary is consistent with the anecdotal observations by BDO.

There has been an increase in the number of Private Ancillary Funds established by BDO clients.

BDO submits that the tax deductibility of contributions to a PAF is an essential requirement. The donor is transferring their contribution into a structure that can only distribute to entities with DGR Type 1 status. The donor is giving away the money that is being contributed to the PAF.

If there is only a partial deduction such as what happens in effect with a flat rate tax credit less than the marginal tax rate, BDO submits that many individuals will question their ability to be able to afford the donation to the PAF.

With a reduced deduction and resultant income tax liability many might decide to retain the funds for private consumption rather than establish or contribute to a PAF.



Draft finding 4.1

People respond to incentives, with those on a higher income more likely to give

Preliminary modelling undertaken by the Commission indicates that people give more than they otherwise would because of the personal income tax deduction for donating to entities with deductible gift recipient status. The modelling draws on Australian taxpayer panel data and is the first time panel data has been used in Australia to estimate how people respond to personal income tax deductions for donations.

The Commission estimated the price elasticity of giving - which is how people change their giving behaviour in response to changes in tax incentives for giving - and the income elasticity of giving, which is how people change giving behaviours in response to changes in their own income.

The Commission's preliminary estimates for:

- price elasticity of giving in Australia ranges from -0.87 to -0.92, meaning a 1% increase in the tax deduction for giving is associated with a 0.87% to 0.92% increase in giving,
- the income elasticity of giving in Australia ranges from 0.555 to 0.564, meaning a 1% increase in income is associated with a 0.555% to 0.564% increase in giving.

However, these estimates are only one factor to consider when evaluating the effectiveness of tax incentives to give.

The share of taxpayers claiming a deduction for giving increases with income. Most of the tax benefits from giving that accrue to people in the lowest taxable income decile go to people who had high incomes before claiming any tax deductions.

The Commission will present final estimates, using different modelling approaches, of the price elasticity of giving and the income elasticity of giving in the final report.

The BDO observation is that the tax deductibility of a donation is a significant factor in a client's decision process of whether to give a donation to a charity, and particularly important in the decision regarding the amount of a donation.

Whilst there can be a science about the price elasticity, the question that is regularly posed to BDO advisers - is it a tax deduction? A negative response results in price resistance, resulting in a reduction in donations and lower funds available to the DGRs.



Draft recommendation 4.1 **Remove the \$2 threshold for tax-deductible donations**

The Australian Government should amend the *Income Tax Assessment Act 1997* (Cth) to remove the \$2 threshold for tax-deductible donations to entities with deductible gift recipient status.

Within BDO there has been a technical debate on the tax treatment of some donations within a regular giving structure such as a workplace giving scheme. The example question was a person who gave \$1 per week out of their pay. Are they giving a tax deductible donation of \$52 in weekly part payments or 52 individual donations of \$1 that as individual donations are less than the \$2 threshold. A hypothetical tax question.

BDO supports the draft recommendation to remove the \$2 threshold and remove the doubt.



Information request 4.1 **Data on giving that is not tax deductible**

While there are estimates of the proportion of people who have given, but do not claim an income tax deduction, more complete and recent data would inform the Commission's final recommendations on policy options that seek to improve incentives to give. The Commission is seeking information, such as survey or other data, about instances where people make donations, but do not claim a tax deduction for reasons including they:

- do not have taxable income,
- choose not to claim the deduction,
- donate to entities that do not have deductible gift recipient status and therefore the donations are not eligible for a tax deduction.

The Commission is also seeking information on the reasons why people choose not to claim a tax deduction for giving if they *do* have taxable income and the donations are eligible for a tax deduction.

BDO can offer the following observations to outline the instances where a donation tax deduction may not be claimed. Unfortunately, we are unable to quantify these instances.

as to those who may not claim an income tax deduction for a donation:

- Those who do not have taxable incomes:
Taxpayers whose taxable income may be under the income tax threshold (currently \$18,200) (such as those drawing tax free superannuation pensions) or the tax payable is covered by rebates (such as for those on disability or aged pensions) and the inclusion of their donations on the tax return is of no consequence.

However, the fact that they chose to not include the donations on their tax return does not indicate that they did not value that their donation is fully tax deductible.

- Individuals who choose not to claim an income tax deduction:
Circumstances where an individual may choose not to claim an income tax deduction may include:
 - Where the donation receipt was lost so the individual is unable to substantiate their income tax deduction.
 - Where the donation was a one off by the individual and the individual did not receive a donation receipt for whatever reason (such as an error in the data provided so the organisation was unable to send the donation receipt).
 - Where the donation was spontaneous, and no receipt was available at the time (examples of this have been collections in support of major catastrophes such as the Victorian bushfires where buckets of cash were collected in public locations and members of the public were keen to support the cause)
 - Where the donation was made by placing coins and notes in a donation collection receptacle at a café, store, hotel or similar. Examples are Royal Flying Doctor Service sealed tins, Guide Dogs plastic dog receptacles, foreign coin containers at airports. Cash donated in these tins and receptacles is included as donations by the beneficiary organisation but no receipt for the actual amount raised can be issued to the actual donor nor to the venue that hosted the collection receptacle.
 - Where the individual donation transaction is less than the \$2 threshold such as where transactions are rounded up to the next dollar with the customer's permission.

- Circumstances where a business may choose not to claim an income tax deduction of the amount as a donation may include:
 - Where the recognition that the charity provided to the business became more than mere simple recognition / receipt thereby making the payment no longer able to be treated as a donation under the ITAA and more in the character of a sponsorship,
 - Where the business suffers a loss for income tax purposes - under the carry forward income tax loss rules a gift cannot give rise to a loss forward. The business may not bother recording the donation in circumstances where there will be a loss for tax purposes as it will in effect be non-deductible,
 - Where there is a statutory cap on the amount of the income tax deduction available which applies to donations to political parties.



Information request 4.2 Government policies to support giving

The Commission is seeking feedback on the advantages and disadvantages of using alternative government policies to support giving, including a tax credit and matched giving, as opposed to a tax deduction.

- How would donors likely change their giving behaviour under different types of tax incentives, such as a tax credit, and what would drive those changes?
- What would be the effect on charities of moving to a tax credit if more people were likely to give smaller amounts, but the overall amount of giving decreases?
- If it were to be adopted, how should a tax credit be designed?
- What would be the effect on donations of moving to a matched giving scheme, like Gift Aid, given it does not provide a direct personal benefit to encourage all taxpayers to give?
- Would such a matched giving scheme be an improvement compared to a tax deduction and, if so, how should it be designed?

BDO does not support the concept of replacing the existing income tax deduction regime for donations with a tax credit / rebate at a rate less than a taxpayer's marginal tax rate.

Importance of income tax deduction

In the experience of BDO, an important issue for the majority of our clients is whether the recipient is a DGR. The ability to claim a deduction and the extent of that deduction are both relevant.

BDO anticipates that a tax rebate rather than an income tax deduction would act as a disincentive for all donors whose marginal rate of tax was higher than the rebate level.

Top marginal taxpayers provide the majority of donations (assessed on a total funds basis). The NFP sector relies heavily on the contributions of top marginal taxpayers. These taxpayers should continue to be provided with incentives to contribute wealth to the sector. A rebate regime would make raising funds from top marginal taxpayers more difficult.

Conversely, BDO considers that a potentially higher tax incentive for lower income earners will not necessarily lead to those low income earners donating more than they already do (nor donating enough to counter any reduction in donations from higher income earners).

Lower income earners have a lesser financial capacity to donate. For most individuals and businesses donations are discretionary expenditure. In 2023 and the year to date there are many references in the media to a cost of living crisis - costs have risen at a faster rate than incomes resulting in individuals and businesses being required to review outlays and this will regularly result in reductions of discretionary expenditure.

Many DGR registered entities are heavily dependent upon community donations and BDO believes that the deductibility of donations is a key driver in encouraging people to donate to support these causes.

A tax deductible based approach is also more easily implemented as a component of workplace giving regimes.

BDO also submits that it believes that a rebate compared to a tax deduction will produce a negative reaction for those whose income is subject to significant fluctuation between years changing the percentage of deduction available.

A tax credit in place of a deduction will create distortions.

BDO submits that adoption of a fixed rate tax credit at a rate less than the taxpayer's marginal rate will introduce distortions and complexity into the tax system.

These distortions that would result from a fixed credit rather than an income tax deduction include:

- Sponsorship deductions at a different tax rate to the rate for a donation / gift of the same value;
- Trust distributions to charities at a different tax rate to the rate for a donation / gift of the same value;
- Social enterprises which distribute to DGRs
- Donations from PAFS and Foundations
- Accounting and tax balances

Sponsorship v donation

Many businesses require their brand obtain recognition in return when they provide financial support to a not for profit. Where an entity receives something more than mere simple recognition in return will generally result in that contribution no longer qualifying as a gift under the income tax rules. The relationship between the business and the charity then becomes one of sponsorship where the expense is claimed for income tax purposes under the standard Section 8-1 of the ITAA 1997 rather than the gift rules.

A rebate / tax credit approach would therefore create an inconsistency where an entity claims an amount as a deductible outgoing, such as a sponsorship instead of a donation. In such circumstances, the entity would enjoy a deduction at its marginal tax rate however the same amount, if claimed as a donation would only result in the rebate / tax credit.

Trust distributions

Many discretionary trusts include in the standard list of beneficiaries charities as a category of beneficiary. The income tax law recognises and supports this by including charities as a member of the "family" for the purposes of the administration of the Family Trust legislative restrictions applying to discretionary trust. Where the charity is exempt from income tax the amount of income distributed to the charity is effectively equivalent to a tax deduction providing a tax benefit at the rate of the marginal tax rate of the other beneficiaries that would have otherwise received the distribution of the trust income.

A rebate / tax credit approach would therefore create an inconsistency in the effective tax rate where a discretionary trust distributed an amount to a charity as compared to a donation of a similar value.

Social enterprises

Social enterprises are increasing in numbers of entities operating as this type of enterprise - a for profit entity structure operates a business and donates the profit generated to a DGR charity.

The social enterprise relies on the tax deduction of the donation to the DGR to reduce its income tax liability to nil or a minimal amount.

A flat rate tax credit would likely result in the social enterprise incurring a tax liability, reducing the ability of the social enterprise to pay the full amount as a donation and causing the social enterprise to be unable to honour its commitment to those who engage the social enterprise.

An example is set out below under the heading Accounting and tax.

Donations from PAFS and Foundations

The flow of new donation funds into a PAF or foundation will be negatively impacted if the donor is subject to a flat tax credit rather than a deduction at marginal rates.

The BDO observation is that many PAFs are established in the year when a transaction event results in a large taxable income. The establishment of the PAF relies on the donation to the PAF being a donation that is able to offset, at least in part the large transaction.

Once the donation enters the PAF it is constrained by the PAF rules and can only benefit DGR Type 1 charities.

Accounting and tax balances

One of the challenges with a fixed rate tax credit at a rate less than the marginal tax rate is that there is a different outcome for accounting and tax.

To demonstrate the issue by use of two examples.

Example 1 Assumptions

Income \$200 and normally donate 50% of income, that is, \$100.

Tax rate 30% and the flat tax credit set at half the tax rate - 15%.

| | Donation fully deductible | Donation at 50% flat tax credit | Adjust donation to retain net income |
|----------------------|---------------------------|---------------------------------|--------------------------------------|
| Gross income | 200 | 200 | 200 |
| Donation | (100) | (100) | (80) |
| Income post donation | 100 | 100 | 120 |
| Tax | (30) | (45) | (48) |
| Net income | 70 | 55 | 72 |

With the deduction fully deductible, an amount of \$70 remains after tax.

If the flat tax credit is set a half of the tax rate, and no change to policy of paying 50% of the profits as a donation the net outcome is that the owner's remaining income is reduced from \$70 to \$55.

If the owner wishes to retain the same net income the solution is to reduce the donation by 20% to \$80.

Example 2 - Assumptions

Income \$200 and normally donate 50% of income, that is, \$100.

Tax rate 48% and the flat tax credit set at half the tax rate - 24%.

| | Donation fully deductible | Donation at 50% flat tax credit | Adjust donation to retain net income |
|----------------------|---------------------------|---------------------------------|--------------------------------------|
| Gross income | 200 | 200 | 200 |
| Donation | (100) | (100) | (67) |
| Income post donation | 100 | 100 | 133 |
| Tax | (48) | (72) | (80) |
| Net income | 52 | 28 | 53 |

With the donation deduction as fully deductible for income tax, an amount of \$52 remains after tax.

If the flat tax credit is set at half of the tax rate, and no change to the individual's policy of paying 50% of the profits as a donation, the net outcome is that the owner's remaining income is reduced from \$52 to \$28.

If the owner wishes to retain the same net income the solution is to reduce the donation by one third to \$67.

BDO believes that donors regularly measure their donation in terms of the after tax cost to them as donors, rather than what the needs of the charity might be.

BDO believes the replacement of a full deduction with flat rate tax credit will result in a reduced level of donations being made.

As part of the BDO commitment to our people, the business will give a donation to a charity selected by the staff, match donations given by employees to a selected charity with a donation by BDO and give donations to charities from time to time.

Currently these donations are deductible at the corporate income tax rate. If a lesser effective income tax rate applies to a donation as a consequence of the introduction of a fixed rate credit, BDO will need to revise its donation policy to reflect the higher effective after tax cost.

BDO anticipates this would result in a reduction of donations by the business.

Effect of more contributions of a lesser value

Subdivision 30CA of the ITAA requires a DGR to issue a qualifying receipt. The majority of donation receipts issued are now done so in an electronic form, with many charity organisations using an automated process supplemented with manually initiated electronic receipts.

Whilst charities in general welcome all donations the reality is that there is a fixed administration cost to receive each donation in recording the donor details, the actual donation details and issuing a receipt. All steps required by Division 30 of the ITAA.

In addition, with an increased number of small donations BDO anticipates that charities will encounter a proportional increase in the number of failed credit cards, failed donor details to be completed correctly.

If there are an increased number of small donations there will be an increase in administration costs.

Gift Aid

The concept of a matching donation is a common feature of many fundraising campaigns - a donor agrees to provide a certain amount and the charity invites supporters to make their donations knowing that their donation will be matched (subject to the nominated limits).

BDO considers that the income tax deduction at the marginal income tax rate remains an essential component of the decision to support the charity.

BDO does not support the Gift Aid concept. BDO submits that the concept outlined in Box 4.9 introduces a complexity in order for a charity to encourage a donation from a taxpayer on the higher marginal tax bracket and places a responsibility on the donor to undertake additional documentation to allow the charity to claim the Gift Aid.

BDO is concerned that the inherent complexity of process in order to claim an amount from Gift Aid will act as a barrier to making a claim.

BDO does not support the concept of digital charity vouchers as set out in Box 4.9 as a replacement for an income tax deduction.

BDO submits that the concept of digital charity vouchers could result in funds being directed to a charity that can be seen to be popular rather than on selected on the basis of merit such as the community need for services.

BDO submits that a matched giving scheme would be a retrograde step and will lead to reduced levels of donations by individuals and by businesses with a consequential reduction in services delivered by charities.



Draft recommendation 6.1

A simpler, refocused deductible gift recipient (DGR) system that creates fairer and more consistent outcomes for donors, charities and the community

The Australian Government should amend the *Income Tax Assessment Act 1997* (Cth) to reform the DGR system to focus it on activities with greater community-wide benefits. The scope of the reformed system should be based on the following principles.

- There is a rationale for Australian Government support because the activity has net community-wide benefits and would otherwise be undersupplied.
- There are net benefits from providing Australian Government support for the activity through subsidising philanthropy.
- There is unlikely to be a close nexus between donors and beneficiaries, such as the material risk of substitution between fees and donations.

In applying these principles, the Australian Government should:

- extend eligibility for DGR status to most classes of charitable activities, drawing on the charity subtype classification in the *Australian Charities and Not-for-profits Commission Act 2012* (Cth) to classify which charitable activities are eligible for DGR status and which are not
- expressly exclude the following classes of charitable activities or subtypes:
 - primary, secondary, religious and other informal education activities, with an exception for activities that have a specific equity objective (such as activities undertaken by a public benevolent institution)
 - the activities of childcare and aged care in the social welfare subtype (other than activities undertaken by a public benevolent institution)
 - all activities in the subtype of advancing religion
 - activities in the other analogous purposes subtype that are for the purpose of promoting industry or a purpose analogous to an exclusion in another subtype
 - activities in the law subtype that further another excluded subtype
- only grant DGR status to government entities where they are analogous to a charity and undertake activities that would be eligible for DGR status if undertaken by a charity
- continue to limit the scope of the DGR system to registered charities and equivalent government entities
- only use the specific listing mechanism in exceptional circumstances. When it is used, the Australian Government should increase transparency about applications, how these are assessed, and the decision-making process to maintain confidence in the broader DGR system.

At present DGR registration is by application and the DGR registration can be achieved in one of two manners:

- The entity is registered as a DGR - where the nature of the activities undertaken by the entity and its purpose indicate that all activities are of a type worthy of DGR status.

- The entity establishes a gift fund which fund is registered as a DGR - where the nature of the activities undertaken by the entity and its purpose indicate that there is a mix of activities that qualify for DGR and some that do not.

Under both scenarios the charity needs to be able demonstrate that the expenditure using the DGR funds is applied in accordance with the DGR purposed.

BDO submits that there is merit in extending the categories under which a charity can apply for entity registration as a DGR or to be able to establish a gift fund. This comment is predicated on the assumption that the current system of income tax deductibility for donations is retained.

If the ability to access DGR registration is to be based on charity subtype, consideration needs to be given to entities that have multiple parts and consequently qualify for several subtypes. This will be particularly relevant where not all parts / subtypes qualify for DGR registration.

BDO submits that the gift fund system where a part of an entity's activities qualify for DGR registration will need to be maintained.

BDO submits that exclusion from entitlement to DGR should not be based on the nature of the body but remained focus on the activity delivered.

School building funds

The Commission recommendation is for the Australian Government to withdraw DGR status from school building funds on the fear that donations to school building funds reduce school fees and that government funding of the education sector has increased since the category was first enacted.

BDO declares that it has and continues to provide audit and other services to education providers.

The BDO observation is that invitations to donate to a school building fund are seeking voluntary donations and no instances where there is any suggestion of a link between school fees and donations to a building fund.

The invitations to donate may contain a suggested amount - this should be seen as a prompt not a requirement to pay.

Charities seeking donations regularly include a series of amounts to prompt a potential donor to consider an amount that may be greater than if the donor was left to nominate their donation amount.

The operation of a school building fund is subject to the governance requirements of the ACNC, the rules contained in Division 30 (the DGR rules) and those in Division 50 (income tax exemption rules).

There is also clear legal case law precedent that if taxpayer obtains a benefit more than simple recognition of a donation that the character of a gift is no longer so therefore it is no longer deductible as gift. BDO submits that there are adequate protections in the existing law governing school building funds to ensure the quantum of school fees is not distorted by donations to school building funds.

In school building funds there is regularly a long lead time between donations received and the new facilities. Often it is past students who choose to donate to the school building fund.

BDO submits that school building funds are essential for new schools being developed and to assist schools to be able to ensure that their resources align to the needs on modern education.

In the Commission's draft report there is also a statement that another factor is the greater government contribution to non-government schools at present compared to the time when the deduction was introduced. This comparison can also be applied to other sectors such as health services, disability support, homelessness support etc.

School building funds for non-government schools reduce the pressure on government funding, allowing the government to focus on the government schools.

In addition, as donations to school building funds are voluntary, fundraising by a school community to support the school building fund and to create new infrastructure provides a bond for that community.

BDO respectfully suggests that the Commission consider recommending that government schools be able to establish a school building fund for their school or group of schools to provide a mechanism for support from current past and future students and their families. Families with children attending government schools are from a wide range of economic backgrounds.

Charity prerequisite

BDO agrees that the DGR endorsed entities must be charities or government entities. This requirement is only reaching full implementation phase. This approach ensures all DGR entities are subject to the governance required overseen by the ACNC or by the particular government.



Information request 6.1

Improving the specific listing mechanism

The Commission expects that, under its proposed reforms of the deductible gift recipient system, specific listing would be used only in exceptional circumstances, but welcomes further feedback on:

- what role it should play, if any
- how applications should be assessed
- how transparency could be improved, including what further information should be published about the entities that apply for specific listing, how applications are assessed and decision-making processes about why or why not an application is approved
- whether specific listing should be done through regulation rather than legislation.

Specific listing

BDO submits that the Australian Government should retain the power to use the specific listing mechanism as the parliament sees fit, rather than being limited to having to first define if the entity satisfies the term exceptional circumstances.

The process of requiring the addition to the specific listing to be considered in the parliament is sufficient to manage the risk of any lack of transparency.



Information request 6.4

How expanded access to deductible gift recipient (DGR) status would change giving

The Commission is seeking information, including survey and data information, on how people would change their giving behaviour if DGR status is expanded to most charitable activities (subject to the exclusions described in draft recommendation 6.1).

- Would the expansion in the scope of the DGR system likely result in additional giving overall? If so, by how much?
- Would donors give less to entities with existing DGR status and more to those that gain DGR status under the proposed reforms? If so, by how much?

BDO's comments are based on the anecdotal evidence of conversations with clients - our experience is twofold:

- Charities that do not have DGR status seek to be able to obtain DGR status so they can offer tax deductible donations and be able to apply for grants from foundations and PAFs who are restricted to donating to DGR Type 1 registered entities.
- Individuals and businesses that value income tax deductions.

Our observation is that with respect to accessing support from foundations and PAFs is that an increase in the number of entities that qualify as DGR registered will not increase the pool of funds available to distribute to DGR registered entities.

However, an increase in the number of entities that qualify as DGR registered is likely to allow more individuals and businesses to find a cause with which they align and thereby increase the total value of donations.

All DGR registrants will need to ensure that they remain relevant to their donors as competition for the donor dollar will be greater.



Draft recommendation 7.1

A more transparent and consistent approach to regulating basic religious charities

The Australian Government should amend the *Australian Charities and Not-for-profits Commission Act 2012 (Cth)* to remove the concept of 'basic religious charity' and associated exemptions, so all charities registered with the Australian Charities and Not-for-profits Commission have the same governance obligations and reporting requirements proportionate to their size.

Eleven years have passed since the commencement of the ACNC and the requirement for a charity to lodge an AIS.

BDO is not opposed to this recommendation but ample time to implement the change should be allowed.



Information request 7.1

Building a stronger regulatory framework

The Commission is seeking information on options that would support implementation of draft recommendation 7.2.

- What changes would be needed to enable the Australian Charities and Not-for-profits Commission (ACNC) to direct a registered charity undergoing revocation of its ACNC registration to transfer surplus assets to another registered charity, without impinging or duplicating the powers available to state and territory regulators? For example, should it be done through an administrative power or by specifying co-operation in the intergovernmental agreement (draft recommendation 7.4)?
- Whether providing the ACNC standing in each jurisdiction's Supreme Court should be in relation to charitable trusts only or other charity structures and, if so, what legislative changes would be necessary to give effect to this?

The Commission is also seeking further information about options for ensuring that the assets of dormant charities are directed toward benefiting the public, including what test may be appropriate for determining whether a charity is 'dormant' and what steps could be taken in response.

Charities at risk of losing ACNC registration

One of the prerequisite conditions to obtaining DGR status is having the appropriate wind up / loss of DGR status clause in the constitution.

The standard clause that on winding up any remaining assets must be distributed to an organisation with like objects needs an additional requirement that where the entity has DGR registration, the assets must be distributed to another entity with like objects AND who also has comparable DGR status. The DGR component of the assets is linked to the loss of DGR status, not just the wind up of the organisation.

If a charity loses ACNC registration status, loss of DGR status is an automatic consequence.

A DGR revocation clause is the main way an organisation can show that it is required to transfer any surplus gifts, deductible contributions and related money to another DGR if it:

- is dissolved or wound up (closed), or
- has its DGR endorsement revoked (cancelled) by the ATO (whichever comes first).

Section 30-125 (6) of the ITAA states:

a document constituting the entity or rules governing the entity's activities must require the entity, at the first occurrence of an event described in subsection (7), to transfer to a fund, authority or institution gifts to which can be deducted under this Division:

(a) any surplus assets of the gift fund (see section 30-130); or

(b) if the entity is not required by this section to meet the requirements of section 30-130 – any surplus:

(i) gifts of money or property for the principal purpose of the fund, authority or institution; and

(ii) contributions described in item 7 or 8 of the table in section 30-15 in relation to a fund-raising event held for that purpose; and

(iii) money received by the entity because of such gifts or contributions.

When ITAA was amended in 2013 to legislate the requirement of this clause, the requirement was not grandfathered for existing charities to apply to all DGR entities.

If the charity loses its ACNC registration it will cease to be regulated by the ACNC

Dormant charities

Legislation now requires that all non-government entity holders of DGR status must be an ACNC registered charity. This replaced the system where entities other than charities could be provided with DGR status.

Consequently, the ACNC is the regulator of all non-government DGR entities. The ACNC is empowered by its governing statute to regulate charities.

Income tax legislation

Division 50 of the ITAA prescribes requirements that must be met at all times to retain income tax exemption by a charity.

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The broad requirements for Australian based charities are:

1. The entity must have a physical presence in Australia and, to that extent, incurs its expenditure and pursues its objectives principally in Australia (paragraph 50-50(1)(a))
2. The entity must be endorsed as exempt from income tax by the ATO.

There are separate requirements for charities:

- That meet the requirements of Item 1 of 30-15 (the DGR rules); and
- Is a prescribed institution located outside Australia and is income tax exempt in its country of residence; or
- Is a prescribed institution based in Australia but incurs its expenditure and pursues its objectives principally outside Australia.

The three specific tests are:

1. Comply with all the substantive requirements in its governing rules (paragraph 50-50(2)(a))
 2. Apply its income and assets solely for the purpose for which the entity is established (paragraph 50-50(2)(b)); and
 3. Continue to be recognised as a registered charity by the ACNC (Section 50-47)
- Director Duties - Australian Charities and Not-For-Profit Commission

The Australian Charities and Not-for-profit Commission, as a separate body to the ATO, governs the duties of the Board (also known as 'Responsible Persons') of a charity.

The ACNC has established seven duties of Responsible Persons: -

1. Act with reasonable care and diligence;
2. Act honestly in the best interest of the charity and for its purpose;
3. Not misuse the position of responsible person;
4. Not to misuse information obtained in performing duties;
5. Disclose any actual or perceived conflict of interest;
6. Ensure that the charity's financial affairs are managed responsibly; and
7. Not allow a charity to operate while insolvent.

The Responsible Persons must ensure their duties to the institution are discharged, or risk the implementation of the following measures by ACNC:

- The Responsible Persons may be stricken off the register and banned from taking the position of a Responsible Person in another institution; and / or
- The institution may lose their charity registration with the ACNC which will result in the ATO removing all income tax and fringe benefit tax exemptions, and DGR and PBI status.

Each charity (other than some exclusions) is required to lodge an Annual Information Statement (AIS) which contains key data and commentary:

- Income for the year by category;
- Expenditure by category;
- Assets by category;
- Text outlining the achievements for the year in the AIS; and
- Text outlining plans for the year ahead.

All of this information is publicly available on the ACNC website, available for access by the ACNC as regulator.

The term dormant should not be interchangeable with low level of activity.

The nature of the sector in which a charity operates may be subject to change and a charity may need to change the focus of its activities. Charities may also have a period during which they need to build their financial base so the charity can be financially sustainable when it increases the level of activity.

Combination

The combination of the ACNC Act and Division 50 of the ITAA, a charity must take caution to clearly demonstrate how each transaction is in within and assists with achieving its purpose and is undertaken in the best interest of the charity.

The directors / management committee of the charity are charged with the responsibilities under the ACNC legislation and the income tax legislation to ensure that all amounts of income received, not just DGR donations, are applied solely to the purpose of the organisation.

BDO submits that there is a strong argument that if a charity is truly dormant, that the charity may not be directing all of its assets solely to the objects of the charity as required by both Division 50 of the ITAA and the ACNC Act.



Information request 8.2

Timely distributions of donated funds for charitable purposes

The Commission is seeking views on whether, and in what circumstances, the regulatory framework for entities that have deductible gift recipient status should encourage timely distributions for charitable purposes, and whether there should be regulatory consistency between giving vehicles to encourage distributions.

This information request suggest that all donations received should be distributed, on a timely manner. Is this to other organisations or as expenditure? What is timely?

Donations are received by charities for multiple purposes including:

- Delivery of ongoing key services/ activities aligned to the charity's purpose;
- Delivery of trial / new services;
- Acquisition of capital assets;
- Financial assistance at times between grants;
- Research projects to identify needs;
- And many more.

Legislation now requires that all non-government entity holders of DGR status must be an ACNC registered charity. This replaced the system where entities other than charities could be provided with DGR status.

Consequently, the ACNC is the regulator of all non-government DGR entities. The ACNC is empowered by its governing statute to regulate charities.

Division 50 of the ITAA prescribes requirements that must be met at all times to retain income tax exemption by a charity.

The directors / management committee of the charity are charged with the responsibilities under the ACNC legislation and the income tax legislation to ensure that all amounts of income received, not just DGR donations, are applied solely to the purpose of the organisation.

For Public Ancillary Funds and Private Ancillary funds there is already a minimum distribution standard established. The nature of these types of funds is that they are regularly established with an amount of seed capital that is invested and

BDO submits there are already adequate legislation and regulatory controls in place.



Draft finding 8.1

There is no case for reducing superannuation taxes for bequests

The current taxation arrangements for superannuation treat a donation to a charity in the same way as a payment to any other non-dependant beneficiary. The tax system is not neutral in death and provides a larger tax benefit for the superannuation component of an estate. Adding further concessions at the time of death would be a relatively costly way for the Australian Government to incentivise philanthropic giving.

BDO notes the recommendation. Commentary is included in the response to the information request to further the discussion.



Information request 8.4

Making bequests through superannuation easier

The Commission is seeking information, including from donors, charities and superannuation funds, on options to allow people to nominate their superannuation death benefit to a charity. The Commission welcomes further information on the:

- potential design of a mechanism to enable people to direct a portion of their superannuation death benefit to nominated charities, including the roles and responsibilities of parties such as trustees and estate executors.
- benefits, costs, risks, necessary safeguards, and potential unintended consequences of policy options enabling a person to direct their superannuation death benefit to nominated charities.
- factors, such as family or financial circumstances, that would contribute to a person deciding whether to take up the option to direct their superannuation death benefit to nominated charities.

All superannuation funds are controlled by Commonwealth legislation which includes as one of the key principles the “sole purpose” test - that is, the sole purpose of a superannuation fund is to provide retirement benefits to its members.

Upon the death of a member, their superannuation benefits are paid by the trustee of the fund to their fund nominated beneficiary or in the absence of any nominated beneficiary to their estate for distribution according to the will of the deceased.

Death benefits paid to a dependent with the definition in the Income Tax legislation can be paid without any amount withheld for income tax. Death benefits paid to a non-dependent beneficiary incur a tax liability of 15% on the untaxed component.

If an individual made a provision in their will to distribute the gross amount of their superannuation death benefits as a bequest to a charity, the result could be that the estate has paid the death benefits pursuant to the will but is left with a taxation liability of approximately 15% of the death benefit.

In circumstances where when doing their estate planning, an individual wishes to bequest a sum of money, BDO had endeavoured to ensure that any taxation liabilities are taken into account in the estate plan.

BDO submits that any death benefit distribution to a charity from superannuation benefits should not be done within the superannuation fund as to do so would require a change to the sole purpose test. Rather the superannuation death benefit should be withdrawn from the superannuation fund as a death benefit and the distribution to the charity by the executors of the estate of the deceased.

If the intention is to allow such a distribution to be made without the estate incurring a tax liability, an amendment to the taxation rules could deem a distribution to a DGR charity as a distribution to a dependent of the deceased.

For integrity purposes the concession could be restricted to amounts paid to charities that are registered DGR entities at the time of the payment.



Draft finding 9.1

Administrative expenses are not an accurate reflection of the performance of a charity

An overemphasis, amongst donors and other stakeholders, on the amount of revenue that charities spend on administrative expenses can lead to incorrect conclusions about charity effectiveness and create perverse incentives for charities. For example, it can result in the underreporting of administrative costs or underinvesting in core capabilities and capacity, such as staff training, which undermines long-term capacity to further charitable purposes and benefit the community.

Charities have incentives to provide information about effectiveness to donors, and this information is shared in various ways. Introducing additional requirements, including standardised quantitative measures, would be impractical and may lead to significant unintended consequences.

Every organisation, whether part of NFP, for profit or government, requires administration in order to manage its activities and to comply with the range of duties and legal responsibilities placed on both the organisation and its governing personnel.

The level of administration required will vary between the type of organisation, the type of services, the compliance requirements of the sector in which it operates, and the information required to inform its funders and supporters.

One of the objectives of the ACNC has been the reduction of red tape including duplicated reporting between the ACNC and State regulators. This has benefitted those charities that are incorporated associations and who suffer from multiple reporting requirements.

BDO endorses this continued push to reduce red tape.

One area of administration that continues to involve duplication is that of the fundraising legislation and the different requirements of each state.



Draft recommendation 9.1

Creating more value from the data held by Australian Government agencies

The Australian Charities and Not-for-profits Commission (ACNC) and the Australian Taxation Office (ATO) should work together to enhance the utility of Australian Government sources of information on charities and giving for donors and the public.

The ACNC should:

- present data on the ACNC charity register in ways that are more meaningful and accessible to donors and the public (such as more prominently presenting charities' deductible gift recipient status), where it is enabled to do so by the Australian Government.

The ACNC and the ATO should work together to:

- publish additional information on distributions by ancillary funds, including collecting and publishing additional information by sub-funds within public ancillary funds.
- raise public awareness of government sources of information on charities, including the ACNC charity register.

The Australian Government should:

- implement reforms to enable the ACNC to publish circumstances and reasons for referrals made to other government agencies (draft recommendation 7.2)
- address regulatory impediments to the ACNC presenting more meaningful information on the ACNC charity register, where necessary.

The ABR currently displays the DGR status of a charity and whether the entity is a Type 1 or Type 2 DGR category.

BDO notes that there is a link from the ACNC “search for a Charity” page to the ABR to check the DGR status. The ABR also lists the current status of the various concessions that the charity holds including:

- is the charity a PBI,
- income tax exemption,
- GST Concessions,
- FBT concessions.

At present the primary register to check DGR status and the above registrations is the ABR.

BDO respectfully questions the need for a duplicated register and the administration cost to maintain the update on the ACNC charity register and whether the charity is a Type 1 or Tye 2 DGR.

The ACNC publishes the data extracted from the AIS lodgements and has also engaged organisations to undertake an analysis of that data. Much of this analysis is focused on the data for the year in question.

BDO has taken the AIS data that has been published for each year and has developed a data analytics tool allowing a charity to benchmark itself against other charities in the similar sector over a range of years. For the charity, how do they compare to others in the same sector, compare key performance data, growth or decline etc.

BDO has participated in previous consultations with the ACNC on the design and content of the AIS and encourage changes under consideration to be open to consultation.



Draft recommendation 9.2

Embedding donor and public views in the Australian Charities and Not-for-profits Commission's (ACNC) regulatory approach

To provide clarity on how the ACNC balances the views of charities, donors, volunteers and the wider public in its regulatory approach, the responsible Australian Government minister should issue a statement of expectations that sets out how these views should be balanced, when:

- designing the content and the presentation of the ACNC charity register and other public resources,
- making decisions about what information to collect through the annual information statement,
- making decisions about whether to withhold or remove information from the charity register.
- forming consultative committees.

The design of the ACNC charity register should be shaped by research on the information needs of donors of all sizes, and evaluation of the charity register should inform its content and presentation.

Each charity is required complete an AIS which contains key information including financial data. The AIS is required to reflect the information for the charity for whom the AIS is applicable.

If the same charity is required to lodge financial statements it is required to prepare those financial statements as General Purpose financial statements, that is, in accordance with all accounting standards.

One of those standards is AASB 10 Consolidated Financial Statements.

Where a charity controls another entity in accordance with the tests in AASB 10, the financial statements of the charity reflect the consolidated Statement of Financial Position and consolidated Statement of Financial Performance.

The financial statements will contain different numbers to the AIS.

In addition, large charities will regularly contain several separate and distinct components or business units. The AIS was updated for the 2022 year to allow charities to provide descriptions of different activities within the AIS, recorded as projects. But this does not contain any financial data.

Consequently interpretations of the data are constrained by the manner in which the data is loaded into the AIS.



Draft recommendation 9.3

Introducing enhanced disclosure and reporting of corporate giving

The Australian Government should introduce a requirement for listed companies to publicly report itemised information on their donations of money, goods and time to entities with deductible gift recipient status. This would enhance accountability to shareholders, consumers, employees and other stakeholders within the community.

The Australian Taxation Office (ATO) should amend the company tax return to require listed companies to report donations of money and assets to entities with deductible gift recipient status as a distinct line item in deductions, similar to what is required for individuals.

The ATO should regularly publish aggregate information on corporate giving in Australia (for example, in the Australian Taxation Statistics) including, at a minimum, donations by company size, taxable status and industry.

The company tax return (single company) and consolidated group tax return are a single format for all companies and all consolidated groups to complete.

For the company return the inclusion of the requirement to separate donations will apply to all company tax returns, listed and private companies.

For the consolidated group tax returns, the taxation information is for all entities in the consolidated group of entities but is disclosed in the tax return of the head entity.

Many listed corporate groups and large family private groups have established a foundation that will either be a stand alone charity (foundation) or will be an ancillary fund.

The donation within the listed / large private group will include tax deductible donations to the associated charity or ancillary fund. The associated ancillary fund will then be providing donations to Type 1 DGR registered entities.

Many listed companies will choose to provide a sponsorship to a charity rather than a donation. Under a sponsorship arrangement the brand of the sponsor is able to make prominent, providing ongoing benefits to the listed company to demonstrate its social commitments.



Information request 10.2

Accessing professional advice on philanthropy

The inability to access high-quality professional advice on philanthropy could prevent some people from identifying giving opportunities or making decisions that align with their preferences. The Commission is seeking information on professional advice on philanthropy.

- Evidence that people who use professional financial services would value and are willing to pay for professional advice on philanthropy, but are unable to source that advice.
- Information on specific regulatory or other impediments (if any) to people accessing advice on philanthropy and ways to address them.
- Evidence that an inability to access professional advice is materially affecting giving or resulting in harm to donors.

BDO provides a wide range of professional services including financial planning advice by appropriately licenced advisers. The BDO experience is that those individuals and businesses that are contemplating a philanthropic course of action will engage their professional advisers to ensure that their objectives of that consideration are met.

This advice will include the option of direct philanthropic support of a particular charity or charities, establishment of a PAF, establishment of a social enterprise, and establishment of a charity.

In addition, the BDO experience is that individuals and businesses will engage their professional advisers as part of an estate planning process where the will may include bequests.

Professional advisers will include accountants, lawyers and financial planners. The planning relating to philanthropic course of action, bequests etc all require the adviser to apply their knowledge of the client their business and financial structures and the clients' personal objectives.

BDO also provides professional support to smaller accounting firms that seek specialist knowledge relating a particular matter so the knowledge about the client is blended with the technical expertise.

In various jurisdictions there is a free government supplied service to assist individuals who do not wish to engage professional services when that individual wishes to prepare a will and consider bequests. In Queensland for example the Public Trustee of Queensland provides the support for will preparation and is closely aligned with the foundation known as Queensland Gives. This foundation offers the individual the opportunity to establish a compartment where the funds remain with and are invested by the foundation and then distributed in accordance with the testators' request.

In addition, all non-government DGR entities are required to be a charity registered with the ACNC. To maintain their registration with the ACNC, most charities are required to lodge an Annual Information Statement (“AIS”) and depending on the category of charity, financial statements.

Members of the public can search, at no charge, the details of a registered charity including:

- The objects of the charity as per its governing documents;
- The responsible persons;
- The activities of the charity and the plans for the year ahead;
- The range of activities of up to ten projects;
- The financial position and result of the charity; and
- The status of its registration with the ACNC.

Based on the experience of the firm, BDO considers that those who wish to consider philanthropy will either access their regular advisers or can access other resources. Consequently, there is limited need to establish additional services.