Productivity Commission:
Review of Philanthropy

Submission made by:
Australian Philanthropic Services
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1. Introduction

Australian Philanthropic Services (APS) welcomes the opportunity to lodge this submission with the Productivity Commission. The submission concentrates on the area of structured philanthropy and details the current barriers to the growth of structured philanthropy which are largely:

- misconceptions held by the community at large about philanthropy generally.
- a lack of awareness about structured philanthropy and its benefits.
- and a lack of knowledge amongst professional advisers such as accountants, financial advisers and lawyers.

2. Australian Philanthropic Services

APS was launched by Chris Cuffe and Michael Traill as the Social Ventures Australia (SVA) Private Ancillary Fund Service in 2010 and spun out into its own entity in 2012. APS celebrated its 10-year anniversary in 2022 with a small event at Admiralty House kindly hosted by the Governor General.

APS works in structured philanthropy and only does three things:

- it provides an all-encompassing accounting, administration, and compliance service for its private ancillary fund (PAF) clients.
- for its clients who have giving funds within our public ancillary fund (PuAF), the APS Foundation, it does all that in addition to managing the investments of the pooled funds.
- it offers giving support to its clients across the two offerings.

Since 2012 APS has grown from a team of three and 14 PAFs to a team of 34 and 320+ PAFs and 420+ clients with giving funds in the APS Foundation. It is the fastest growing PuAF in the country and APS consistently establishes about a third of all the PAFs created each year. Over the last decade, from a standing start, APS clients have given away over $600M to charities and now have over $2BN in funds irrevocably donated into ancillary funds for the future use of the community.

Importantly, APS is a charity itself, is registered with the Australian Charities and Not for Profits Commission (ACNC) and has Item 1 Deductible Gift Recipient (DGR) Status.

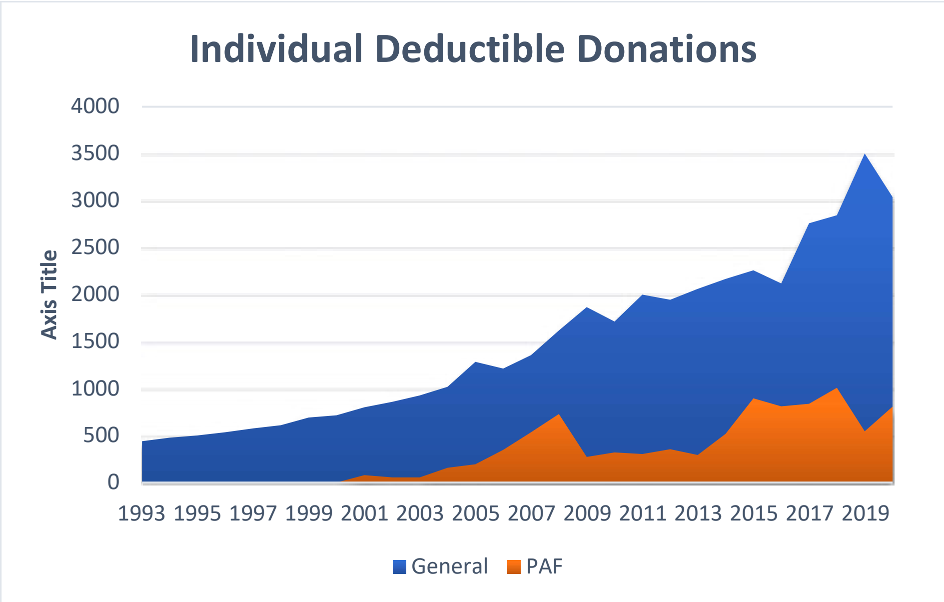
3. Doubling philanthropy by 2030

APS supports the government's goal and the peak body's goal of **doubling (structured) philanthropy by 2030**. It is something we are entirely comfortable with as over a comparable timeframe of the last seven years the amount of giving by APS supported clients has doubled and then doubled again from $35.5M in FY2016 to $139M in FY2022.

By any measure the APS model has been successful in growing philanthropy more so than the overall sector and APS' growth over the last decade is evidence that ancillary funds, both private and public, are effective vehicles in encouraging philanthropic giving and supporting the charitable sector.

4. Barriers to philanthropy

Australians are generous people which is evident from the immediate response to natural disasters with significant increases in giving for the 2004 Asian Tsunami, 2009 Black Saturday Bushfires, 2017 Brisbane Floods and 2019 NSW Bushfires.



Source ATO Statistics

4.1 Public perceptions limit growth

4.1.1 Misconception that "Philanthropy is only for billionaires".

It is terrific to see some ultra-wealthy people being open about their philanthropy in order to inspire other ultra-wealthy people to give or to give more; but the focus on the ultra-wealthy, while understandable from a charity fundraising perspective, gives the impression that philanthropy is something billionaires engage in rather than it being a community wide activity with each person giving to their capacity.

There are only so many philanthropically minded billionaires in the country. The growth in giving needed to meet the 2030 goal will come from wealthy and comfortable Australians who have the capacity to give but don't know about structured giving. This is the area of specialty for APS.

4.1.2 A more sophisticated understanding of charities and their impact would be welcome. There is an over focus on administration costs when donors are assessing whether or not to support charities without an understanding of impact or outcomes or contextual costs.

4.1.3 The joy and satisfaction of giving is generally totally underestimated. APS clients, regardless of their different interests in terms of giving, almost uniformly express two thoughts after engaging with APS for a period: they wish they had started giving earlier and they are surprised by the absolute joy it brings them.

Question: Who is advocating for giving generally? No one.

Suggested solution:

✓ A widespread public funded campaign promoting the community, social and personal benefits of giving to broaden Australian giving culture beyond just as a response to natural disasters.

4.2 The public and professional advisers lack of knowledge

4.2.1 Structured philanthropy is a niche area and unknown to most financially comfortable Australians. Even amongst professionals the level of knowledge is low. Here are a couple of recent examples of the lack of knowledge amongst those who should know.

- In a March "Ask an Expert" column in a major daily paper a writer asked how best to make a bequest to charity of some Australian listed shares. The expert advised the writer that their estate would have to sell the shares, pay capital gains tax (CGT) on the disposal, and then pass the net amount to the charity. This is not the full story. A better result would be to transfer the shares in specie to a DGR tax-exempt charity, there are over 20,000 of them including ancillary funds, and allow the charity, as a tax-exempt entity, to dispose of them thus boosting the amount given to the charity. The charity receives more as no CGT would be paid.

- An APS client was recently advised not to make any further donations into their PAF because in the view of their professional adviser there was no further taxable income to offset in that financial year. The professional adviser was unaware of the 5 year Spread Rule on donations into DGR charities. Once made aware, the client was able to make a large, irrevocable donation into the PAF, in the knowledge that the tax deduction could be used over the next 5 years. The result is more funds in the PAF for the future use of the community.

4.2.2 Public Ancillary Funds (PuAFs) generally are not well known or understood, yet they are an approachable way for people to begin structured giving with modest amounts. APS has a minimum requirement of $40,000 but some PuAFs have smaller minimums as starting points. Some financial advisers are particularly cautious because they lose control of their clients' funds (and lose the fees that flow from the management of those funds) once irrevocably gifted into a PuAF. Others are very supportive of their clients' philanthropic goals.

4.2.3 Accountants and lawyers mostly only have one or two clients involved in structured philanthropy so don't invest in either initial knowledge or in maintaining their knowledge base. Most accountants and lawyers only think of philanthropy in terms of bequests or immediate tax relief for the current tax year, rather than thinking of the long-term benefits of structured philanthropy for their clients' and the community's future.

Many potential donors who come to APS have already sought advice from their accountant, lawyer, financial adviser and gotten nowhere. One of our clients tells the story of having their recommended specialist lawyer talk to their accountant about structured philanthropy. They both billed her for their time but decided nothing and came up with no solution!

Suggested solution: In addition to community awareness solution above:

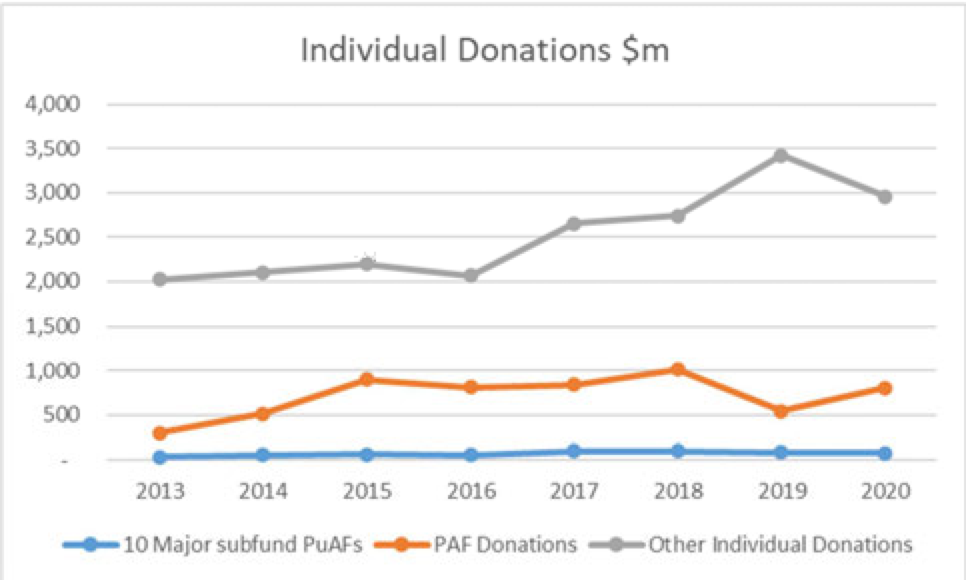
✓ Inclusion of a mandatory module about structured giving in professional courses for accountants, lawyers and financial advisers would shift the dial in a decade's time as new graduates take up roles but in the shorter term including mandatory Continuing Professional Development (CPD) training for financial advisers, and accountants and lawyers around structured giving and integrating the topic into Annual Conference Programs would bring current professionals up to speed.

4.3 Public Ancillary Funds restrictions are curtailing its potential major role in Philanthropy

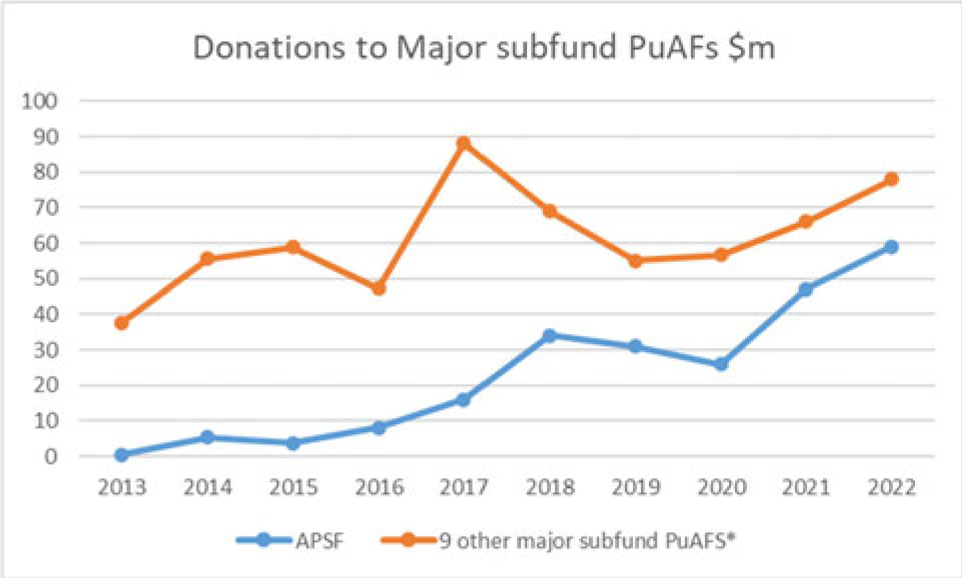
PuAFs are a great structure for busy philanthropists who want to expend all their limited energy on community engagement and grant making (and not on administration or investments, leaving those to a professional). They are also appropriate vehicles for place-based Community Foundations.

Donor Advised Funds (DAFs) are enormous in the U.S.A. (Fidelity Charitable being the best example https://www.fidelitycharitable.org/). PuAFs have been in Australia since 1963 but they have a long way to go to reach their potential.

The substantial growth in recent years in our PuAF, the APS Foundation, shows the possibility but that growth has not been replicated across the sector.



Source ATO and ACNC Data



Source ACNC Data - estimate for Equity TCF for 2022 as not yet reported.
Adjusted for estimated Foote donations in 2013 and 2014

Suggested solutions:

- ✓ Changes in PuAF Guidelines needed for more donor "influence" over grant recommendations.
- ✓ Taxation Determination (TD) 2004/23 requires softer words to give donors assurance that their wishes on grant recommendations distribution will hold weight (still without fettering Trustee responsibility).
- ✓ Engagement and grant due diligence expenses that would be eligible expenses for PAF donors should also be eligible expenses for PuAF donors.
- ✓ Consideration be given to PuAFs being given a grant to enhance marketing and community awareness.

4.4 Do we need more tax incentives?

The current tax incentives are reasonable and crucial to build philanthropy and must be retained. We do not believe there is a need for further substantive initiatives. People don't understand the ones we have!

- Ancillary funds offer full donation tax offset (to zero taxable income) with ability to spread deductibility over 5 years.
- Families can maintain control of their family foundations (with an independent director and comprehensive and transparent reporting to the ACNC and the ATO).
- Charitable foundations are tax exempt with franking credits refunded.

We believe there is no need for additional tax incentives – particularly if they are complex as they may just muddy the waters and make it even harder for potential philanthropists to get coherent advice.

4.5 Is the 5% minimum distribution for PAFs too high?

The minimum 5% distribution requirement for PAFs is not a major issue in our view. While 5% is challenging it is not unreasonable given the 100% tax deductibility of donations. While maintaining the ATO Commissioner's current discretion, which in our experience has been judiciously used, we would go no further than aligning PAF and PuAF Guidelines both at 4% as that would remove confusion.

5. General comments and suggestions

5.1 Legislation

We believe two important principles have underpinned the success of the ancillary fund framework:

- Clarity, simplicity, transparency, and integrity of the compliance framework
- Longevity without frequent change and all changes involving consultation.

The stability of the ATO Ancillary Fund Guidelines is very important for donors who do not wish to see frequent changes. There are, however, opportunities for tidying some practical irritations in regulation and legislation that Treasury never quite has the bandwidth to deal with due to other priorities.

A short sharp focus by Treasury on these easy fixes would be very welcome:

5.1.1 Portability

Portability, with ATO approval, to move from one ancillary fund to another, should be viewed as a large improvement in consumer rights, an issue we know the Commission is interested in, but it is not well known and has not been embraced by some sector participants as it should be.

Here is an example of the current limitations: last year a client approached APS wishing to port into the APS Foundation, from a sub-fund within a large trustee company PuAF. Even though the sub-fund had itself met its minimum 4% grantmaking requirement, the PuAF had not met the 4% minimum requirement overall and did not meet the minimum requirement until the last week of June. Application to the ATO could not be made until the 4% had been met and it was an extremely stressful race to meet the 30 June deadline before the new financial year would start the clock again on another round of 4%.

A small change to the ATO PuAF Guidelines Section 27(1)(b) by applying the 4% minimum at sub-fund level would relieve this pressure and grant donor/consumers the ability to move more readily.

5.1.2 Divorce clause

A small change to Section 28 of the ATO PAF Guidelines would allow a PAF to be easily split in the event of divorce or similar which would be helpful in allowing portability of half of a PAF to another ancillary fund so both parties can continue giving.

5.1.3 PuAF and PAF Guidelines Section 22 (3) Reinstate "material" before benefit

This clause is not designed to capture immaterial benefits and should be consistent with the general wording in TR 2005/3 "what is a gift" which uses the word "material" in relation to benefit. If there is a benefit which is not material the penalty for the breach under this Section is "the value of the benefit". So, in the case of an immaterial benefit being inadvertently provided, the penalty will be similarly immaterial and certainly not worth the effort or angst by the PAF Trustee or the ATO in working this out. So, what is the point? Are there not more important matters that ATO resources could be focused on?

5.2 Other regulatory matters

5.2.1 ACNC reporting date

31 January is not practical reporting date for PAFs which are discretionary investment trusts with a diversified investment portfolios for the following reasons:

- Some investments do not issue annual tax reports till November or later.
- There is an obvious loss of time from mid-December to mid-January in terms of school holidays, business closures and the potential for directors to reasonably be away during the holiday period.
- All PAFs need to be audited at roughly the same time, creating a choke point with professional auditors who also, quite reasonably close, for a short time over the Christmas break.
- It is a misalignment of dates if there is a family trust making distributions to the PAF as the family trust might not produce tax documents needed by the PAF's auditor until the trust's reporting date which is May.

Suggested solution:

✓ More practical dates would be 28 February which is when PAFs used to report to the ATO prior to the ACNC coming into existence in 2014; or 15 May, similar to other entities that report to the ATO and have a tax agent. This might sound like a small issue but the impact on staff and clients is serious and acts as a disincentive for the professionalisation of structured giving.

5.2.2 ACNC Privacy regulation

This has been a matter of some discussion over time with the ACNC but it is hamstrung by the regulations which do not sit in alignment with the Explanatory Memorandum or Second Reading Speech. It would be much clearer if Treasury could find the bandwidth to fix the regulations to work as intended so all PAFs can access privacy easily if they wish. About half of existing PAFs have privacy. Why should the rules around privacy of giving be different for individuals as opposed to private ancillary funds? Yet they currently are: individuals can receive the same tax deductions for giving to charities but PAFs, unless granted withholding from the ACNC Register, need to display annual financial statements for all to see; including potentially other family members, ex-partners, current and former employees, and competitors.

5.3 Data

The ACNC now has several years of data but who is doing analysis? To date, we still don't know how many charitable trusts there are in Australia and is the number growing or shrinking?

The ATO provides good data on PAFs but the PuAF data needs dissection. Overall PuAF numbers are falling but sub-fund numbers are growing.

5.4 StartGiving

We understand that StartGiving has already had discussions with the Productivity Commission, and we support their approach of using in specie donation arrangements and gaining a better understanding of the ATO Valuation process to support tech entrepreneurs locking away a small proportion of current equity in the hope that the philanthropic sector captures the value of the next Atlassian or Canva as a community resource.

5.5 Pledge 1%

We also support Pledge 1%'s submission relating to the complexity of the value shifting rules and their impact on corporate entities wishing to make a legally binding pledge to donate equity to an Australian DGR entity.

Removing the obstacles to the StartGiving model for individual philanthropy and the Pledge 1% model for corporate philanthropy would be helpful toward meeting the government's goal by 2030.

5.6 Public Beneficial Ownership Register (PBOR) Discussion Paper

We have been involved in consultation around the forthcoming legislation establishing a **Public Beneficial Ownership Register.** Charities are too often not considered in the drafting of general legislation and PAFs appear never to be considered. The introduction of the Common Reporting Standards (CRS) is a good example of this. Charities were exempted from this legislation in some other OECD countries but not here. The CRS is intended to capture the movement of funds to other jurisdictions with the intentions of ensuring the integrity of the tax system. For ancillary funds, which can only make gifts to Item DGR entities which are all Australian tax residents, the legislation is irrelevant. Nevertheless, ancillary funds are obliged under the legislation to consider every year if they need to report around the issue, come to the same consultation every year and minute the consideration. It would be disappointing if ancillary funds specifically and charities generally ended up with a similar result under the Public beneficial Ownership Register; that is additional administration for no community benefit. We suggest that charities be exempt from the PBOR legislation or, if that is not achievable, then apply a carve out so only charities with Significant Contracts on their books should need to report.

5.7 Common Reporting Standards

The Common Reporting Standards (CRS) application to charitable trusts creates significant administrative burden mostly in determining a nil report. Where occasionally reporting is required, generally it is a duplication of a subset of the ACNC External Conduct Standards. Charities should be removed from CRS.

6. Charity grant programs

On the question of Treasury efficiency of philanthropic tax incentives (donation deductibility, income tax exemption and franking credit refund) the comparison should be made with the various (and numerous) government grant programs which often have substantial bureaucratic cost which is (necessary for fully public funds) and a high administration cost for recipient organisations.

Suggested action

We would hope the Commission's investigation would include whether philanthropy tax forgone or government grant programs are the most efficient way of getting funds to **priority** community projects.

7. Conclusion

APS works only in structured giving but the principles that apply in this area can be equally applied in all areas of giving.

7.1 The rules and legislative context need to be simple, stable, and approachable.

By and large this is true for the area of structured giving. We would suggest a small project with Treasury to tidy some of the regulatory issues that are irritants or barriers to increased giving. No complex or additional tax arrangements are necessary; in fact they could be counter productive; transparency and building a general culture of giving requires that the tax rules be the same for billionaires as for a PAYG workplace donor.

7.2 Public education and professional education are integral

A publicly funded campaign promoting a culture of giving would be helpful. The "You can't be what you can't see" approach indicates the campaign should not be about billionaires, who have the resources to drive their own campaigns targeting other ultra wealthy people, but instead showcase wealthy, comfortable Australians who already give.

Professional education both long term in professional qualifications and immediate in CPD education sessions and conferences will promote professionals being able to better advise clients of their options around structured giving.

7.3 Public ancillary funds (PuAFs)

The growth of the APS Foundation is evidence that well managed, well invested public ancillary funds are the sleeper vehicles to achieve the goal of doubling (structured) giving by 2030. They are accessible in terms of starting sums and provide the overarching investment, compliance, and administrative architecture so that donors can concentrate only on their giving. In terms of consumer/donor protection, portability needs to be better understood by the sector and a small tweak to the ATO Guidelines would help. Public and professional education are the keys to growth in this area and we are doing our best, but as a charity, APS does not have the resources to drive change at the level required. A government funded campaign supporting a culture of giving would be very welcome.

Thank you for the opportunity to make this submission.

We look forward to participating further in whatever way would best assist the Commission in concluding its report into Philanthropy in Australia.

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David Ward, Technical Director