

PRODUCTIVITY COMMISSION: REVIEW OF PHILANTHROPY

Submission from StartGiving (May 2023)

Introduction and scope of review

StartGiving (ABN 13 655 567 767) is an Australian not-for-profit organisation inspiring a new movement of giving in the innovation community.

We support successful start-up founders and tech execs to launch personal charitable foundations by connecting them to ideas, experts, and like-minded peers. StartGiving is fully funded by our founder and Chair, Daniel Petre AO, and does not charge any fees.

Our mission is to change the culture of philanthropy in this cohort of Australians – making giving for them the expectation and the norm.

StartGiving is pleased make this submission to the Productivity's Commission's Review of Philanthropy. We note the purpose of the inquiry is to understand philanthropic giving in Australia; to identify opportunities for and obstacles to increasing philanthropy giving; and to recommend ways to respond to these opportunities and obstacles.

This submission provides general information that contributes to the Productivity Commission's overall analysis of giving trends and specifically addresses: Scope of Inquiry Item 2 to identify opportunities to increase philanthropy; Item 3 to examine barriers to philanthropic giving; and Item 6 to identify ways to address barriers and harness opportunities to increase philanthropy.

Background and opportunity

Australia has experienced an unprecedented tech boom in the ten last years, creating around 100 tech companies valued at over \$100 million.¹ There is untapped potential among founders and execs in these companies who have the capacity to establish a private ancillary fund (PAF) and make a significant contribution to the Australian philanthropic sector.

Our focus in this submission is on founders or other equity holders of tech companies who are still building their companies and have yet to realise any significant financial returns. Their main asset is a portfolio of shares in their company which is unlisted and private.

We believe that motivating donors to donate shares in their company to a PAF will enable them to have a materially greater impact on the charitable sector as they are:

- Contributing to the philanthropic sector sooner, as their donation is not contingent on a liquidity event occurring years later (e.g., an acquisition or Initial Public Offering (IPO) of the company they founded); and
- Giving an asset with significant growth potential.

¹<https://techcouncil.com.au/wp-content/uploads/2021/10/2021-October-Roadmap-to-Deliver-One-Million-Jobs.pdf>

By contributing shares sooner, they are also having a lower impact on the tax system as the deduction claimed is likely to be lower than it would be when a later liquidity event occurs. Early donations minimise tax system impacts but maximise future philanthropic value.

With the Albanese government's commitment to double philanthropy by 2030, we believe that the proposal we have outlined provides a low risk and high return program that focuses on this election promise.

The current obstacle

Under the current Australian Taxation Office (ATO) administration process, donors who are gifting unlisted shares over \$5,000 are required to have gifted their shares to their PAF before the ATO undertakes the valuation and when they can claim a deduction on their tax return.

The impact of this arrangement is to create uncertainty and concern that there may be a mismatch between the market valuation of the shares and the ATO's valuation.

If there is a dispute, the donor would have already transferred legal title to the shares without the ability to retrospectively unwind the transaction.

Further compounding this issue is the fact that the donor's shares are in unlisted tech startup companies and their price (or value) is not referable to any stock exchange or listed market.

Opportunity to increase giving

We would like to see a simple and repeatable approach for valuing donations of unlisted equity that makes the creation and administration of PAFs as risk free as possible, both for the ATO and donors, thus encouraging more philanthropy.

To achieve this, it is imperative that certainty is available for the valuation process prior to the legal transfer of the shares to the PAF. Resolving this aspect clarifies the donor's tax implications as it relates to gifting shares to the PAF.

We believe this is a matter that can be addressed through a procedural clarification by the ATO and does not need legislative change.

The methodology that StartGiving proposes is one of several valuation methodologies currently used by the ATO. We suggest making it the default methodology.

A standardised valuation process would encourage donors to start contributing to the charitable sector earlier (rather than waiting for a liquidity event to happen). By gifting shares (rather than cash), donors are contributing an asset to the philanthropic sector that has significant growth potential and is intended to provide increased support to charities in the future.

Proposed approach to valuations of certain types of unlisted equity

We believe that an appropriate approach to valuing a donation of unlisted equity to a PAF is to use the latest institutional funding round for valuation.

When a donor gifts shares in their tech startup to a PAF, the only valuation that has been tested with rigour is the valuation of the company at the last institutionally-led funding round.

We propose that an acceptable funding round that can be used to value the shares donated to a PAF would apply where:

- The last funding round was within a reasonable timeframe;
- The last funding round was led by well-regarded, scaled institutional investors (i.e., investors who are investing other people's money and so have more formal and measured approaches to making investments). This construct provides a transaction involving a willing buyer and a willing seller; and
- Institutional investors took more than 50% of the funding round.

This should be the case whether the funding round was an 'up' round or a 'down' round.

There are situations outside of a funding round where the company valuation is decreased (not due to a formal down round) and published externally by institutional investors in the company. We expect that a revaluation of this type, outside of a funding round, would be viewed as a materially adverse event by the ATO and would also need to be taken into consideration in valuing the unlisted equity donated to the PAF.

Additionally, we propose that as an integrity undertaking to the donation process, a declaration is made by the company founder (or executive) at the time of the donation to declare that, to the best of their knowledge, no down round or valuation downgrade is anticipated in the upcoming three-six months.

If this approach is clarified and adopted, then the ATO as administrator has a well-documented valuation methodology applicable for both the initial and the annual PAF valuation, and donors have greater confidence around how their donation will be valued.

Policy suggestion for consideration

We are open to ideas on how to improve the current situation, which includes a pilot program limited to specific circumstances and categories of taxpayers, to explore what is possible within the ATO's existing powers. This program could also demonstrate methods to increase giving (as well as protecting tax revenue).

We would like to highlight that:

- The specific circumstances of the pilot would involve a donation of unlisted equity that follows an institutionally-led funding round which has resulted in an arm's length market valuation/transaction with a willing commercial buyer and willing seller.
- This restricted pilot program would also involve a reasonable and verifiable process, as distinct from just any gift of shares or any start-ups that are only at the stage of being self-funded.

Using a standardised valuation method that is captured, shared, and applied across similar situations can improve integrity, assist the market, reduce compliance costs, provide certainty, and increase philanthropy.

A pilot program could have six- or twelve-monthly joint reviews, and even a designated ATO point of contact to ensure consistency and integrity, and to ensure the program is working as intended by all parties.

OTHER MATTERS

Corporate philanthropy by tech companies and Pledge 1%

StartGiving's proposal relates specifically to *personal* philanthropy by tech founders.

Pledge 1% is an organisation that encourages *corporate* philanthropy among tech companies. Pledge 1% encourages businesses to pledge to use 1% of equity, profit, employee time and/or product for social impact.

We are aware of the submission made by Pledge 1% which relates to corporate philanthropy. Pledge 1% is seeking to find a way for companies to make a legally binding pledge to donate 1% of its equity capital to an Australian non-profit with DGR registration, effectively for nil consideration. Due to the complexity of value shifting rules, this is currently not possible. Pledge 1% has proposed an approach to address the existing impediment to this form of corporate philanthropy which is to make a direct value shift in favour of a charity with Deductible Gift Recipient registration a specific exclusion from Division 725 of the Income Tax Assessment Act 1997.

We support the proposal being made by Pledge 1%.

Philanthropy Australia submission

StartGiving is a member of Philanthropy Australia and has contributed to their submission being made to the Commission.

We support the submission being made by Philanthropy Australia and would be happy to provide further commentary on the issues it addresses, if required.

Thank you for providing us with the opportunity to participate in this inquiry.

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