

07 February 2024

The Productivity Commission

www.pc.gov.au

Dear Sir/Madam,

PRODUCTIVITY COMMISSION'S REVIEW OF PHILANTHROPY,

Please find attached a submission in relation to the Draft Report's, information request: 8.3.

Regulatory arrangements for charitable trusts by licensed trustee companies.

The Commission is seeking further evidence regarding the administration of charitable trusts by trustee companies, given changes over the past 10 years that have led to further concentration in the market for licenced trustee services. This includes information about arrangements for switching providers or charging fees, particularly for funds held in perpetuity.

The Commission invites views on whether there is a need for policy reforms in relation to the administration of charitable trusts by licensed trustee companies, and if so:

- *the nature and rationale for any proposed changes*
- *accompanying evidence, such as data or case studies*
- *any potential role or implications for Australian regulators.*

Morgans (previously known as RBS Morgans) made a submission to the Corporations and Market Advisory Committee (CAMAC) inquiry into the administration of charitable trusts managed by **Licensed Trustee Companies (LTCs)** in 2013 and agrees with the findings and recommendations put forward by CAMAC, in their report date 10 May 2013.

Unfortunately, as highlighted in the CAMAC report, there is a 'deficit of relevant and indisputable information on' the state of the administration and the fees charged by trustee companies. What's more, there are over 2000 charitable trusts, investing over \$6billion, in perpetuity, where there is only one entity with the relevant information, and they are a sole trustee and an LTC. As such, there is little to no independently verified information on the fees these charitable trusts are being charged and no evidence of switching.

Consequently, our submission comments primarily on the areas for policy reform, in particular:

- The urgent need for the stewardship audits recommended by CAMAC.
- Why all fees, charges, remuneration, commissions et cetera must be fair and reasonable, and
- Key legislative enhancements, to judicial processes, to support the governance and accountability of trustees.

If there is anything we can do to further assist your inquiry, please contact Ken Howard.

Regards

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Morgans

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Abbreviations:

CAMAC	Corporations and Market Advisory Committee
LTC	Licensed Trustee Company

Australia’s largest LTCs

LTC	Charitable trusts	Annual giving	Funds under management	Number of specialist staff
Equity Trustees*	1000 trusts	\$100 million	\$3.0 billion	20 specialist staff
Perpetual **	1100 trusts	\$120 million	\$3.3 billion***	16-person philanthropy team
TOTAL	2100 trusts	\$220 million	\$6.3 billion	36 specialist staff

Source:

* Productivity Commission, *Philanthropy inquiry, submission 259, Equity Trustees, page 1*

** Productivity Commission, *Philanthropy inquiry, submission 254, Perpetual, pages 1 and 6*

*** Perpetual 2023 Annual Report page 93

A summary of the CAMAC recommendations.

Stage 1:

- Conduct stewardship audits of a cross-section of charitable trusts administered by LTCs to address the deficit of relevant and indisputable information on the state of administration of charitable trusts.
- Introduce a 'fair and reasonable' requirement for all fees and costs charged against a charitable trust, and
- Change the judicial dispute resolution procedures to enhance access to the court and broaden the remedial powers, including whether the fees and costs charged against a charitable trust are excessive or whether a LTC should be replaced as the trustee of a charitable trust.

Stage 2:

- Would build on the information gathered from the stewardship audits and focus on what, if any, additional changes to the regulation of administrative arrangements for charitable trusts are required to promote the primary intent of the donor (*that is the philanthropic or benevolent purpose or objectives for which the donor established and funded the charitable trust*).

The public benefit role of charitable trusts, distinguishes charitable trusts from private and commercial trusts and for this reason, the advancement of the primary intent of the donor, should not be degraded by drafting (*potentially many decades old*), which for example did not contemplate the efficiencies of a modern computerised administration system, or cost-effective access to global investment markets, nor changes the government may make to the regulation of LTC services for charitable trusts.

The need for stewardship audits.

The fees allowed under the Corporations Act (*sections 601TDD & 601TDE*) are reminiscent of the 1980's and 1990's. In all areas of the financial services sector, where there is transparency and competition, fees have fallen to a fraction of the fees allowed under sections 601TDD and 601TDE.

601TDD	Annual management fee (includes GST)	1.0560%
601TDE	Common fund administration fee (includes GST)	1.1000%

In addition to these fees, LTC's asserted in their CAMAC submission, that Investment Management Services are not covered by Chapter 5D of the Corporations Act (*refer page 21 of the final CAMAC report*).

These 'investment management services' could include:

- Preparation of investment proposals
- Preparation of investment strategies
- Provision of investment research
- Preparation of investment recommendations
- Implementation of investment recommendations
- Performance reporting
- Regular asset allocation reviews
- Regular portfolio reviews and
- Management of pooled investment vehicles,

In other words, even in today's competitive financial services industry, it is entirely possible that the provision of investment services could add an additional 1.1% or more the costs of the charitable trust, and these services could be provided by an associate of the LTC.

So, it is entirely possible, that the charitable trust is paying the trustee company or an associate of the trustee company:

- An annual management of fee of 1.056% (*601TDD*), *plus*
- A common fund administration fee 1.1% (*601TDE*), *plus*
- Investment fee(s) (*apparently not covered by Chapter 5D*) as guess, 1.1%, *plus*,
- Additional expenses and outgoings, for example to cover the cost of a tax-return.

Total (*potentially*) 3.256% (*plus*) per annum.

I would hasten to add, that this illustration is mere speculation, as opposed to an assertion of what is occurring and this is why the stewardship audits, proposed by CAMAC, are an essential prerequisite to an informed discussion around the future regulation of LTC services provided to charitable trusts.

‘Fair and reasonable’ costs.

As mentioned above, there is very little, publicly available, verifiable information around the services currently being provided and the fees charged for those services, which is why it is prudent to introduce a ‘fair and reasonable’ requirement into the legislation for all fees, costs, remuneration et cetera being paid, from the income and or capital of a charitable trust.

There were several formulaic arguments presented to CAMAC, to replace the maximum caps in sections 601TDD & 601TDE. In essence they were all attempting to define how you could determine if a charge; be that for trustee services, management services, administration services, investment services or any other services reasonably required in achieving the primary intent of the donor, was ‘fair and reasonable’.

So, in short it doesn’t matter if an LTC uses a:

- Fee for service model with hourly rates, or
- Scaled fee model, or
- An unbundled / disaggregated / outsourced model or
- Any other model

If the costs the LTC is agreeing to, in their capacity as trustee, and imposing on the charitable trust, are ‘fair and reasonable’ and for services reasonably required for achieving the primary intent of the donor.

For illustrative purposes, I have included some fee comparisons, similar to those included in the Morgans submission in 2013, with equivalent figures from 2023, albeit we certainly accept CAMACs comments, that there are material differences in the scale, operation and services provided by industry and retail superfunds, with the services provided by an LTC to charitable trusts.

However, the point of including the data in 2013 was simply to illustrate the fees charged by an efficient and competitive industry operating at scale, (*both the ‘for’ profit and ‘not for’ profit providers*) to give the fee limits in the Corporations Act some perspective.

An illustration of fees in superannuation.

AustralianSuper 2023

Reference: Member guide dated Nov 2023, downloaded from the website <http://www.australiansuper.com> on 19 January 2023

Page	Details
Page 5	Investment Fees for Balanced option <ol style="list-style-type: none"> Investment fees 0.40%, plus Performance fees 0.10%, plus Transaction costs per annum 0.06% TOTAL 0.56% p.a.
Page 2	Member fees <ol style="list-style-type: none"> Weekly fee of \$1 per week, plus An asset-based fee of 0.10%, capped at \$350 p.a.

Investment Option	Amount invested	
	\$ 1,000,000	\$ 5,000,000
Balanced (<i>with performance fee</i>)	0.60%	0.57%
	\$6,002	\$28,402

Perpetual Select Super Plan 2023

Reference: PDS Downloaded from the website <https://www.perpetual.com.au/resources/continuous-disclosure-and-important-information/superannuation/perpetual-select-super-plan-updates/> on 25 Jan 2023,

Page	Details
Page 6	Fees for the balanced option <ol style="list-style-type: none"> Investment fee 1.17% p.a. (includes an estimated performance fee of 0.17%), + Transaction costs estimate 0.13% p.a. A total potential annual fee of 1.30% But there is an investment fee rebate for balances over \$900,000 of 0.32%
Page 6	Administration fees and costs <ol style="list-style-type: none"> 0.10% per annum

Investment option	Amount invested	
	\$ 1,000,000	\$ 5,000,000
Balanced (<i>with performance fee</i>)	1.37%	1.14%
	\$13,680	\$56,880

Potential LTC fees applied to charitable trusts.

An illustration of the potential fees, and I say potential because,

(A) The actual fees imposed on over 2,000 charitable trusts, with \$6 billion plus in assets, is not in the public domain.

(B) It is entirely plausible that without transparency, and without competition, a for-profit service provider would charge what they are allowed to charge, under the trust instruments and the legislation. and

(C) Based on submissions to the CAMAC inquiry, over 90% of these charitable trusts have a for-profit service provider, either Perpetual or Equity Trustees, acting as the sole trustee.

	Potential LTC fees applied to a Charitable Trust	
Capital	\$ 1,000,000	\$ 5,000,000
Annual Management Fee	1.056%	1.056%
Common fund administration fee	1.10%	1.10%
Investment fee(s)	1.10%	1.10%
Total potential fees	3.256%	3.256%
	\$32,560	\$162,800

Compared to the fees of:

	Australian Super	
Capital	\$ 1,000,000	\$ 5,000,000
Balanced (with performance fee)	\$6,002	\$28,402

Or

	Perpetual Select Super	
Capital	\$ 1,000,000	\$ 5,000,000
Balanced (with performance fee)	\$13,680	\$56,880

It is true that there are differences between the; trustee, management, administration, and investment services provided to charitable trusts and superfunds, and there are material differences in the scale of operations like Australian Super and the LTCs in Australia, which is why Morgans supports the CAMAC proposal for:

- A. Stewardship audits, and
- B. Amending the legislation to include a requirement for all charges to be 'fair and reasonable'.

The services being provided, and the fees and charges could very well be fair and reasonable, particularly for smaller charitable trusts, there is just no transparency, and a lack of standing for appropriate parties to seek judicial review, hence the need for policy reforms.

Enhanced judicial processes.

The Morgans submission in 2013 focused on portability, independence, and competition as the leavers for balancing the legitimate commercial interest of service providers with the primary intent of the donor, in perpetuity. However, as CAMAC points out, these policy tools are not as easy to apply once a donor is deceased, and there are a range of tools to improve access to, and reduce the time and cost, of judicial review, which are better suited to the governance of charitable trusts.

As recommended by CAMAC, enabling legislation should deal with:

- Standing to apply for a judicial hearing,
- Grounds for granting a hearing,
- Guidance on applying the primary intent of the donor,
- Powers of the court to make orders,
- Grounds for appeal,
- Costs of the parties, and
- Special rights and powers for the ACNC to supervise the management of charitable trusts.

The CAMAC recommendation addresses many of the areas of frustration for co-trustees and other interested parties seeking to improve the governance structure applied to perpetual charitable trusts. It certainly bears repeating, that codifying the right of co-trustees and or the donee(s) and or a potential donee(s) to apply; in good faith, where there is a genuine dispute over what's in the best of the Trust, for judicial review and where appropriate, recover costs from the Trust, will introduce a level of accountability, presently absent.

There are many tools open to legislators to reduce costs and time frames for judicial review by, for example,

- allowing courts, the discretion to appoint mediators, potentially a financial services ombudsman,
- allowing courts to appoint an independent co-trustee (paid or unpaid),
- allowing courts to order disclosure of relevant information to a co-trustee or relevant person.
- limit grounds of appeal to errors of law,
- to make it clear in law, that the primary intent of the donor prevails over any statement by the donor in a charitable trust instrument or otherwise, as to the administration and appointment of a particular Trustee. Or to put it another way, a Trustee can be replaced, notwithstanding the Trustee has not breached any legal or fiduciary obligation or requirement, if the court believes this is called for to achieve the primary intent of the donor.

Conclusion.

Under the current rules, there is little evidence of transparency or independent accountability for the efficient and effective management of over 2000 perpetual charitable trusts, where the sole trustee is an LTC. Collectively these trusts have over \$6billion in assets, to be managed in perpetuity, for a charitable purpose and the Stage 1 CAMAC recommendations will address three major concerns.

- **Transparency:** The proposed stewardship audits will provide relevant and reliable information for assessing the efficiency and effectiveness of the current framework,
- **Efficient and effective management:** Legislating, that all charges are to be fair and reasonable, should be sufficient to ensure that the costs imposed on charitable trusts, are meeting community expectations, while allowing the LTC to innovate and implement a competitive business model of their choice, and
- **Accountability:** Enacting enhancements to the current judicial processes, will provide an effective governance framework, should there ever be concerns around whether the management and administration of a charitable trust is achieving the primary intent of the donor.

As highlighted in the CAMAC recommendations, Stage 2 can build on the information gathered from the stewardship audits and focus on what, if any, additional changes to the regulation of administrative arrangements for charitable trusts, are required to promote the primary intent of the donor.

Thank you for considering our submission and if there is anything we can do to further assist your inquiry please contact Ken Howard via email

Regards

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