DF Mortimer & Associates

Law Institute Victoria
Member of the LIV

Our Ref: DFM:09/0005
Your Ref:

18 June 2010

Senate Inquiry into Charities and Public Benefit:
an inquiry arising from Tax Laws Amendment (Public Benefit Test) Bill 2010

By electronic upload

Dear Senators

Senate enquiry into public benefit test

We are pleased to present our submission to the Senate inquiry into Charities and Public Benefit: an inquiry arising from Tax Laws Amendment (Public Benefit Test) Bill 2010.

Who we are

DF Mortimer and Associates is a law practice that specialises in the law relating to not-for-profit organisations and charities. We have prepared this submission mindful of our current and prospective clients' need for:

- Maintaining public trust and confidence in the charitable sector; and
- A minimal administrative and regulatory burden on charities.

Executive summary

Overall, we support the introduction of a statutorily supported public benefit test ('the Test") which requires charities to demonstrate public benefit.

In our opinion the reliance by charities on a *presumption* that the public benefit test under common law has been met is not in accord with modern day principles of accountability and transparency; principles actually aspired to by the charity sector. That this presumption is relied upon by charities one needs only to look at transcript of proceedings of a case heard in the High Court on 15 June. [1]

[1] Transcript of proceedings, *Aid/Watch Incorporated v Commissioner of Taxation* [2010] High Court of Australia HCAtrans154.

DF Mortimer & Associates Pty Ltd
ABN 48 135 534 851
9/135 Mooltan Street
Travancore VIC 3032
P (03) 9370 9333
F (03) 9370 9333
www.dfmortimer.com.au
dmortimer@dfmortimer.com.au

Counsel for the applicant entity (which had seen its charitable endorsement revoked by the Commissioner of Taxation) states[2]:

> "it was not up to us to have to demonstrate public benefit. It was up to the Commissioner [of Taxation], if he sought to do so, to disprove any public benefit."

Our submission addresses what may be described as questions arising from "the devil in the detail" of the Tax Laws Amendment (Public Benefit Test) Bill 2010 ("the Bill") namely:

- Why does the Test only apply to charitable and other "institutions" but not "charitable funds"?;
- Does the Test replace or supplement the common law public benefit test?;
- Is it intended that the Test "principles" form part of the Test?; and
- Should the Minister formulate the Test?

Prior to addressing these questions we will make a preliminary comment on the Church of Scientology and denial of its charity status in Britain.

The Church of Scientology in Britain

The UK Charity Commission in its decision dated 17 November 1999[3] determined that the Church of Scientology (England and Wales) ('the Church") was not an entity established for the charitable purpose for the advancement of religion. Having established that the Church was not a charity, the Commission concluded at page 37 of its decision, that there was no need to discuss whether that Church was established for the public benefit.

Even though it was not strictly necessary, but for the sake of completeness, the Commission however went on to determine whether the Church was established for the public benefit.

We have attached the Commission determination to this submission as an Appendix as we believe it will be relevant to readers of this submission not only in relation to the Church but to a discussion of the public benefit test.

Our point is that a public benefit test may not be needed to revoke an entity's charitable status.

Why does the Test only apply to charitable and other "institutions" but not "charitable funds"?

As currently drafted the Bill applies only to entities covered by Item 1.1 or 1.2 of section 50.5 of the *Income Tax Assessment Act 1997* ("ITAA 97"). These sections apply to charitable, religious and scientific "institutions". Note that Items 1.5 and 1.5B of section 50.5 ITAA97 applies to "funds" established for public charitable purposes by will or by instrument of trust.

The Bill explanatory memorandum however does not provide a rationale as to why "institutions" as distinct from "funds" (such as trusts) should be caught by the Test.

[2] Ibid, paragraph 235.
[3] See Appendix for complete reproduction of this decision.

The common law public benefit test applies to charitable institutions and charitable trusts so we would think that the Test contemplated by the Bill would apply equally. Accordingly, in our opinion, the Test ought also to apply to charitable trusts.

Does the Test replace or supplement the common law public benefit test?

We are not clear whether the Bill drafters intend the Test to replace or supplement the common law public benefit test.

For example under the Bill a new Section 50-51(1) is to be inserted into the ITAA 97 which states:

> The regulations must formulate a test (to be known as the public benefit test) against which the aims and activities of an entity *may* [our italics] be assessed.

One reading of this sub-section is that the aims and activities of an entity could be assessed by the Test but could also be assessed by some other criteria (eg the common law public benefit test). If the drafters of the Bill intend the Test to replace the common law public benefit test we suggest that sub section 1 delete the "*may"* and replace it with "must".

The mischief is that courts may attempt to apply a common law definition of public benefit test in addition to the Test.

Is it intended that the Test "principles" form part of the Test?

In our opinion the Test principles are a welcome move towards codifying best practice by not-for-profit organisations such as can be found in the for-profit sector in the ASX *Corporate Governance Principles and Recommendations.* We are not clear however if the principles form part of the Test.

Section 50-51(2) of the Bill states that the Test must *include* certain key principles. In our opinion it may be clearer for the section to state that the public benefit test must be *based* upon certain key principles ie the Test is not itself a set of principles but rather a set of rules or guidance based on those principles.

In our opinion the principles themselves require no more of a charity than what it would need to do if it is going about its business in a responsible manner. Even a small charity with very limited resources should be able to show that there is an identifiable benefit arising from its operations and that it had considered any adverse consequences of those operations. Accordingly, we think the principles are not controversial.

An exception is the word "significant" at Bill section 50-51(2)(c). We think this word ought to be deleted. Common law decisions simply require a section of the public not to be numerically "negligible". One can think for example, of a charity for persons suffering a rare health disorder, the beneficiaries of which may be numerically insignificant but whom otherwise merit assistance from a charity.

The important distinction to maintain in the Test in our opinion is that between public" and "private" benefit.

Should the Minister formulate the Test?

In our opinion, the Test (ie not the "principles") ought not to be formulated by the Minister.

Instead the Test ought to be formulated (with reference to the principles) by an independent statutory body such as the Registrar for Community and Charitable Organisations contemplated by a recent Productivity Commission Report.[4] If the Bill proponents cannot wait until such time as an independent body is established, we think the Tax Commissioner through his tax ruling system would be sufficiently divorced from political processes to fulfil such a role in the interim.

We think and with respect, that the Minister will unavoidably be influenced by public opinion when drafting the Test, despite scrutiny of for example, the Senate Standing Committee on Regulations and Ordinances. In our opinion the better approach is to specify key principles for the Test in statute, which a decision maker must then take into account when formulating a Test.

Conclusion

In our opinion efforts to create a statutory public benefit test that places the onus on charities to demonstrate public benefit, particularly where such onus is not administratively consuming, will only build public trust and accountability for charities. It is for this reason that we commend the efforts by Senator Xenophon and the Senate inquiry to establish and investigate respectively, a public benefit test in statute.

If you wish to discuss our opinions in further detail, please feel free to contact us.

Yours faithfully
DF MORTIMER & ASSOCIATES

Derek Mortimer
Principal

[4] Productivity Commission Research Report *Contribution of the Not for Profit Sector* January 2010, 148.