YMCA

We build strong PEOPLE strong FAMILIES strong COMMUNITIES

YMCA Australia Submission to the Senate Economics Reference Committee

Inquiry into mechanisms and options for the development of a capital market for social economy organisations

April 2011

YMCA Australia welcomes the opportunity to provide our views to the Senate Economics Committee regarding its current inquiry into financing the not-for-profit sector.

While we will aim to contribute to this inquiry from an organisational point of view, we consider it equally important for us to consider and respond to the shifting contextual issues that will have implications for the not-for-profit sector more broadly. These issues include, but are not limited to:

- the increased prevalence of social enterprises and social businesses as a model of delivering sustainable social outcomes in the not-for-profit sector;
- the growing recognition on the part of Government of the value and importance of social enterprise in addressing significant community issues;
- the expectation of the not-for-profit sector to be able to measure and demonstrate its impact – to Government, donors and the community;
- steps being taken on the part of Government to harmonise the regulatory frameworks governing the not-for-profit sector; and
- the changing nature of philanthropy from grant making to investment in social change.

Our response to this inquiry also follows our recent contribution to the consultation paper *'Scoping study for a national not-for-profit regulator'* and our previous submissions to related inquiries, including:

- our 2009 submission in response to the Productivity Commission Issues Paper: *The Contribution of the Not-For-Profit Sector in Australia;* and
- our response to the 2008 *Inquiry into the Disclosure Regimes for Charities and Not-for-profit Organisations.*

Level 1, 88 Market Street, South Melbourne, 3205
ABN: 45 004 076 297
Telephone (03) 9699 7655 **Facsimile** (03) 96992365
Email: admin@ymca.org.au www.ymca.org.au

YMCA Australia

The profile of the YMCA in Australia is one of diversity – in terms of our programs and services, the communities we serve and our geographic reach. YMCA Australia also has a diversity of relationships with all levels of government and has a broad variety of revenue streams that support our programs.

In Australia, the YMCA:

- is a federated organisation comprising 30 independent Associations;
- employs over 7,500 staff;
- is supported by over 3,000 volunteers;
- works across more than 500 sites in every state and territory;
- derives 2% of revenue through contributions from the philanthropic sector and public donations;
- derives 4% of revenue from government sources; and
- derives the remaining 94% from the provision of programs and services that are operated on a cost-recovery basis.

This enables the YMCA to invest in local community strengthening programs and provides us with a high degree of sustainability, independence and a capacity to remain financially viable while continuing to be mission-focused.

The ability of not-for-profit community organistions to access funding and finances from a range of sources allows for a greater degree of flexibility in terms of program innovation, service planning and strategic development. Greater support from all levels of government, particularly the Federal Government in funding innovation that builds on successful community initiatives will greatly enhance the capacity and diversity of not-for-profit organisations.

Current Issues of Concern

Issues of concern regarding the sustainable financing of the not-for-profit sector are not unknown and are not new; many of these were noted by the 2009 Productivity Commission Issues Paper: *The Contribution of the Not-For-Profit Sector in Australia*.

These concerns include, but are not limited to:

- the cost-shifting of the delivery of community and social services to the not-for-profit sector and the under-financing of government obligations in this regard;
- short-term financing by governments and the timing of funding agreements, particularly in regional areas exacerbating existing difficulties regarding staff recruitment and retention, strategic planning and infrastructure development;
- detailed compliance and acquittal processes that are not commensurate with the activity undertaken by the not-for-profit entity and do not accurately reflect the true outcomes of the activity;
- the lack of collateral that inhibits commercial borrowing by most small not-for-profit entities;
- the lack of government funding available to support existing capital facilities; and
- the difficulty many not-for-profit entities face as they are unable to enter into commercial partnerships to contribute to a capital project because they have ineffective title to the land which is the subject of the project.

A Proposal: Australian Charity Bonds

This proposal has been put forward by financial management personnel within the YMCA in Australia and is a concept that builds on the intent of the social impact bond as a mechanism to increase and sustain capital investment in the not-for-profit sector in Australia.

- Enact changes to Income Tax Legislation to enable the creation of Australian Charity Bonds (ACB) as a bond delivering income tax exempt income returns, issued by eligible charities for the funding of social enterprises. This taxation status can enable market based mechanisms to raise capital for social enterprises, where the charity can convince investors of a sustainable approach and a strong probability of a return of capital at the maturity of the Bond.

- The creation of this market can reduce pressure on government resources to provide large grants to enable development where capital cannot be accessed by the charitable sector or fund social enterprises that would be otherwise restricted in their scale due to a lack of access to capital. The potential loss of taxable income collected from the tax exempt bonds would be offset through a reduced need to directly fund developments or issue specific purpose grants from a federal government level.

- As yields on taxable investments need to be higher in order to match those of ACB's (given a tax exempt status), it provides an opportunity for Charities to be able to raise funds at more sustainable levels of funding costs to enable the achievement of social outcomes.

- Eligibility for charities to issue ACB's would be linked to Tax Concession Charity (TCC) income tax exempt status as currently administered by the Australian Taxation Office (ATO). This is an existing mechanism that certifies the charitable intent of the entity.

- Ensure that ACB's be subject to regulatory requirements that provide strict compliance for the protection of investors, while ensuring that onerous and costly regulatory requirements are minimised for charities seeking to raise capital in the public market.

- The effective administration through established mechanisms within the ATO and ASIC avoids the need to establish any additional government bodies and minimises the required legislative changes to enable the creation of ACB's.

- Creates a market for bonds with a socially responsible outcome. Australian has an underdeveloped bond market in comparison to other developed market economies such as the United States. The lack of choice in the corporate bond market is a regular criticism by investors who want to weight part of their investment portfolios to fixed income.

- ACB's may be attractive to investors who currently support charities via donations and can provide greater effective support through the loan of capital to the charity. Managed Funds or investment trustees with mandates for socially responsible investments or fixed income may also be a potential group of funders for this financial instrument.

- There are examples of tax exempt bonds internationally such as higher education bonds issued by institutions such as Yale or Harvard and municipal, county or state issued bonds in United States. These are well established financial instruments with significant levels of capital raised.

- Charities issuing ACB's can seek rating by rating agencies to assist in market acceptance and promotion of their issue and for larger retails issues can utilise the services of registry companies to administer ACB's rather than creating in-house costs.

- A standard terms and product disclosure statements could be developed to minimise the issue costs associated with establishing ACB's.

- Good financial governance would still be required by charities as while ACB's provide an alternative source of capital, excessive debt levels may endanger the viability of a charity when they experience a decline in cash flow.

- ACB's do not require agreement of complex delivery measurements such as those required to measure social impact bond programmes.

For example : Charity A issues $25M in ACB's for the development of affordable housing in a region with an identified need for more affordable housing stock.

Issue Size	$25M*
Term	7 years
Coupon (Interest)	4%
Effective yield at a 46.5% tax rate[1]	7.47%
Effective yield at a 38.5% tax rate[2]	6.5%

*If investment in this issue size may more likely to be a contribution by a company, rather than an individual this would therefore have a different yield result.

Pricing of the coupon can be structured to be competitive with existing corporate bonds, while providing a cost efficient source of finance to the charity to develop and

[1] 2010-11 Marginal tax rate including Medicare levy for taxable income greater than $180,000
[2] 2010-11 tax rate including Medicare levy for taxable income greater than $80,000 and less than $180,000

sustain the social enterprise. The bonds can be secured against an underlying asset such as the housing stock or a rental stream related to the affordable housing.

Conclusion

When developing alternative mechanisms to provide capital support to the not-for-profit sector a number of key principles including sustainability; equity; accessibility and efficiency will need to be considered. The continued growth and development of the not-for-profit sector will require financial support mechanisms that foster and promote innovation, forward planning and reduce the level of dependence on government as a source of funding. While independence from government is a central tenet of the not-for-profit sector, it is also critical to ensure that the primary responsibility for the delivery of essential services and supports to the community rests with government.

We look forward to the outcomes of this inquiry and if there are any questions or comments in relation to this submission, please do not hesitate to contact us.

Yours Faithfully,

Mr. Peter Malone
Acting CEO
YMCA Australia