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Office of the President

11 October 2024

Our ref: [WD:NFP]

Senate Standing Committees on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

By email: economics.sen@aph.gov.au

Dear Committee Secretary

Not-for-profit Entities – Tax Assessments

Thank you for the opportunity to provide feedback on the Senate Committee inquiry into Not-for-profit Entities – Tax Assessments.

The Queensland Law Society (QLS) is the peak professional body for the State's legal practitioners. We represent and promote over 14,000 legal professionals, increase community understanding of the law, help protect the rights of individuals and advise the community about the many benefits solicitors can provide. QLS also assists the public by advising government on improvements to laws affecting Queenslanders and working to improve their access to the law.

This response has been compiled by the QLS Not for Profit Law Committee, whose members have substantial expertise in this area.

QLS has previously engaged with the Australian Tax Office about these reforms. A copy of our letter of 9 April 2024 is **enclosed** for your reference.

At that time, we highlighted the following key concerns:

- The proposed self-assessment review returns will impose undue compliance costs on not for profit organisations, with a wider impact on Australian civil society and diminishing social capital.
- QLS recommended an alternative policy approach, under which the Australian Charities and Not for profits Commission (ACNC) should, in accordance with the Australian Charities and Not for profits Commission Review, register large non-profit organisations (that are not charities) with a revenue of over \$5 million to access tax concessions.

Since our April 2024 correspondence, QLS has also received the following feedback from a member. We provide the following, on a de-identified basis, as an example of the practical consequences of these reforms giving rise to significant time and financial costs for smaller organisations.

Not-for-profit Entities – Tax Assessments

The member is employed by a not for profit (**NFP**) company that is required to lodge a self-assessment return before the end of October 2024. The process to determine, objectively, that the company qualified for the tax exemption status, was complex. It required a proper understanding of item 8.2(a) of section 50-40 of the *Income Tax Assessment Act 1997* (Cth), tax rulings and case law to evaluate the company's activities over the past financial year to satisfy that it was an eligible entity.

For those NFP entities that provide a mixture of member services as well as broader activities, it requires a detailed examination of the company's activities to judge that the activities were eligible.

Having undertaken this task on behalf of their employer, our member provided the following comments:

1. Small NFP entities, particularly those that also provide member services, will incur considerable expense requiring (often external) expert advice from an accountant or solicitor to make this determination. By way of example, the member completed a review of ATO rulings and case law, the company's activities, reported to the Board, and the Board passed a resolution that the objectives, activities, history and proposed direction of the company fell within the exemption, total time spent exceeded 40 hours. External cost would be in the vicinity of \$24,000.
2. The NFP entity will need to properly detail its activities over the past financial year and as the self-assessment review is an annual requirement, the entity's activities may change each year, so this will be an ongoing expense.

Our member also observed:

"Small NFP entities (revenue less than \$1 million) do not operate to make huge profits. The source of revenue for small NFP entities is from its own members. It is highly unusual, in my experience, that small NFP entities engage in commercial activities to generate profit. Any profit made by the entity is not distributed to members, but utilised to support the NFP entity's objectives. Members will not pay membership fees to a small NFP entity just so the NFP entity can make a huge profit."

QLS supports these observations and highlights again the concerns we raised in April 2024 to the ATO in relation to the disproportionate impact of these reforms on small NFPs.

If you have any queries regarding the contents of this letter, please do not hesitate to contact our Legal Policy team via [REDACTED] or by phone on [REDACTED].

Yours faithfully

[REDACTED]
Rebecca Fogerty
President

Encl (1) QLS letter of 9 April 2024 to Australian Taxation Office

9 April 2024

Our ref: [WD:NFP]

Commissioner of Taxation
Australian Taxation Office

Attention: Victoria Rogers

By email: [REDACTED]

Dear Ms Rogers

Draft instrument – Taxation Laws (Requirement to Lodge a Return for the 2024 Year) Instrument 2024 – not for profit organisations and self-assessment review returns

The Queensland Law Society (QLS) appreciates the opportunity to provide feedback on the draft legislative instrument LI2024/D2 *Taxation Laws (Requirement to Lodge a Return for the 2024 Year) Instrument 2024 (Draft Instrument)*.

QLS is the peak professional body for the State's legal practitioners. We represent and promote over 14,000 legal professionals, increase community understanding of the law, help protect the rights of individuals and advise the community about the many benefits solicitors can provide. QLS also assists the public by advising the government on improvements to laws affecting Queenslanders and working to improve their access to the law.

This response has been compiled by the QLS Not for Profit Law Committee, whose members have substantial expertise in this area.

This submission addresses our concerns with subsection 6(11) of the Draft Instrument.¹

It relates to a self-assessment return being lodged with the Australian Taxation Office (ATO) by certain not for profit organisations that are not charities registered with Australian Charities and Not for profits Commission (ACNC).

It is acknowledged that the ATO has been engaged for some time in the implementation of the self-assessment return, however this submission is concerned with the policy of establishing the self-assessment return, not its implementation.

¹ The legislative instrument is proposed to be made under the *Income Tax Assessment Act 1936* (Cth), *Income Tax Assessment Act 1997* (Cth), *Superannuation Industry (Supervision) Act 1993* (Cth) and *Taxation Administration Act 1953* (Cth).

Draft instrument - Taxation Laws (Requirement to Lodge a Return for the 2024 Year) Instrument 2024 – not for profit organisations and self-assessment review returns

Summary of Issues

1. The proposed regulation is not proportionate to the mischief. It will impose undue compliance costs on not for profit organisations, with a wider impact on Australian civil society and diminishing social capital.
2. A possible interim measure to provide proportionality would be to set an appropriate gross income threshold for filing a not for profit self-review return with a staged implementation across years, to reduce the burden on smaller not for profit organisations. This would be a more proportionate response to the tax risk.
3. Our preference is for an alternative policy approach, under which the ACNC should, in accordance with the Australian Charities and Not for profits Commission Review (**ACNC Review**), register large nonprofit organisations (that are not charities) with a revenue of over \$5 million to access tax concessions.
4. Given that this is the most significant change to reporting obligations for the nonprofit sector in over a decade, we believe the consultation is inadequate. The consultation process does not meet the standard required under section 17(1) *Legislation Act 2003* (Cth) (the **LA**), as persons likely to be affected by the proposed instrument (micro and small not for profit organisations) were not given an adequate opportunity to comment on its proposed content (s 17(2) LA).
5. Conducting consultation over the Easter school holiday period is disappointing and counterproductive. With public holidays, only 19 business days were available to gather comment. Further, in our experience, volunteer office bearers of targeted nonprofits do not convene during school holidays, which impacts their ability to respond.
6. The explanatory statement released with the Draft Instrument does not contain sufficient information about s 6(11) of the Draft Instrument to enable readers to understand the instrument's need, objectives, and intended operation. It should be amended to reflect the requirements of the Office of Parliamentary Counsel Instruments Handbook to include:
 - a. the issues giving rise to the need for the legislative instrument;
 - b. why legislation is necessary to address the issues;
 - c. an explanation of how the instrument is intended to operate, and its likely impact.

Context

As part of the 2021-22 federal budget, the government announced that it had provided \$1.9 million in 2022-23 capital funding for the ATO to build an online system to enhance the transparency of income tax exemptions claimed by exempt not for profit entities.²

² 2021-22 Budget Paper No. 2, 11 May 2021, 22. <https://archive.budget.gov.au/2021-22/index.htm>

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The reasons given were:

“Currently non-charitable NFPs can self-assess their eligibility for income tax exemptions, without an obligation to report to the ATO. From 1 July 2023, the ATO will require income tax exempt NFPs with an active Australian Business Number (ABN) to submit online annual self-review forms with the information they ordinarily use to self-assess their eligibility for the exemption. This measure will ensure that only eligible NFPs are accessing income tax exemptions.”³

The ATO further explained on its website that:

“From 1 July 2023, NFPs with an active Australian business number (ABN) will be required to lodge an annual self-review return in order to access an income tax exemption. In subsequent years, NFPs will confirm or amend information provided to them on a pre-filled self-review return. If a return is not lodged, they may become ineligible for an income tax exemption and penalties may apply under the ATO’s penalty framework.”⁴

This announcement appears to be related to one of the recommendations of the ACNC Review, that large nonprofit organisations (not charities) with a revenue of over \$5 million be required to register with the ACNC to access tax concessions.⁵

In response to the ACNC Review, the Governance Institute considered that extending the current ACNC regime to small not for profit entities, particularly small community-based incorporated associations, might not be workable.⁶ The Australian Institute of Company Directors (AICD) supported an extension to not for profit organisations on a voluntary basis but strongly recommended that further consultation be undertaken on the practical implications of such a model.⁷

Further, the ATO advised the ACNC Review that of the 130,000 income tax-exempt not-for-profits on their records, approximately 580 had estimated revenue (GST turnover) of \$5 million or more.

The ATO also recommended to the ACNC Review that a staged implementation of its proposal, with the highest turnover entities that qualified for the threshold of a large charity (over \$1 million) first, followed later by those with a turnover of \$250,000 to \$1M per annum. It was silent as to the remaining entities below that threshold, but the assumption appears to be that they would not be required to register.⁸

³ 2021-22 Budget Paper No. 2, 11 May 2021, 22. <https://archive.budget.gov.au/2021-22/index.htm>

⁴ <https://www.ato.gov.au/General/New-legislation/In-detail/Other-topics/Not-for-profit/Enhancing-the-Transparency-and-Integrity-of-Not-for-Profits/>

⁵ Strengthening for Purpose: Australian Charities and Not-for-profits Commission Legislation Review - Report and Recommendations, 31 May 2018. <https://treasury.gov.au/publication/p2018-t318031> (ACNC Review).

⁶ Governance Institute Submission p 4. <https://treasury.gov.au/sites/default/files/2019-03/Governance-Institute-310865.pdf>

⁷ AICD, p 5. <https://treasury.gov.au/sites/default/files/2019-03/AICD-310865.pdf>

⁸ ATO Submission to the ACNC Review. https://treasury.gov.au/sites/default/files/2019-12/c2017-t246103_submission_ato.pdf

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The ACNC Review concluded that:

“The Panel has taken the view that revenue size should be the basis upon which not-for-profits should be migrated to the ACNC. Based on information provided by the ATO, the Panel considers the entities to transition first could be the income tax exempt entities under Division 50 of the ITAA 1997, tax deductible entities under Division 30 of the ITAA 1997 and research organisations within section 73A of the ITAA 1936, with revenue of \$5 million or more per annum. As it is estimated that there are approximately 580 such entities, this should not create an unreasonable burden on the ACNC” (emphasis added).

The ACNC Review then made a formal recommendation that:

“24. The ACNC Act be amended to provide that certain not-for-profits with annual revenue of \$5 million or more must be registered under the ACNC Act to be exempt from income tax and access Commonwealth tax concessions.”

The Government’s response to Recommendation 24 was:

“The Government does not support the recommendation. The Government considers that eligibility for income tax exemptions and other tax concessions for non-charitable not-for-profits is best regulated by the ATO. The Government will consider options for tightening the ATO’s existing regulatory framework for not-for-profits and consider any implications for the regulatory scope of the ACNC.”⁹

There was no discernible public debate concerning the government's response to the ACNC Review recommendation for large nonprofit organisation registration with the ACNC in 2018 or its later budget announcement. Neither the government nor the Treasury have offered reasons why the ATO is the more appropriate agency to undertake this transparency measure rather than the ACNC. Further, there has been no public disclosure of indications of an actual manifest threat to the fiscal revenue or publicly identified tax abusive behaviour about exempt NFPs.¹⁰

This consultation is the first time that affected parties have been able to formally respond to the policy of the proposed measure (as opposed to its implementation).¹¹

Size and Gravity of the Proposed Regulation and disproportionate response to the tax risk

The ATO Assistant Commissioner Not for profit, in her [monthly blog](#) (Straight from the Source – June 2023), described the changes as:

From the 2023–24 income year, non-charitable NFPs that self-assess as income tax exempt are required to lodge an annual return with the ATO. This is the most significant

⁹ Government Response to the Australian Charities and Not-For-Profits Commission Legislation Review 2018, 6 March 2020, 18. <https://treasury.gov.au/sites/default/files/2020-03/p2020-61958-govt-response.pdf>

¹⁰ Refer answer 11 to Senate Economics Legislation Committee, Budget Estimates 2022 – 2023, Question No: SBE072, 16 November 2022.

¹¹ [202204] Self-assessed income tax exempt not-for-profits - <https://www.ato.gov.au/about-ato/consultation/in-detail/matters/matters-under-consultation/not-for-profit>

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change to the sector since the introduction of the Australian Charities and Not-for-profits Commission (ACNC) in 2012.

We strongly endorse the sentiments of the Assistant Commissioner.

We also believe that the vast majority of the targeted not for profit organisations are small micro-organisations with no employees and with volunteer committee management.¹² They are an indispensable part of civil society and generators of valuable social capital, but they are fragile in the face of unwarranted increased regulatory burdens.

Given the number of small organisations caught by these reforms, we are of the view that imposing this requirement on all not for profit organisations within the proposed scope is not proportionate given:

- The best estimates are that a large percentage of the within-scope organisations are micro or small;
- Do not represent a risk to taxation revenue or are currently involved in significant tax abusive behaviour; and
- There will be incommensurate compliance costs for micro and small organisations.

We would support a threshold relating to gross income that is proportionate to the tax risk.

We further support that the introduction of self-assessment returns be staged over several years as suggested in the ATO submission to the ACNC Review.

Alternative Policy approach should be considered

We believe that a better policy approach would be to follow the recommendation of the ACNC Review rather than the current proposal, being that:

“The ACNC Act be amended to provide that certain not-for-profits with annual revenue of \$5 million or more must be registered under the ACNC Act to be exempt from income tax and access Commonwealth tax concessions.”¹³

This proposal has the following advantages:

- Being proportionate to the tax risk;
- Fulfils the initial policy vision of the ACNC to be concerned with both charities and not-for-profit entities;
- The ACNC is a bespoke regulator with the skills, experience and knowledge to deal with not-for-profit organisations and often their volunteer governance arrangements with an appropriate touch;

¹² For estimates of the numbers of small organisations refer McGregor-Lowndes, M., (2022). *A Primer on Reform of Tax Exempt Nonprofit Entities*, Australian Centre for Philanthropy and Nonprofit Studies (ACPNS), QUT. Available at <https://eprints.qut.edu.au/232181>

¹³ ACNC Review, 13.

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- Takes advantage of the digital infrastructure and experience of the ACNC in online filings;
- Facilitates the collation and distribution of statistics about significant not-for-profit organisations, which may not be the case with the ATO secrecy provisions preventing full statistical disclosure;
- Allows public transparency of financial and governance records that:
 - o Allows the public to scrutinise and hold to account substantial not-for-profit organisations through a fit-for-purpose digital register not possible with the ATO secrecy provisions;
 - o Encourages regulatory co-option of the public and media to scrutinise public records more effectively and efficiently than the secrecy of the ATO.

Regulatory tool – online form

However, we agree that requiring the filing of ‘an online annual self-review form’ to establish income tax-exempt status is preferable to the higher compliance cost of filing a tax return for not for profit organisations and the ATO's administration cost.

The tool builds on the ATO worksheets for self-determination of the tax status of clubs, societies and associations in operation since July 1994.¹⁴

However, there needs to be a threshold to ensure proportionality to tax risk and compliance costs on micro and small not for profit organisations.

Consultation concerns

We acknowledge that the ATO has conducted targeted consultations since February 2022 led by Ms Moltisanti, ATO Small Business.¹⁵

However, these consultations have not been about the suitability of the policy or alternative policy approaches, but were:

“To understand the impacts that the government announced reform will have on self-assessing income tax exempt not-for-profits (NFPs) and co-design the lodgment process.”¹⁶

Given that the ATO recognises this as the most significant change to the nonprofit sector in over a decade, we believe there has not been appropriate consultation as required by s 17(1) of the LA Act, as persons likely to be affected by the proposed instrument were not given an adequate opportunity to comment on its proposed content (s 17(2) LA Act).

¹⁴ Produced by the Small Business Section, Northbridge. Later editions had the reference Nat 2442-6.

¹⁵ <https://www.ato.gov.au/General/New-legislation/In-detail/Other-topics/Not-for-profit/Enhancing-the-Transparency-and-Integrity-of-Not-for-Profits/>

¹⁶ <https://www.ato.gov.au/about-ato/consultation/in-detail/matters/matters-under-consultation/not-for-profit>

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We acknowledge the notice in the ATO legal database of the consultation¹⁷ but cannot find any notice of the consultation on the ATO 'What's New' Page, despite the news item published on 5 April 2024 providing information about the new return obligations from 1 July 2024.¹⁸

We have been unable to find since 12 March 2024 to 8 April 2024 any mention of the consultation process on the ATO social media accounts on Facebook¹⁹ or X.²⁰ Whilst there have been multiple posts on Ms Moltisanti's LinkedIn page about the upcoming self-assessment changes, there does not appear to be any post about the consultation process itself.²¹

We are also concerned there has been limited discussion of the policy consultation in professional updates and bulletin services. The Wolters Kluwers CCH Tax Alert service has published details of the consultation process, but the equivalent Thomson Reuters Latest Tax News service noting the Draft Instrument did not highlight the not for profit implications of the Draft Instrument.

We agree with the ATO's assessment this is the most significant change to the not for profit sector in over a decade. For this reason, we consider there was inadequate time for a consultation from 12 March to 9 April as it included the Easter period of three business-day holidays, school and university breaks, and amounted to only 19 business days.

Further, in our experience, volunteer office bearers of targeted nonprofits do not meet during school holidays, which will impact their ability to respond to the consultation.

Our observations are that many professional advisors, let alone micro and small not for profit organisation have not become aware of the consultation.

Sufficiency of the Explanatory Statement

The explanatory statement does not contain sufficient information about s 6(11) of the Draft Instrument to enable readers to understand the instrument's need, objectives, and intended operation as required by sections 17(2) and 15J (2)(b) of the LA.

The only substantive mention of the self-review return is:

"That is, the same classes of persons that have been required to lodge a return in previous income years are also required to lodge a return this year, although there is also a new requirement for certain entities to lodge a NFP self-review return."²²

¹⁷ [https://www.ato.gov.au/law/view/view.htm?docid="ops%2Fli2024D2%2F00001](https://www.ato.gov.au/law/view/view.htm?docid=)

¹⁸ <https://www.ato.gov.au/whats-new#sortCriteria=%40dateupdated%20descending>

¹⁹ <https://www.facebook.com/atogovau/>

²⁰ https://twitter.com/ato_gov_au

²¹ https://www.linkedin.com/search/results/all/?fetchDeterministicClustersOnly=true&heroEntityKey=urn%3Ali%3Afsd_profile%3AACoAAAYWGscB2W9dsI0HoJWQ4EtTjuOtgI_1m6U&keywords=jennifer%20moltisanti&origin=RICH_QUERY_SUGGESTION&position=0&searchId=7bfe31e0-7da1-480a-a547-5e231b3170ee&sid=167&spellCorrectionEnabled=false

²² Paragraph 17, ATO Legislative Instrument 20241A102 Taxation Laws (Requirement to Lodge a Return for the 2024 Year) Instrument 2024

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We note that the Office of Parliamentary Counsel Instruments Handbook states:

“The explanatory statement should contain sufficient information to enable readers to understand the need for the instrument, its objectives and its intended operation. As a guide, it is desirable for the statement to include the following information:

- a) the issues giving rise to the need for the legislative instrument;
- b) why legislation is necessary to address the issues;
- c) an explanation of how the instrument is intended to operate, and its likely impact.”²³

The LA does not require consultation if the rule maker considers it inappropriate or impractical.

Further, the Office of Parliamentary Counsel Instruments Handbook mentions that the rule-maker may consider it inappropriate or impractical to “implement a decision announced in the Budget” despite these words about Budget announcements not appearing in the LA.

This ought not to be the end of the matter as the Office of Parliamentary Counsel Instruments Handbook qualifies this by noting that:

Even if an instrument falls into one of these examples, a case by case assessment is still important and necessary to satisfy the requirements of section 17 of the LA and of scrutiny bodies.²⁴

We would strongly argue that full consultation with an explanation is required as:

- The ATO recognises the measure as the most significant change to the nonprofit sector in over a decade, and we agree;
- The Budget announcement was an outcome that was neither considered by the ACNC Review nor any of its submissions;
- The government has not provided any rationale or explanation for its policy proposal; and
- The public and affected stakeholders were not given the opportunity to be heard on the proposal until this consultation.

We recommend that the explanatory statement be expanded to “contain sufficient information to enable readers to understand the instrument's need, objectives, and intended operation”, as outlined in the Office of Parliamentary Counsel Instruments Handbook.

Conclusion

We regret that the consultation on the design of the proposed regulation has been left to a matter of weeks before its intended implementation.

²³ <https://www.opc.gov.au/drafting-resources/legislative-handbooks> Page 63, paragraph 259.

²⁴ Page 59 at paragraph 242.

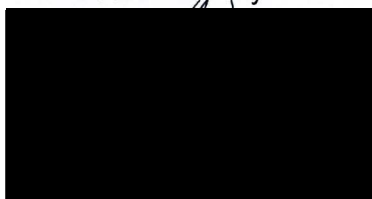
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We strongly recommend that a proportionate response be made to self-assessment returns to avoid imposing undue compliance costs on micro and small not-for-profit organisations, which would impact Australian civil society and diminish social capital.

This can be simply achieved by inserting a reasonable threshold into the provision.

If you have any queries regarding the contents of this letter, please do not hesitate to contact our Legal Policy team via [REDACTED] or by phone on [REDACTED]

Yours faithfully



Rebecca Fogerty
President