

Senate Economics Legislation Committee
ANSWERS TO QUESTIONS ON NOTICE
TREASURY
Australian Taxation Office
(Additional Estimates 17 February 2005)

Outcome 1

Topic: Meaning of ‘primary purpose’ for DGR

Hansard Page E70-71

Senator Mason asked:

Getting back to the question that the chair raised before—we always come back to this ‘primary purpose’, and what is ancillary or incidental—does ‘primary purpose’ mean, for example, that, if a body receives \$1 million and they give \$501,000 for the purposes of educating the community about the environment and they give \$499,000 to the Greens, they satisfy that test?

Mr Konza—The actual test is that the activities that are not charitable are incidental or ancillary, so the percentage that you are posing there would be much more skewed. For something to be incidental it might, in the case that you have given us this afternoon, be raising awareness about the environment. There might be incidental mention of thinking carefully about voting or something. Ancillary, I would have thought, denoted a relatively small percentage.

Senator MASON—Could you give me a ballpark figure, Mr Konza?

Mr Konza—No, I am not that brave. These are common-law definitions, and I would need to do a bit of research.

Senator MASON—How much of the money that goes to the Wilderness Society is ancillary—10 per cent, 20 per cent, 30 per cent, 40 per cent?

Mr Konza—I would not want to be drawn on that. I would be speculating. I would need to go and find out what the law says.

Answer:

Charities and other non-profit organisations do a range of things, and these activities can vary from time to time. However, the test of whether an organisation is charitable is, in Australia, a purpose test.

Following the terminology used in *The Commissioners for Special Purposes of the Income Tax v. Pemsel* [1891] AC 531; [1891-4] All ER Rep 28, there are ‘four heads of charity’:

- the relief of poverty;
- the advancement of education;
- the advancement of religion; and

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- other purposes beneficial to the community.

The actual activities of the organisation are theoretically only part of the evidence considered in reaching a conclusion about what the purpose of the organisation is. Many charities engage in a range of activities. Where those activities are carried on within an organisation, provided they are merely incidental or ancillary to a charitable purpose, then the organisation as a whole is still considered to be charitable, and will be wholly exempt from income tax.

This is a question of fact and degree and depends on the circumstances of the particular case:

- in *Royal Australasian College of Surgeons v. FC of T* (1943) 68 CLR 436 (where the issue was whether the College was a scientific institution) the court held that any promoting of the professional interests of members (which would be a non-scientific activity) was incidental to the purpose of advancing science.
- in *Australian Council of Social Service Incorporated v. Commissioner of Pay-Roll Tax (NSW)* 16 ATR 394, the Court of Appeal (NSW) made no consideration of the organisation's written objects, and turned only to a consideration of activities in determining that ACOSS was not a public benevolent institution (PBI).
- in *Maughan v. FC of T* (1942) 66 CLR 388, the High Court looked at the broad objects of the Boys' Brigade (providing for 'the development as good citizens of the boys ...; to cultivate Christian manliness; to promote habits of reverence, loyalty, industry, discipline and self-respect ...' and for 'the delivery and holding of lectures, entertainments, games, sports, tournaments, meetings, classes, debates and conferences ...') but it also considered other factors - the Brigade's branches were located in the worst slum areas of Sydney and the boys who enrolled were underprivileged and invariably in poor circumstances. It concluded that organisation's activities were clearly targeted at the relief of the needy, and that it was a public benevolent institution.

As noted above, an institution is charitable if its purpose is charitable. A charitable institution's purposes are wholly, solely and exclusively charitable. To the extent that any of a charitable institution's objects, activities and other features would (when viewed in isolation) be non-charitable, they must be no more than incidental or ancillary to the charitable purpose.

An issue of importance is what evidence may properly be considered in reaching a conclusion about purpose.

The purpose of a charitable institution is determined having regard to its constitution, any legislation governing its operation, its activities (see above), history and control.

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The determination of purpose involves an objective weighing of all relevant features. No one factor, in isolation, can be taken as an indicator of an organisation's purpose.

The Tax Office view about how purpose is determined is set out in Draft Taxation Ruling TR 2005/D6. It relevantly says of charitable institutions:

149. However, if an institution exists or operates for any purpose that is not a charitable purpose, it will not be a charitable institution. This is the case even if its non-charitable purpose is secondary or minor. For example, an association set up for two separate purposes – to look after injured animals for the benefit of the public, and to be a stamp-collecting club for its members – would not be a charitable institution even if it mainly cared for animals, with lesser attention given to the stamp-collecting.

150. Because a charitable institution is only for a purpose that is charitable, all of its activities will be solely and entirely to carry out or give effect to its charitable purpose. Of course, many of a charitable institution's activities and powers might, when viewed in isolation, be indistinguishable from those of a non-charity. Examples might be hiring staff, cleaning premises, insuring property, buying and selling assets, preparing and maintaining accounts, complying with regulatory requirements, conducting meetings, and so on. For a charitable institution, though, all of these things would be done only for the sake of, or in aid of, or in furtherance of, its charitable purpose. Accordingly, an institution's activities, powers and objects which, when viewed in isolation, would not be charitable, must be incidental or ancillary to the charitable purpose:

Such a body is a charity even if some of its incidental and ancillary objects, considered independently, are non-charitable.

As well as incidental and ancillary, other expressions used in the cases are 'subsidiary' and 'concomitant'. They all express the idea that the objects or activities are not the organisation's ends in themselves. They are only for the sake of, or in aid of, or in furtherance of, its charitable purposes.

151. Finding an institution's purpose involves an objective weighing of all its features. These include its constitutive or governing documents (memorandum and articles of association, trust deed, constitution, and so on), its activities, policies and plans, administration, finances, history and control, and any legislation governing its operation.

152. The features of an institution's constituent documents will be the starting point, and in normal situations will have the most weight (see paragraph 154). However, the constituent documents are not considered in isolation. 'And in order to ascertain what the purposes of an association are, the court is not limited to consideration of its rules or its constituent documents', as Lord Normand said in *Inland Revenue Commissioners v. City of Glasgow Police Athletic Association* [1953] 1 All ER 747 at 752.

153. The other features of an institution will usually have more or less weight depending on aspects of those documents, their relations to them, and other circumstances (see paragraph 162).

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Even though the actual activities of the organisation are theoretically only part of the evidence considered in reaching a conclusion about what the purpose of the organisation is, and despite what is said in para 154, the reality is that courts usually turn to a consideration of an entity's activities where the entity's character and purpose is at issue. Also relevant is *Australian Council of Social Service Incorporated v. Commissioner of Pay-Roll Tax (NSW)* 16 ATR 394, where the Court of Appeal gave no consideration to written objects, and only considered its activities in determining that ACOSS was not a public benevolent institution (PBI).

The Tax Office's consideration of activities is directed only to the determination of whether in fact an entity has a charitable purpose: not with the intention of second-guessing the entity about what is the most effective way to further its charitable purpose.

It is possible that an entity with a governing document containing clearly expressed charitable objects could be found not to be in fact a charitable institution if most or all of its activities do not further the stated charitable purpose (in this context the effect of what is achieved becomes in essence relevant).

The concepts of 'ancillary' and 'incidental' have a long history in this area of the law.

The courts have not developed prescriptive rules for deciding whether particular purposes are ancillary or incidental to charitable purposes. It is an objective weighing of all the relevant facts of each individual case that leads to determination of the matter.

Consequently, the Tax Office does not seek to apply prescriptive rules for deciding whether particular purposes are incidental or ancillary to a main or dominant charitable purpose(s). It is a matter of weighing up all relevant features to assess whether certain purposes are ancillary or incidental.

The presence or scale of particular activities, such as advocacy, is not in itself an indication or confirmation that those activities are a purpose in their own right. While an organisation might engage in advocacy, that activity may be the means by which the main or fundamental charitable purpose(s) of the organisation is or are achieved. For example, an overseas aid organisation may seek to conduct a fund raising drive for starving children overseas, and as a part of that activity, raise public awareness by distributing leaflets or writing letters to the newspaper.

An institution or fund is not charitable if its purpose or one of its purposes is advocating for a political party or cause, attempting to change the law or government policy, or propagating or promoting a particular point of view. However, if the purpose of an institution or fund is charitable, the presence of political or lobbying programs and activities will not detract from this status, provided that they are incidental to the charitable purpose.

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Paragraphs 100-124 of Draft Taxation Ruling TR 2005/D6 deal with this issue in detail. However it is clear that an organisation clearly carried on for charitable purposes can participate in many ways in engagement with government, in presenting its views to the public, and in the democratic process.

The law requires a gift deductible organisation to maintain a gift fund, and that the gift fund must be maintained for the principal purpose of the fund, authority or institution.

The Tax Office position is that the principal purpose of a fund, authority or institution includes purposes that are incidental or ancillary to that principal purpose. However, where a gift fund is maintained only for an incidental or ancillary purpose of a fund, authority or institution, it does not satisfy the gift fund requirement. Nor does a gift fund operated for various purposes, only one of which is the principal purpose of the fund, authority or institution. (Taxation Ruling TR2000/12 refers)

Further particular conditions may be imposed by law. Environmental organisations and harm prevention charities are required to 'have a policy of not acting as a mere conduit for the donation of money or property to other organisations, bodies or persons'.

The Tax Office position about a gift fund acting as a conduit is also set out in Taxation Ruling TR2000/12. It says:

While gift funds may usually act only as a conduit to their fund, authority or institution, for passing on and accounting for gifts, this need not be their only function. Other disbursements could include paying for purchases of property or services for use by the fund, authority or institution, purchases of property to be made available for use by the fund, authority or institution, and meeting obligations of the fund, authority or institution. A gift fund might finance fund raising.

In limited cases involving statutory extension to the law, a test of activity has been imposed, in lieu of a test of purpose.

Specific examples are:

- child care - subsection 4(1) of the *Extension of Charitable Purposes Act 2004* provides that '[w]ithout limiting what constitutes a charitable purpose, *charitable purpose* includes the provision of child care services on a non-profit basis';
- harm prevention charities - section 30-289 of the *Income Tax Assessment Act 1997* provides the test that '[t]he principal activity of the institution must be the promotion of the prevention or the control of behaviour that is harmful or abusive to human beings'; and

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- health promotion charities - item 1. 1.6 in the table in subsection 30-20(1) of the *Income Tax Assessment Act 1997* provides the test that the organisation must be 'a charitable institution whose principal activity is to promote the prevention or the control of diseases in human beings'.

Additionally, where the law has been extended by the specific listing of an organisation, there is no requirement in the law for the organisation to meet any purpose or other tests although at an administrative level, such organisations are expected to maintain a gift fund for receipt of gifts to the organisation.