

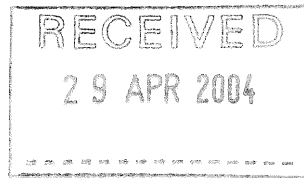


## Australian Government

### The Treasury

28 April, 2004

Dr Sarah Bachelard  
Committee Secretary  
Economics Committee  
Australian Senate  
Parliament House  
CANBERRA 2600



Dear Dr Bachelard

#### **TAX LAWS AMENDMENT (2004 MEASURES NO.1) BILL 2004 - LEGAL ADVICE**

I refer to the Committee's hearing of 1 April 2004, in relation to the Tax Laws Amendment (2004 Measures No.1) Bill 2004.

At the hearing, I agreed to seek legal advice on issues raised in a submission to the Senate Committee by Mr John Wardle, Special Counsel at Corrs Chambers Westgarth. Mr Wardle's submission relates to Schedule 10 of the Bill, which requires charities to be endorsed by the Commissioner of Taxation to be entitled to various tax concessions. Mr Wardle's submission raises issues about the treatment of entities that are both charities and religious institutions. In particular, Mr Wardle notes his concern that, while the revenue laws have distinguished between religious institutions and charitable institutions, a religious institution may nevertheless only be entitled to claim concessions if it is endorsed as a charity. He considers that this requires clarification. I have attached the advice of the Australian Government Solicitor (AGS) on this matter for consideration by the Committee.

The AGS advice confirms that it is an existing requirement of the *Income Tax Assessment Act 1997* (the ITAA 1997) that entities that are both charities and religious organisations must be endorsed by the Commissioner of Taxation in order to access an income tax exemption.

Endorsement is not currently required to access fringe benefits tax or GST concessions, and so there are not provisions in the corresponding fringe benefits tax or GST legislation pertaining to organisations that are both charities and religious organisations. The AGS advises that the effect of schedule 10 of the Bill is to extend the current treatment that applies for the income tax exemption to fringe benefits tax and GST concessions. In all cases, the AGS advises an entity that is both a charity and a religious organisation will be required to be endorsed to access the various tax concessions.

The AGS makes particular note of section 63-5(2) of the *A New Tax System (Goods and Services Tax) Act 1999*, which relates to the ability of an entity to register their separately identifiable branches as separate entities for GST purposes. In relation to this section, the advice concludes that all charities that are also religious organisations will be required to be endorsed in order to utilise the provision.

Currently, there are two ways that a charity may qualify under this provision. The first way is by qualifying under paragraph (a) of this subsection as a charitable institution, or a trustee of a charitable fund. The provisions in Schedule 10 of the Bill require that, to access the provision under this paragraph, an organisation that is both a charity and a religious organisation must be endorsed. The second way is by qualifying under paragraph (b) as an exempt entity under section 50-5 of the ITAA 1997. Charities that are also religious organisations have always been required to be endorsed to qualify under paragraph (b), as endorsement is a requirement for charities to be exempt under section 50-5 of the ITAA 1997.

The application of Schedule 10 would therefore mean that organisations that are both a charity and a religious organisation would be required to be endorsed to access the concession under either paragraph (a) or (b) under section 63-5(2). This is consistent with the intention of the schedule to require charities to be endorsed for all concessions even where they could otherwise access the provision as another type of entity.

Yours sincerely



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Dear Ms Ransley

**Tax Laws Amendment (2004 Measures No.1) Bill 2004 - taxation status of religions institutions**

1. Thank you for your request for advice of 7 April 2004 regarding certain amendments to be made by the Tax Laws Amendment (2004 Measures No. 1) Bill 2004 (the Bill).

**BACKGROUND**

2. The Senate Economics Legislation Committee is currently conducting an inquiry into various aspects of the Bill. In particular, Schedule 10 of the Bill contains amendments to a range of Acts and would require all charities, public benevolent institutions and health promotion charities to be endorsed by the Commissioner of Taxation before being entitled to receive certain taxation benefits.
3. Corrs Chambers Westgarth has made a submission to the Committee on the Bill concerning the impact of proposed amendments on religious institutions. Corrs queries whether the amendments to be made by Schedule 10 are really intended to apply to religious institutions as distinct from other types of charities. The Committee has requested that Treasury obtain legal advice on these matters.
4. We note that the question of whether it was or is the Government's policy intention to treat religious institutions differently to other types of charities is not a legal question. This advice will therefore examine the existing taxation exemptions provided to religious institutions and charitable institutions and consider the effect of the amendments proposed by Schedule 10.

**SUMMARY OF ADVICE**

5. In our view, the effect of the Bill is that a religious institution that is also charitable institution will be required to be endorsed by the Commissioner in the same manner as any other charitable institution to be entitled to any of the various tax benefits. In our view, this is already the case for income tax exemption.

**Discussion**

- 6. At present, there are a variety of taxation concessions available to religious institutions and charitable institutions. The amendments contained in Schedule 10 to the Bill deal only with the concessions available to charitable institutions. As noted in the Corrs submission, religious institutions will generally also be charitable institutions as the advancement of religion is one of the four heads of charity at common law. Generally, there is a presumption that the element of public benefit exists where the purpose falls under the first 3 heads of charity (relief of poverty, advancement of education and advancement of religion).
- 7. However, there may be circumstances in which a religious institution is not a charitable institution. In *Gilmour v. Coats* [19650 CH 85, the House of Lords held that the purposes of a community of cloistered and contemplative nuns were not legally charitable. We note that it has been suggested by one commentator that the reasoning in this case is unlikely to be considered favourably by modern Australian courts.<sup>1</sup>
- 8. We will examine in turn the availability of each tax benefit for religious institutions and charitable institutions and consider the effect of the Bill on this availability.

**Income Tax**

- 9. Section 50-1 of the *Income Tax Assessment Act 1997* (the ITA) provides:
 

The total ordinary income and statutory income of the entities covered by the following tables is exempt from income tax. In some cases, the exemption is subject to special conditions.
- 10. Section 50-5 of the ITA list a variety of charitable entities including:

**Charity, education, science and religion**

Item	Exempt entity	Special conditions
1.1	charitable institution	see sections 50-50 and 50-52
1.2	religious institution	see section 50-50

<sup>1</sup> Dal Pont, *Charity Law In Australia and New Zealand*, 2000, OUP, p.171.

1.3	scientific institution	see section 50-55
1.4	public educational institution	see section 50-55

11. The separate inclusion of 'religious institutions' as opposed to 'charitable institutions' is somewhat ambiguous. Applying the maxim of interpretation 'generalia specialibus non derogant', it would be possible to argue that the express reference to religious institutions implies that the meaning of 'charitable institutions' should not include religious institutions and therefore that the requirement of endorsement does not apply. However, in our view, this interpretation is not to be preferred.

12. Section 50-52 of the ITA provides:

- (1) An entity covered by item 1.1, 1.5, 1.5A or 1.5B is not exempt from income tax unless the entity is endorsed as exempt from income tax under Subdivision 50-B.

Note: The entity will not be exempt from income tax unless it also meets other conditions: see section 50-50 (for an entity covered by item 1.1), 50-57 (for an entity covered by item 1.5) or section 50-60 (for an entity covered by item 1.5A or 1.5B).

- (2) However, an entity that is a charitable institution prescribed for the purposes of paragraph 50-50(c) or (d) may be exempt from income tax even if the entity is not endorsed as exempt from income tax under Subdivision 50-B (as long as the entity meets the other requirements of this Division).

- (3) This section has effect despite all the other sections of this Subdivision.

Note: This means that an entity covered both by an item other than 1.1, 1.5, 1.5A or 1.5B and by one of those items is not exempt from income tax unless the entity is endorsed under Subdivision 50-B as exempt from income tax (or is prescribed for the purposes of paragraph 50-50(c) or (d)) and the entity meets the requirements of whichever of sections 50-50, 50-57 and 50-60 is relevant.

13. In our view, section 50-52 has the effect that where a religious institution is also a charitable institution, it must be endorsed as exempt from income tax under Subdivision 50-B to be exempt from income tax. This is clear from subsection 50-52(3) and the note thereto (section 15 AB of the *Acts Interpretation Act 1901* provides that regard may be had to extrinsic material to assist in ascertaining the meaning of a provision). In other words, the classes of entities in section 50-5 are not mutually exclusive and subsection 50-52(1) therefore extends the conditions imposed by section 50-52 to entities falling within item 1.2 (religious institutions) where they are also 'covered' by item 1.1 (charitable institutions).

14. For religious institutions to be exempt from income tax regardless of whether or not they are also charitable institutions would require an amendment to the ITA. We

note that Corrs submissions suggests that all religious institutions should be exempt. This is not a legal issue.

15. The amendments to the ITA contained in Schedule 10 of the Bill will not alter this outcome. Religious institutions that are also charitable institutions must still be endorsed to be exempt from income tax.

#### ***Fringe Benefits Tax***

16. Section 65J of the Fringe Benefits Tax Assessment Act 1986 (the FBT Act) sets out the employers who are entitled to a rebate of fringe benefits tax and this includes 'religious institutions' (paragraph 65J(1)(a)). Charitable institutions are also included (paragraph 65J(1)(b)).
17. Unlike the ITA, there is presently no requirement for endorsement of charitable institutions to be eligible for the FBT rebate and there is no endorsement required for religious institutions.
18. The amendments to the FBT Act contained in Schedule 10 will require religious institutions that are also charitable institutions to be endorsed in order to be eligible for the FBT rebate (see item 22 - proposed new subsection 65J(1A)). The explanation of the effect of these amendments in paragraph 10.13 of the Explanatory Memorandum to the Bill confirms this interpretation. Therefore, under the amendments to be made by Schedule 10, entitlement to the FBT rebate in relation to religious institutions that are also charitable institutions will operate in the same way as for income tax exemption.

#### ***Goods and Services Tax***

19. The *A New Tax System (Goods and Services Tax) Act 1999* (GST Act) gives charitable institutions certain exemptions from particular aspects of the GST arrangements. For example, charitable institutions may chose to account on a cash basis regardless of their annual turnover (see section 29-40). With one exception, there is no separate exemption in the GST Act provided to religious institutions (as distinct from charitable institutions). Of course, there are specific provisions relating to the supply of services by religious institutions (see for example, section 38-220) but these provisions have no relevance to charitable institutions per se. Therefore, a religious institution (that exceeds the annual turnover threshold) is only entitled to account on a cash basis if it is a charitable institution. Similarly, a religious institution is only able to treat a supply of second-hand goods as GST-free if it is a charitable institution (see section 38-225).
20. The amendments to the GST Act will require that charitable institutions be endorsed in order to have access to these various exemptions. Religious institutions that are charitable institutions must therefore be endorsed to continue to have access and will be treated in the same manner as other charitable institutions (as is currently the case).

21. The one exception under the existing law is in relation to the ability of an entity to register their separately identifiable branches as separate entities for GST purposes (enabling the parent not to be responsible, for GST purposes, for those branches). Subsection 63-5(1) of the GST Act provides that an entity may choose to apply the Division. Subsection 63-5(2) sets which entities may so choose and provides:
- (2) However, the entity must be registered and must be:
    - (a) a charitable institution, a trustee of a charitable fund, a gift-deductible entity or a government school; or
    - (b) a non-profit body that is exempt from income tax under any of these provisions of the ITAA 1997:
      - (i) section 50-5 (charity, education, science and religion);
      - (ii) section 50-10 (community service);
      - (iii) section 50-15 (employees and employers);
      - (iv) section 50-40 (primary and secondary resources, and tourism);
      - (v) item 9.1 or 9.2 of section 50-45 (sports, culture and recreation).
22. Item 12 of Schedule 10 to the Bill will amend subsection 63-5 to provide that paragraph 2(a) does not apply to a charitable institution unless that institution is an endorsed charitable institution. A religious institution (that is not a charitable institution) is entitled to choose to apply Division 63 under subparagraph 63-5(2)(b)(i). However, at present, where a religious institution is also a charitable institution, in our view, the exemption under subparagraph 63-5(2)(b)(i) is not available unless the institution is endorsed. This is because the effect of section 50-52 of the ITA (discussed above) is that religious institutions that are charitable institutions are not exempt from income tax unless endorsed. If the amendments are passed, religious institutions that are charitable institutions will also not be able to rely on paragraph 63-5(2)(a) unless they are endorsed. In other words, if the amendments are passed, in all cases, religious institutions that are charitable institutions must be endorsed in order to choose to apply Division 63.
23. I am happy to discuss any aspect of this advice or to provide further advice if that would be of assistance.

Regards



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