

**IMPROVING THE INTEGRITY OF PRESCRIBED PRIVATE FUNDS
THE TREASURY – DISCUSSION PAPER, NOVEMBER 2008**

SUBMISSION BY BUSH HERITAGE AUSTRALIA – January 2009

Bush Heritage Australia, as a Deductible Gift Recipient organisation, submits this response to the Treasury's Paper from the perspective of a not-for-profit organisation that receives significant benefit from Prescribed Private Funds (PPFs). This support for Bush Heritage's vital conservation work in Australia is provided not only from financial gifts distributed by PPFs, but also through the increased engagement of individuals involved with these PPFs. For a number of these individuals the opportunity to strategically plan for long-term funding support of conservation projects has also resulted in increased engagement of the individuals and their families in our organisation's work. Many individuals have provided the additional benefits of their professional advice and hands-on assistance, and increasingly these supporters are encouraging their peers to become involved with our cause.

Bush Heritage views the Government's establishment of the PPF structure as a considerable success in encouraging philanthropy amongst Australia's growing pool of high net worth individuals, with a resulting increase in funding now available for community purposes, such as the preservation of Australia's threatened ecosystems and species. Whilst we applaud the decision to legislate guidelines to improve the integrity of PPFs, and to provide trustees of PPFs with greater certainty as to their obligations, we would hope that the Government is cautious in introducing any changes that may discourage individuals to support this form of structured giving.

Australia still has a considerable way to go in encouraging philanthropy amongst the wealthy and there needs to be a long-term plan to encourage this. As noted in the paper 'Good Times and Philanthropy; Giving by Australia's Affluent'¹ –whilst the mean household income for Australia's affluent population has increased by 36% over the ten year to 2005, 'charitable contributions, as measured by the percentage of taxable income claimed as charitable giving increased from just over 0.36% to just over 0.45%, still well under 1% for the vast majority of wealthier Australians'. Considerable effort is still warranted to encourage engagement of Australia's affluent in establishing a culture of philanthropic giving. From our own experience in encouraging support from wealthy individuals, we support the following recommendations from the afore mentioned paper, including the need to 'increase visibility of philanthropy amongst the affluent' (open peer to peer discussion is integral to this), 'offer more guidelines for giving, promote affluent giving norms and build the practice of 'planned' versus spontaneous giving', 'train and support professional advisers about providing philanthropic advice' and finally to 'improve awareness amongst Australia's affluent population of the benefits of involving their children in giving'. Integral to this is the importance of public awareness campaigns to encourage philanthropy with a particular emphasis on long-term goals and timelines in encouraging change in philanthropic activity².

PPF have been one very effective means of increasing giving from Australia's wealthy in the last eight years. As at July 2008, over 769 PPFs have been established with current estimated value of all PPFs at over \$1.5 billion now irrevocably committed for charitable purposes. Support for this philanthropic structure has also continued to gain momentum in this time, with \$471.7 million donated to PPFs in 2006/07, an increase of 73.8% on the previous year, and \$117 million distributed to charities in the year ending June 2007³.

¹ 'Good times and Philanthropy; Giving by Australia's Affluent'¹ – March 2008 by Dr Kym Madden and Dr Wendy Scaife of the CPNS

² Promoting Philanthropy: Global Challenges and Approaches; Paula D. Johnson, Stephen P. Johnson and Andrew Kingman, International Network on Strategic Philanthropy, December 2004

³ Prescribed Private Funds, CPNS Current Issues Sheet 2008/6, The Australian Centre for Philanthropy and Nonprofit Studies, Queensland University of Technology

PPFs provide a structure that effectively addresses a number of the recommendations for promoting philanthropy amongst the wealthy, including:

- promoting structured giving, and long-term engagement in philanthropy, rather than one-off gifting;
- providing a simple structure that has encouraged advisors to raise philanthropy with clients;
- promoting family involvement in philanthropy, and a means to encourage a philanthropic culture during a time of expected increased intergenerational transfer of wealth;
- allowing individuals to retain a level of control over their philanthropic giving, that also promotes increased engagement with causes and the organisations they choose to support; and
- providing increased promotion of philanthropy, both publicly, with an increased number of PPFs publicly promoting their support whilst allowing anonymity for individuals; and privately, with increased peer-to-peer discussion of structured philanthropic giving.

In improving the integrity of PPFs we agree with the need to legislate guidelines and improve accountability, and in particular support the changes proposed to 1) bring administration of PPFs under the authority of the Commissioner of Taxation, 2) amend the current 'all or nothing' penalty system, and 3) reduce the current complexity that exists around accumulation plans, target sizes and methods of calculating distribution levels. We are also supportive of changes that assist trustees and advisors in understanding guidelines and obligations, and in promoting the dissemination of such information.

However, we are wary of a number of proposed changes that may be detrimental to the continuation or continued establishment of PPFs amongst Australia's affluent.

In order to recognise those proposed changes in the guidelines that may negatively impact on the growth of this form of structured giving, it is important to consider some of key elements in the current structure of PPFs that encourage their establishment.

As recognised in 'Tools for Good: A guide to Vehicles for Philanthropy and Charitable Giving'⁴ private and family foundations are often a preferred vehicle for giving for many reasons, including providing a 'valued structure to philanthropy – a framework through which to pursue immediate and long-term philanthropic goals – while at the same time preserving personal control over and unequalled flexibility in charitable gifts'; and is a vehicle that 'can be used to strengthen family ties and connections...the principal reason for creating a foundation has to do with intersecting considerations of mission, perpetuity, control and family bonds.'

Two key aspects that are identified above and are regularly cited as motivators in establishing PPFs are their ability to allow donors to effectively plan for long-term support of causes and, directly related to this long-term aspect of their structure, allowing donors to encourage further generations to engage in philanthropic planning. 'Private foundations offer a means through which to pursue a philanthropic mission in perpetuity, if that is what the donor seeks. Many foundations are established with the expectation that their endowment will be permanent, and that its charitable mission will – with sound investment management – guide grantmaking into a virtually unlimited future. In a word, foundations are a vehicle that lends itself to significant long-term philanthropic impact.'⁵

In direct response to these identified motives, we would therefore caution imposing a minimum distribution rate that affects the ability of many PPFs to continue to operate in the long-term.

⁴ Tools for Good: A Guide to Vehicles for Philanthropy and Charitable Giving; Paula D. Johnson, Stephen P. Johnson, International Network on Strategic Philanthropy, November 2004

⁵ Tools for Good, et al.

Consultation questions:

1a - What is an appropriate minimum distribution rate? Why?

Whilst it was noted that a distribution rate of 15% has been the historical average to date we certainly caution using this figure as an appropriate level at which to set future giving as is average will have been considerably influenced by three factors: the past decade of considerable capital gains; the distribution of 10% of new donations as part of existing accumulation plans; and the number of PPFs that distribute 100% of their capital each year, particularly corporate workplace giving PPFs.

For many current PPFs that have been in the establishment phase or that are fully funded, a 15% minimum distribution rate could effectively run down the capital within 10-15 years. Whilst a boon to charities in the short term, this would not lead to long-term growth and increase in support.

Key to the question of whether a PPF should be allowed or indeed encouraged to exist in perpetuity, is the effect this would have on the motivation to encourage extended family and multi-generational support for philanthropy. In a number of cases PPFs have been established following a significant 'windfall' event, such as the sale of a business. In such cases whilst there is a considerable tax advantage in establishing a PPF there is also considerable long-term benefit for the community in choosing to establish a long-term giving structure, and encouraging family to engage in this as a means to establishing a philanthropic culture amongst the next generations. In such cases there may be limited capacity for family members to continue to contribute significant capital to the PPF in the following decade/s, however engaging family members in its establishment and running allows philanthropy to become integral to family financial planning in the long-term.

We do not agree that the guiding principle for distributions should be that "tax revenue foregone should be directed to the charitable sector in a relatively short period of time" (discussion paper p.5). Most DGRs have at least some of their mission directed to solving difficult problems which require long-term programs. The large majority of tax incentives for philanthropy result in immediate gifts, where the DGR receives the gift in full when the donor gives it. It would be good public policy to allow for some philanthropic giving structures which allow and encourage donors to make irrevocable commitments, which will be disbursed only gradually to DGRs. Bush Heritage Australia deals with nature conservation outcomes which are sometimes emerge slowly (dictated by ecological processes), and almost always require continuing resource commitments to continue to abate threatening processes.

We therefore think that a *minimum* required distribution should allow for a PPF to maintain a corpus at its nominal (original intended) value for 20 or 30 years – while also maintaining the public interest via adequate distributions to DGRs. Obviously, over 20 to 30 years the real (inflation adjusted) value of the corpus is substantially less. However we do not think the public interest requires forcing PPFs to be "run down to zero" over this period.

This would suggest a minimum distribution in the next year of 5% of net asset value⁶, or all income and *realized* capital gains (net of the PPFs own expenses), *whichever is greater*. This approach would result in some years where the net value of a PPF would reduce (e.g. if its net asset value growth was negative or less than 5%), and some where the net value a PPF would be stable or increasing (e.g. if it had unrealized net capital gains). Overall, the PPFs would generally be obliged to give more in "good years". Some of the motivations of trustees and founders to allow for capital growth and longer-term philanthropy would continue to be met (by allowing them to decide whether to realize capital gains or not), however in the long term distributions would tend to increase

⁶ This rate is similar to the rate used in the USA, and greater than in other countries, such as Germany, where 'payout is based on annual revenue earned from endowment investments. Most countries require no specific distribution'. Tools for Good: A Guide to Vehicles for Philanthropy and Charitable Giving; Paula D. Johnson, Stephen P. Johnson, International Network on Strategic Philanthropy, November 2004

(income would tend to increase with increased capital value, and all income must be distributed).

We hope that some PPF founders will succeed in including their next generation family members as donors to the PPF, and/or add to the PPF in the future by bequests by the founder/s. If so, founders or their families can anticipate and plan for increased giving beyond 20 or 30 years. This preserves the public interest in a philanthropic structure which can last and grow in real (inflation adjusted) value beyond one generation of a family, if they so choose by adding more of their own capital.

Importantly, providing further clarity around the guidelines for PPFs, in conjunction with a set distribution rate which allows funds to operate over a long period of time, may lead to an increase in the establishment of PPFs now, providing further benefits for charities in the long-term.

1c - Is setting a minimum PPF size appropriate? What should the minimum PPF size be in dollar terms?

For those PPFs with a corpus at or near \$500,000, consideration should be given to intentions to provide additional capital over time to grow this corpus, and guidelines should be put in place that allow consideration for market volatility. Were a newly established or growing PPF to fall below this minimum time for a short period due to investment performance and were subsequently required to be wound up, regardless of long-term plans for growth, this would again be detrimental to the long-term potential for charitable benefit from this PPF.

1d – Are there any relevant issues that need to be considered in improving and standardizing the public accountability of PPFs? Are there any concerns with the proposal to require that the contact details of PPFs be provided to the public? What information should be provided publicly?

Given the considerable tax advantages that those contributing to PPFs receive from the Government, there is certainly need to ensure that PPFs are accountable and transparent in their administration, and we therefore agree with the need for increased regulatory powers to be provided to the ATO in order to ensure this occurs.

However, in response to the question of providing contact details to the public, and the noted benefit of making it easier for charities seeking funding to make representations to PPFs, the mere public listing of PPFs with provision of contact details would by itself lead many charities to waste resources in applying to PPFs that do not fund their areas. This would further lead to an increase in resources required by PPFs to manage this increase in unsolicited applications. Of greater benefit would be a central publically accessible register of PPFs that provides information of the areas of interest that they fund, whether they are willing to consider unsolicited applications and appropriate contact details for such submissions.

We would not support any proposal that would lead to individual contributors to be named or their contact details to be made publicly available. 'Many wealthy individuals give generously but do so anonymously. There are excellent reasons for such anonymity, reasons that range from cultural and religious norms to individual safety and security. But where appropriate donors should be encouraged to give more publicly. Such openness affirms the value of social investing, demonstrates the impact of giving and attracts the attention of other potential donors and the media.'⁷

Whilst we acknowledge the need for increased promotion of philanthropy amongst Australia's affluent, we do not believe that this is most effectively achieved by being forcefully imposed. We recognize that many of our own donors wish to remain anonymous, and we respect their decision. We believe that encouraging philanthropy to be central to their financial decision making does increase an individual's willingness to

⁷ Promoting Philanthropy: Global Challenges and Approaches; Paula D. Johnson, Stephen P. Johnson and Andrew Kingman, International Network on Strategic Philanthropy, December 2004

discuss this with their peers. In many cases, the strategic structure of a PPF provides an increased opportunity for high net worth individuals to discuss philanthropy more openly with their peers in an open dialogue that is on some level removed from discussing their own personal contributions and wealth. We believe that continuing to encourage the establishment of structured philanthropy through PPFs, and promoting this through direct education of the advisors and to the greater public will have considerably more advantage to contributions to charitable organisations, than increasing the ease of contact details.

Conclusion

As highlighted by the report 'How the wealthy give: comparison between Australia and comparable countries (USA, Britain and Canada)'⁸ charitable giving by Australia's affluent still falls a long way behind that of other comparable countries but has considerable potential for growth. Reporting that 'Australians with a taxable income of more than \$AUS1 million contribute less than 2% of their income, compared to Canadian millionaires who on average contribute 3.2% of their pretax income and US millionaires who on average give more than 3.55 (>7% for those with incomes in excess of \$US10m)' this report also highlights the trend for Australia in the growth in number of wealthy individuals, and the value of that wealth; the scale of the intergenerational transfer of wealth that is to occur over the impending decades; and the tendency for these individuals to seek professional support in managing their wealth, including distribution, are all factors that lead to positive potential for a subsequent increase in philanthropic giving in Australia.

Philanthropy needs to be actively encouraged in Australia, not just among the wealthy. Whilst Australia has experienced a considerable period of increasing affluence in recent times, there will always be periods of economic slowdown, such as we are currently experiencing. It is particularly important at such times that we continue to encourage philanthropic support for community needs. During such periods, guaranteed sources of income for charities, such as those provided by PPFs, will be increasingly important in continuing to meet community needs. Further to this, effective philanthropy requires a long term approach to major issues facing the community. As one organisation that is faced with a long-term mission to protect Australia's unique species, we see PPFs as a significant means to provide support for long-term projects, and to encourage the growth of philanthropic giving in Australia.

PPFs are still a relatively new giving structure in Australia with knowledge of, and popularity, still growing amongst the affluent and their advisors. It would be disappointing to introduce changes to the PPF structure now that hampers their continued growth.

⁸ 'How the wealthy give: comparison between Australia and comparable countries (USA, Britain and Canada)' Prepared by Denis Tracey and Christopher Baker, Asia-Pacific Centre for Philanthropy and Social Investment, October 2004