

27 May 2009

The Manager
Philanthropy and Exemptions Unit
Personal and Retirement Income Division
The Treasury
Langton Crescent
PARKES ACT 2600

Submission

Exposure Draft - Improving the Integrity of Prescribed Private Funds ("PPFs") - Concerns about joint and several penalty liability

Dear Sir/Madam

We are providing comments in response to the Exposure Draft dealing with PPFs released on 14 May 2009.

1. Introduction

PPFs (for the purpose of this submission, the name PPFs will be used rather than private ancillary fund) were introduced into Australia's tax legislation in 2000, as a response to the report on philanthropy in Australia by the Business and Community Partnerships Working Group on Taxation Reform.

PPFs are a form of ancillary trust fund designed to encourage private philanthropy by providing private groups, such as businesses, families and individuals, with greater flexibility to start their own trust funds for philanthropic purposes. PPFs are limited to making distributions to other deductible gift recipients. Various tax concessions are available with respect to the PPFs themselves and contributors to those funds.

Since 2000, there are now currently approximately 800 PPFs in existence, with total contributions of approx \$1.2 billion.

In the 2008 Budget, the Government announced its commitment to improve the integrity of PPFs. In November 2008, Treasury released a Discussion paper on PPFs, titled "Improving the Integrity of Prescribed Private Funds". Treasury received over 100 submissions by the end of January 2009.

On 14 May 2009, Treasury released Draft Legislation to give effect to its commitment to improve the integrity of prescribed private funds and in this regard we provide the following comments.

2. Executive Summary - Concerns about joint and several liability

Amongst the proposed amendments released in the Draft Legislation on 14 May 2009, the Draft Legislation currently provides the following:

Subdivision 426-120(1) of the *Tax Administration Act 1953*

“the trustee of a private ancillary fund, and the directors of the trustee, are jointly and severally liable to an administrative penalty if the trustee or any of the directors falsely holds the fund out as being endorsed, entitled to be endorsed, or entitled to remain endorsed, as a deductible gift recipient.”

The purpose of this submission is to strongly object to the proposed inclusion of joint and several liability for trustees and the directors of the trustees of PPFs, other than in cases where the director is knowingly and dishonestly involved in the offence.

- ▶ Imposing joint and several liability on trustees, and directors of the trustees, will grossly discourage people from volunteering to be a director of the trustee of a PPF; and
- ▶ is a heavy handed method of addressing breaches of the PPF guidelines

3. Discussion

We acknowledge that there are no doubt instances where the tax concessions afforded to PPFs are abused. We rarely if ever see such instances but they of course arise; but probably no more so than the abuse of tax concessions that apply across all forms of business including those available to individuals and corporates.

However, trying to stamp out such abuse cannot be a justifiable reason for seriously damaging the need for, and encouragement that should be afforded, to PPFs across the donor community.

Accordingly, our reasons for objecting to the proposed legislation are specific and are outlined below.

3.1 Discourages people to be on the board of the corporate trustee of a PPF

The experience of PPFs to date has shown that due to a limited amount of administrative resources the people acting as trustees (or who are directors on the board of a trustee) may fall within two categories. First, those who potentially are not really qualified to operate or advise PPFs and those who are experienced and qualified and who volunteer their services on a not for pay basis. In this regard, imposing joint and several liability on directors (and other individuals who participate in the management or control) of PPFs would effectively discourage both sets of people from acting in these roles, not just the former.

It is most important to recognise that PPFs, unlike many forms of corporate or public enterprises, do not have plentiful, or often even adequate, resources to administer the fund. In fact, many donations that are given to not for profits are often given with the express intention that they not be directed to administrative costs but must find their way to the ultimate beneficiaries. This invariably makes it very difficult for not for profits to devote sufficient and adequate resources to administrative matters. As a result, these organisations are much more prone to administrative oversights – not only because of the lack of staff but also because of the quality of the staff that they can often attract compared to the better paid private and government sectors.

Secondly, many of these organisations are successful only because of the calibre of good intentioned people that sit on their board on a not for pay basis. These people are typically successful people in business or the community and provide networks and commonsense commercial guidance on a range of issues. They often become hands on involved in assisting the organisation in a way that they would not normally do for other private or public sector boards they sit on which are better resourced. These people are critical to the success of PPFs and not for profits generally.

It should therefore be obvious to see that any heavy handed penalty regime which runs the risk of personally penalising such individuals as a result of administrative oversights will lead to such individuals refusing to take such board positions. This will be disastrous for the not for profit and PPF sector.

3.2 Imposing joint and several liability is a heavy handed method of addressing breaches of the PPF guidelines

In our view there are more refined and much more responsible ways of dealing with any abuse of the tax concessions afforded to PPFs - which we continue to emphasise is likely to be in a minority of cases - than a heavy handed approach that runs the risk of destroying the sector completely.

One only has to look to the rather well considered penalty regime that applies under the US Not for Profit sector to see how this can be done. In such a regime individuals, be they at management level or at the board level, are typically not personally liable for any penalties unless they have been willingly or dishonestly involved in the abuse - or alternatively knowingly refuse to amend the circumstances under which such an abuse exists.

The regime also has specific rules that deal with people who benefit from the abuse of such concessions and we naturally would support any regime that applied a heavy handed approach in cases where the people involved knowingly and intentionally benefited from an abuse of a concession. However, we strongly oppose any heavy handed approach that could be applied to bona fide well intentioned individuals who participate in these organisations, where there is no intended benefit to them or their associates of any failure to meet a technical requirement.

4. Conclusion

As outlined above, imposing joint and several liability on trustees and directors is an unreasonable method of addressing abuses to the PPF guidelines. Such methods will discourage involvement in PPFs to the point of providing an impossible governance framework. As a consequence this will threaten the existence of PPFs and impact adversely on the future of the not for profit sector generally.

It should only be in very narrow circumstances involving dishonesty, or direct or indirect intended benefaction that should be exposed to such penalties.

It should also not be forgotten that the law (outside of the tax laws) already provides sanctions for directors who act dishonestly.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Alf Capito'.

Alf Capito
Partner