IMPROVING THE INTEGRITY OF PRESCRIBED PRIVATE FUNDS

DISCUSSION PAPER

SUBMISSION FROM

THE MYER FOUNDATION

and

SIDNEY MYER FUND

IMPROVING THE INTEGRITY OF PRESCRIBED PRIVATE FUNDS

INTRODUCTION

The Sidney Myer Fund (SMF) was formed in 1934 on the death of Sidney Myer, one of Australia's most prominent, well known and generous philanthropists. He established the Fund through donating 10% of his wealth, in perpetuity, for the charitable needs of the "…community in which I made my fortune".[1] The Fund commenced with an endowment of £150,000, approximately $10million in today's terms. In 2009, the Fund will celebrate 75 years of giving.

In 1959, Sidney's two sons Baillieu and the late Kenneth Myer established The Myer Foundation (TMF). Through their financial contributions and those of their two sisters and successive generations of Myer family members, the Foundation has accumulated a corpus, the investment from which is used to make grants. In 2009, the Foundation will celebrate 50 years of giving.

In the 2007/2008 financial year across both the Fund and the Foundation, grants to the community were made in excess of $11million.

Additionally, in recognition of 125 combined years of giving in 2009, the Fund and Foundation will give away an additional $26million over five years. This will be supplemented by a further $8million to be given directly by family members.

Myer Family Philanthropy is one of the finest examples in Australia of the power of private giving, committed to in perpetuity, and involving successive generations of active family members. The family remains involved as Trustees of the Fund, Directors of the Foundation, convenors of Committees, and representatives in project groups and task forces.

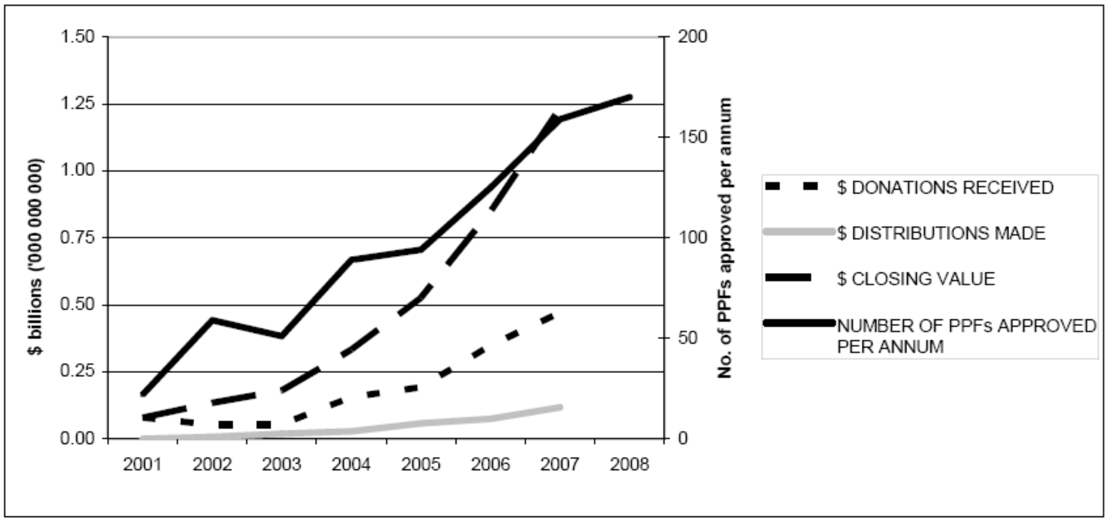
PHILANTHROPY IN AUSTRALIA

It is well known that Australia does not have the rich culture of giving as experienced in the USA and Europe: it is estimated that wealthy Australians donate 3% of their net worth, compared to up to 15% given by wealthy Americans.[2] However wealth from families is the highest single source of funds to the fifteen largest Australian foundations that provided an annual report to Philanthropy Australia in 2007. In this group, ten foundations are based in family traditions of philanthropy.[3]

[1] Will of Sidney Myer
[2] Reported in "*Aussies not Pulling Weight in Charity Stakes*", 11 March 2008, referring to research undertaken by the Australian Centre for Philanthropy and Nonprofit Studies, Queensland University of Technology, accessed at www.news.com.au/story/0,23599,23355087-31037,00.html
[3] Philanthropy Australia, Fact Sheet - *Australian Foundations*, 4 September 2007, accessed at www.philanthropy.org.au

It is also well known that Australian philanthropy has grown significantly in recent years, mainly due to a new environment that supports the establishment of Prescribed Private Funds (PPFs). See Figure 1 below:[4]

Figure 1: Approved PPF Donations Received, Distributions Made and Closing Value by Year



However increased giving in Australia is measured by more than increased donations of money. It reflects the greater engagement of the Australian community in the life, problems and issues of the community. This surely makes for a better community: one where people are concerned and involved, and where more individuals pursue justice and equity.

Civic involvement in the pursuit of a better world is a valued achievement in any society. Philanthropy allows and encourages this, beyond restrictions imposed by election cycles and public shareholders. Many people in the philanthropic and not-for-profit sectors applaud, and are involved in supporting the Commonwealth Government's new commitment to "…build civic engagement and civil society."[5]

RESPONSES TO THE DISCUSSION PAPER

- **PPFs in Context: paragraphs 5-8**

There can be no doubt that the creation of PPF's has deepened philanthropic giving in Australia. This is a positive change, as philanthropy is a significant player in society, alongside government, academia, business and the not-for-profit sector. In partnership with these players, philanthropy plays a unique role in supporting democracy, justice and engagement in civil society.

- **Areas for improvement: paragraphs 9 – 12**

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[4] Australian Centre for Philanthropy and Nonprofit Studies, Queensland University of Technology, *"Prescribed Private Funds"*, Current Issues Sheet 2008/6, accessed at http://cpns.bus.qut.edu.au

[5] Senator the Hon Ursula Stephens, 2008, "*Rudd Government's Social Inclusion Agenda*", presentation given to Australian Council for International Development Forum, Parliament House, Canberra, accessed at http://mediacentre.dewr.gov.au/mediacentre/Stephens/Releases?RuddGovernmentsSocialInclusionAgenda.

While the current regulations address some elements for the establishment and operation of PPFs, it is clear that there is room for improvement. Improvements can be made by legislating the PPF Guidelines, bringing the administration of PPFs under the control of the ATO, giving the ATO greater regulatory powers, and setting minimum compulsory distribution levels.

- **Principles underpinning the rules governing PPFs: paragraphs 16 - 20**

The four principles as listed are good bases for establishing legislated guidelines. However, the first principle falls short by only stating that attention must be paid to the features of the **distributions** (my emphasis) such that they be of "…a quantity and regularity…".

A principle that has been omitted but which in our view is fundamental is that "PPFs can be a permanent entity, and not mandated in such a way that defines their existence only for a certain period of time".

There may be confusion in the Discussion Paper in the language used about PPFs not being "…prolonged accumulators of funds…" (pg 4). The proposal to do away with an accumulation plan is supported. However, PPFs at the same time should be able to be "…prolonged accumulators of funds…" because they should be able to be set up in perpetuity, and contributions made if possible and desirable. PPFs should be seen as long-term entities that can attract and accumulate funds over their lifetime.

To increase the size of compulsory distributions to 15% of the previous year's closing value of the fund will not ensure a sustainable fund. If the principle of perpetuity is accepted, and it is strongly recommended that it is, then this regulation will have extremely negative long-term consequences. This is one of the most concerning proposals in the Discussion Paper.

While analysis of available data leads the ATO to estimate that 15% will be the long-term proportion of PPFs value, analysis of the current state of the global financial crisis alone demonstrates that this high figure is not sustainable. In these circumstances, it would be a short time before many PPFs would be dissolved.

There may well be times when PPFs do not continue to receive donations, for a number of reasons. However these times should not be correlated with the fund no longer continuing to have purpose, merit or intent to continue. There is a hidden assumption in these principles that in order to survive, PPFs must attract at least 15% of the previous year's corpus in donations, year after year, and that if this doesn't happen, the fund no longer continues to be "philanthropic". We argue that there may be many reasons why a fund does not receive ongoing contributions: a family's reduced means and resources, and the current economic climate being good examples of this.

We do not support the Commissioner for Taxation having the capacity to change the minimum distributions depending on market conditions, but do support a minimum distribution of 5% of past year's net assets.

There is merit in allowing newly established PPFs to have a lower distribution rate in their first years. This would not constitute an accumulation plan, but would be a net asset target below which it is financially inefficient to make distributions.

- **Regular valuation of assets at market rates: paragraph 21**

The yearly evaluation of assets would enable PPFs to take account of all realised and unrealised assets, thus maximising capacity to make distributions. It is foreseeable though that due to unexpected economic circumstances, this valuation may place the assets at a level too low to make efficient distributions. We suggest that there be some capacity built into the guidelines to allow for a temporary cessation of distributions, based on exceptional circumstances.

- **Increased public accountability: paragraph 23**

One of the attractive features of PPFs is that they are private. This does not mean that they are unaccountable. Caution should be exercised in dealing with the terms "transparency" and "accountability", and care taken not to join them mistakenly. "Transparency" is best applied to how a PPF meets the regulatory requirements as set by legislation, not whether the details about a PPF's funds under management, funding preferences and contact details are available to the public. It would be too easy to claim that foundations are not transparent, implying not accountable, when what is being argued is that contact and operating details are not known to the public and should be made so.

The current requirements for reporting, and therefore of accountability, are not insubstantial. PPFs have to provide an annual statement of financial performance, an annual statement of financial position, an imputation credit refund return, and an ATO information return which includes details of any changes to trustee arrangements, details of donations, gifts and grants received, and details of distributions to DGR's of amounts greater than $1,000.[6] These should remain, and we believe that as they exist, they provide for high levels of accountability.

In order to be accountable, PPFs should continue to report annually, as is currently required. However, accountability is not enhanced by releasing public details of PPFs, including contact details. This will make management of PPFs more time consuming, and operating costs will increase as staff or PPF trustees will need to attend to an increase in enquiries and applications for funds that have nothing to do with the PPF's objectives. It will also lead to wastage of resources in not-for-profit organisations as they submit applications for which there is no hope of success.

Enhanced accountability is well addressed by other proposals in the Discussion Paper, namely to regulate the guidelines, streamline management of PPFs in the ATO, increase the flexibility of responses by the ATO in relation to non-compliance, and in pursuing ways to enhance the skills and capacities of trustees.

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[6] Myer Family Office, 2004, *"Prescribed Private Funds: Accounting and Audit Issues"*, presentation made by Graham Reeve, Managing Director

- **Greater regulatory powers: paragraphs 25 - 35**

The current reporting requirements, including the auditing of financial statements by registered persons, should continue. Increasing remedial responses by the ATO, including enabling action to be taken against trustees, is supported.

The establishment of transitional rules, and a transitional period, would be beneficial in deepening understanding about how new regulations need to be applied and in ensuring compliance. This will reduce the compliance costs of the ATO, as well as allow time to iron out unforeseen complications.

- **Introduction of a fit and proper person test for trustees**

A test for a fit and proper person is not supported. While the intent of this proposal is acknowledged as a good one, this mechanism would work against many of the things that are valuable in PPFs. Many family PPFs bring in younger family members to learn, under guidance and mentoring, how to manage a philanthropic entity. They learn, in situ, about good decision making, governance, research, and ethical practice. Younger people, or perhaps older family members who have not attained formal qualifications, would be barred from participating under a system that formalised essential criteria. The Myer Foundation and Sidney Myer Fund, while not PPFs, are nevertheless good examples of this, as younger members of the family are highly involved in the philanthropic process, and in their turn are educated and inspired to establish their own PPFs.

We suggest that there is capacity for trustee education and training to be taken up by trustee, financial and philanthropy advisors, as well as the peak body for philanthropy, Philanthropy Australia.

- **Limit the number of PPF donors**

We agree that PPFs are about private philanthropy and argue that the requirement relating to restricting the number of donors must specify a difference between public and private donors.

Again, drawing on the experience of Myer Family Philanthropy, and in particular The Myer Foundation, one of the strengths of this entity has been the capacity to draw in family members across the generations. If PPFs are to continue in perpetuity, then it is foreseeable that a limit on the number of family or private donors would restrict opportunities for growth of family philanthropy and could eventually lead to the cessation of the PPF. Limiting long-term intergenerational philanthropy will do more than restrict the growth of philanthropy – it also runs the risk of disengaging young people from involvement in their community.

CONCLUSION

A review of the regulations in relation to PPFs is timely. On the whole, the proposals reflect a wish to retain the private nature of PPFs and to make their functioning more accountable and efficient. The two most concerning suggestions are that the minimum contribution be set at 15% of the previous year's net assets, and that the contact details of PPFs be made public.

We suggest that these two proposals in particular would have the most significant consequence of undermining the existence of viable private philanthropy in Australia and therefore the objectives of the original PPF legislation.

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2 January 2009

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