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LexisNexis Butterworths

When enough is more than enough!

Chris Wallis *VICTORIAN BAR (GREENS LIST)*

The Australian Government wants a broad conversation about the current tax system and the issues confronting it.

Chapter 7 of the *Re:think Tax Discussion Paper*[1] (discussion paper) articulates the view that governments provide a number of tax concessions, including fringe benefits tax (FBT) concessions, to support the not-for-profit (NFP) sector with the aim of helping increase the level of activity in the NFP sector.

Similarly, some years ago the government of the day boosted economic activity with the pink batts insulation scheme. In hindsight it was a poorly administered scheme riddled with flaws which facilitated rorting and resulted in considerable waste.

When hospital workers started collecting tax invoices from other dinner guests who had paid for their own meals at a restaurant table, it was time middle Australia started to take notice.

When, during a post dinner speech at the 2015 Australasian Tax Teachers Association Conference, a former president of the Tax Institute outlined common salary sacrifice exploitation techniques in the the NFP sector, there was silence at some tables and laughter at others. But immediately the speech ended the conversations started — many of the tax teachers are employed in the broader NFP sector. Why not us?

The exploitative fringe benefit practices:

- are centred on salary sacrifice arrangements;
- are promoted extensively and regularly to employees of NFP entities by the commercial salary packaging operators;
- reflect only one of many revenue concessions extended to entities operating in the NFP sector; and
- provide the greatest advantage to the highest income earners.

What is the NFP sector

The discussion paper cites both the Australian Charities and Not-for-Profits Commission as at 1 December 2014[2] and Australian Bureau of Statistics (ABS) figures to justify the following observations:

- there are around 600,000 NFPs in Australia;
- of these NFPs, around 60,000 are registered charities;
- almost 57,000 NFPs (1 per each 400 head of population) operating in both market and non-market sectors are economically significant;
- NFPs that are economically significant employ 1.1 million people in three principal areas — social services, education and research;
- 38% of the revenue of the economically significant NFPs is sourced from direct government funding (including tied funding); and
- in 2012–13, economically significant NFPs accounted for around 3.8% of GDP (up from 3.2% of GDP in 2006–07).

The public view of NFPs

There is a degree of public dissatisfaction with the overall performance of the NFP sector.

High on the list of things that the public dislikes is the ongoing refusal of NFPs to disclose in a standard and comprehensible manner what proportion of their budget "hits the road" as opposed to being chewed up in administration or on perks for administrators.

The public dissatisfaction is directly traceable to the arbitrary reallocation by some NFPs (generally charities) of public donations to the many tsunami appeals following the 2004 Boxing Day Tsunami in particular:

- the tardiness of NFPs to spend the money donated on the purpose for which it was donated; and
- the unconvincing explanations given by the CEOs for the reallocation of donations.

More recently the public has been unwilling to readily accept the purchase by some NFPs of expensive pieces of art without appropriate due diligence.

A significant proportion of the public has concluded already that the administration of NFPs chews through too much of their revenue — flash offices in prime locations, the best of facilities and generous salary packages and expensive "company cars", while not universal, are too common.

Extended range of revenue concessions

The federal government provides a range of revenue concessions beyond the FBT concessions:

The cost of the FBT concession alone (for public benevolent institutions (PBIs)) is growing rapidly and is estimated that it will shortly cost the federal government around $1.6 billion annually but it is only one of the revenue concessions that is available. The other tax concessions are:

- tax exempt income;
- higher GST registration threshold;
- a limited ability to make supplies GST-free; and
- the ability to receive tax deductible gifts.

The cost of the deductible gift recipient revenue concession is increasing at a slower rate but it is estimated that it will shortly cost the Federal Government $1.2 billion annually.

At the state and local government level, many NFPs qualify for land tax concessions, payroll tax concessions, stamp duty concessions, motor vehicle registration fee concessions and municipal rate concessions. The concessions may lead to a 100% reduction.

Perhaps the most outrageous statement in Ch 7 is the following:[3]

> However, the actual revenue forgone from NFP concessions [provided by the Australian Government] cannot be quantified because many organisations are not required to submit tax returns. This means that the actual revenue forgone is likely to be higher than is currently reported.

The NFP sector is an industry

The NFP sector is an industry, members of which compete aggressively against listed and private entities that operate without the benefit of revenue concessions.

The NFP sector provides tax structuring opportunities that are exploited by tax advisors to minimise tax.

The NFP sector has protected itself from attack by finding reasons not to adopt any uniform reporting standards.

None of the Federal Government, the various state governments or local authorities have any role in deciding which NFPs can or should exist but they each have an obligation to decide:

- the aggregate value of revenue concessions to be extended to the NFP sector; and
- how those concessions are to be accessed and by which NFPs.

All things being equal the public might expect to see the revenue concessions reflected in prices where similar goods are provided — they are not. Whether it be hospital beds, spectacles or breakfast cereals, NFPs do not offer discernibly lower prices.

There is emerging evidence of membership being used in ways that infringe competition laws — health insurers effectively engaging in third line forcing, in relation to the supply of many items, to secure bigger benefits than those payable to members who shop outside specified suppliers.

In short the public supports an industry but the Australian Government is unable to tell us how much that support costs.

The threshold requirements for a broad conversation

It is time for a broad conversation about not only fringe benefit exploitation in the NFP sector but, more fundamentally, about the desirability of any revenue concessions in the NFP sector.

Before there can be a broad discussion about revenue concessions for NFPs, some threshold issues must be addressed:

- First, a shift of language is required — there is a presumption that NFPs are entitled to revenue concessions.
- Second, we need to know the total value of revenue concessions provided to NFPs by the Federal Government, the state governments and the municipalities.
- Third, the government must recognise that most of the lobbying about taxation in Australia is undertaken by NFPs that are unlikely to argue for measures that will adversely impact their own budgets.
- Fourth, politicians have always been willing to spend public money to secure votes.

That the desired broad discussion may proceed without the real cost of revenue concessions being known tends to suggest that the discussion in relation to NFPs will be nothing more than window dressing.

Shift in language

Question 49 of the discussion paper reflects an attitude, presumably of Treasury, that NFPs have an entitlement to revenue concessions: “What, if any, administrative arrangements could be simplified that would result in similar outcomes, but with reduced compliance costs?”

NFPs have no underlying right to revenue concessions. But NFPs have an acutely developed sense of entitlement and they are adept at articulating their entitlement to politicians.

What is the total value of revenue concessions

Each of the Federal Government, the various state governments and local authorities has an obligation to the public:

- to consider and regularly review how much can be directed to supporting NFPs;
- to identify those NFPs that qualify for those revenue concessions; and

- to provide revenue concessions only to NFPs that are totally transparent in all aspects of their work and in their reporting.

Given the discussion paper disclosure that 38% of the funding of economically significant NFPs is provided by the Federal Budget, there is no compelling argument against implementing a requirement for standardised and transparent reporting.

Treasury's central role

Federal Treasury has a central role in the issue of revenue concessions but this role must involve collaboration with the various state treasuries and likely harmonisation of legislative provisions between all jurisdictions.

An army of NFP entities are active and persuasive participants in the tax debate on a daily basis and enjoy enviable access to, and relations with, Treasury.

Federal Treasury must not allow professional bodies and industry groups to "sell" or "promote" self-serving solutions. Treasury must be willing to seek disinterested advice from further afield.

Buying voters

Politicians can no longer chase votes by providing revenue concessions for NFPs or even promises of initial funding for NFPs.

Conclusion

The current "tax arrangements" for the NFP sector are not appropriate.

No one can identify the total cost to the public of the revenue concessions provided to NFPs by federal and state governments and local authorities.

Reporting transparency reflecting consistency and objectivity must be a fundamental requirement for any NFP seeking revenue concessions.

A single regime ought to provide revenue concessions to NFPs and a single regime ought to establish what is and is not an NFP and how those entities are required to report:

- the most practical single regime to mandate standards for the NFP is the Federal Government; and
- the most practical single regime to provide any revenue concessions is a state government within that jurisdiction.

The cold hearted logic and analysis that resulted in the abolition (albeit too slowly) of subsidies to the car industry ought to be applied to the growth of revenue concessions provided to the NFP sector.

The current system cannot be fixed by making changes at the edge but only by identifying the total value of revenue concessions that it is appropriate to provide and then by identifying which entities ought to "share the pie".

It likely that some NFPs would collapse if support was withdrawn but if their work is worthwhile collapses would facilitate consolidation while reducing the number of administrators.

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Footnotes

1. Department of the Treasury (Australia) *Re:think Tax Discussion Paper* (March 2015).
2. See Australian Charities and Not-for-Profits Commission website at http://acnc.gov.au.
3. Above n 1, p 125.