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*Our Ref:* *NEH:ah* *X:\Internal\H&A\Trusts\20101214 re Public Ancillary Funds - Integrity.doc*

16 December 2010

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

Dear Sir/Madam

**Re: Public Ancillary Funds - Integrity**

You are seeking responses to your discussion paper "Improving the Integrity of Public Ancillary Funds". As an accountant specialising in the Not-for-Profit Sector and with substantial knowledge and experience in respect to tax compliance matters in that Sector, I have a significant interest in providing a response.

Ancillary Funds serve a very wide range of purposes. It is no simple matter to give an absolute response to some of the questions posed in the discussion paper, as the response will be different for different applications. Having advised and assisted in the establishment of a significant number of ancillary funds over time, I am aware that in by far the majority of cases, they are used as a management tool for larger charities, that have within their structure more than one Deductible Gift Recipient (DGR) Fund. In a much more limited group, they are used as a structure for providing a capital fund for a substantial charity. In those cases special approval for capitalising donations is required from ATO, – and ATO have established clear guidelines in handling these matters. Another group again, are linked to overseas aid entities and assist in the fund-raising and management of overseas aid projects. They all serve a different purpose to Private Ancillary funds. I wish to record my disagreement with seeking to apply Private Ancillary Funds criteria to the Public Ancillary Funds. The whole control mechanisms and purposes are sufficiently different to establish grounds for an alternative, more flexible procedure.

I now turn my attention to the consultation questions themselves: -

1. Where the Ancillary Fund is established as a management tool for a large charity, the procedure and common practice is that all DGR revenue is to be distributed within a short time frame. There will be some instances where, for budgetary purposes, the distribution of the revenue is staggered, but would still indicate a distribution within twelve to eighteen months. If, on the other hand, it is a fund-raising foundation to

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establish a capital base and appropriate Government approval is given, then the expectation would be that the DGR gift would be invested and the income from the investment would be distributed. This provision is a valuable facility, which must not be lost.

2. With the exception of the capital-raising foundation, most or all ancillary funds would distribute their DGR gifts regularly. As such there is little likelihood of them having investments. Where they do exist, they would, in almost all cases, be term deposits or Government bonds where the value is already clearly established. With a foundation, that has real estate or a share portfolio, the governing board would normally be assessing the value of such investments periodically. A binding obligation to revalue at certain periods would, in my view, be counter-productive. This would force a real estate valuation at set times without regard to market fluctuations. Further, the obligation to engage a licensed valuer incurs a cost for no identifiable benefit.

   I see little benefit in the valuation rules applicable to Private Ancillary Funds being imposed upon the Public Ancillary Funds. As stated above, the Objectives of those in the management of Public Ancillary Funds is different to the Private Ancillary Fund.

3. The lodgement of a tax return for a Public Ancillary Fund is in principle supported. However I would strongly encourage this being a specialist type of form. This is currently the position with the Private Ancillary Funds and recognises the difference between these funds and a conventional trust income tax return.

   Most accountants in public practice will have little or no awareness of ancillary funds, public or private. If they have a requirement to prepare a conventional trust tax return for a Private Ancillary Fund, they will approach the matter as if it was a commercial tax return. The probability of misleading tax returns and misleading information would therefore be high. On a number of occasions I have needed to repair the damage done by accountants and solicitors in public practice, who have sought to assist a client in respect to a charitable institution or a charitable fund, and have prepared documents, which do not comply with Tax Concession Charity (TCC) and DGR requirements. In my view, most accountants in public practice would experience difficulty in handling the tax return for a Private Ancillary Fund.

   I support disclosure to Government through ATO as I see that is of public benefit. It is unclear to me what "greater public disclosure" would mean. If this means all Balance Sheets for Public Ancillary Funds would be made available on the ATO or Treasury website, I have some reserves. I do not see what benefit would arise from that. If, on the other hand, a website was providing information which identified summary information and, as a consequence identified that an annual "Return" had been lodged, I see that as beneficial.

4. I consider the ATO handles the penalty arrangements in a responsible, thoughtful manner and therefore support this proposal.

5. In my view, a Public Ancillary Fund should always have a corporate trustee. This may be under the provisions of Corporations Act, the State Associations legislation or a corporation sole, such as exists with certain Church denominations.

It is appropriate to have in place responsible rules for suspension or removal of trustees. The proposal is supported.

6. The present "Responsible Persons" requirement as identified in TR97/27 appears, in my view, to be serving the needs of the charitable sector well.

7. Transitional arrangements to modify present rules are appropriate. I would suggest a period of 18 months be allowed for. There will be some instances where an existing Public Ancillary Fund may need to be vested to a replacement Ancillary Fund because of difficulties with the change of rules for the existing fund. Given the time required for incorporation of a new Trustee (if such is needed), creation of the Trust and having the appropriate TCC and DGR endorsement provided by ATO, a lesser time frame would impose considerable difficulty on some entities. This is related to the difficulty of conveying information to the Sector, when many Ancillary Funds were established many years ago.

8. I support the classification of the term "Public Fund".

9. The majority of Ancillary Funds would not require an investment strategy, as their only "investment" would be an interest-earning bank deposit.
    - To require such an entity to have an investment strategy is imposing unnecessary regulation.
    - I would encourage there being a limitation on an Ancillary Fund borrowing money at all. In the event that the Ancillary Fund is an asset-holding foundation, I would recommend that any borrowing be subject to ATO or Treasury approval. The State Trustees Acts vary substantially from State to State. The WA Trustees Act, as a result of amendments to the investment area, is quite wide and, in my view, wider than an authorised trustee investment should be.
    - I support the proposal regarding fund transactions be conducted at arm's length.
    - The protection of assets of the fund is an essential issue. This is however the responsibility of the trustee entity and its Board and should be expressed in the Trust Deed itself, and not in some Government regulation of which the Board itself may be unaware.

I trust these comments are of assistance.

Yours faithfully

**N E HARDING**