

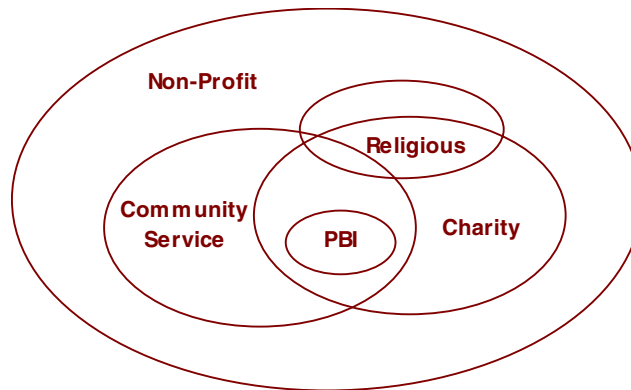
OVERVIEW

This Report is about definitional issues concerning charities and related entities, namely public benevolent institutions, religious institutions and community service organisations. The Committee's terms of reference require it to consider these matters in the context of Commonwealth law. Although that law is for the most part revenue law, this Report is not about the taxation treatment of charities and related entities.

The current understanding of what constitutes a charity has been developed by the common law over several centuries. The term 'charity' has not been legislatively defined in Australia, nor in the United Kingdom or any common law country with the exception of Barbados. Furthermore, there is no judicial definition of it. Many judges have said that it is impossible to define. Nevertheless, it is possible to extract from the vast numbers of judicial decisions the elements that will identify a purpose as charitable. Fundamental to the judicial development of the law relating to charities has been the Preamble to the *Statute of Charitable Uses* enacted by the English Parliament in 1601. The Statute was repealed long ago but the Preamble was preserved and pervades the law relating to charity today not just in the United Kingdom but throughout the common law world.

Community service organisation, public benevolent institution and religious institution, and other terms, have been introduced into the Commonwealth revenue Acts in a piecemeal way over the years in response to changing policy priorities. Their relationship with charity is unclear and the boundaries between them are blurred and cause confusion. The current situation is well represented in the following diagram from the Australian Taxation Office (ATO) submission to the Inquiry.

Figure 1: Non-profit sector¹



Many of the submissions received by the Committee disclosed that there was considerable concern within the charitable sector about the ambit of charity, its relationship with the related entities and the meaning and ambit of each of the expressions used to identify them. They also pointed to a number of other matters including commercial activity, political activity and advocacy, whether governments or government bodies can in some situations be charitable and the extent to which charities must be for the public benefit. As we shall see, the charitable and related sector in Australia is vast in numbers of organisations and in the resources it controls. Yet the legislative, judicial and administrative frameworks within which charities and related entities operate are not well understood. Unquestionably, charity as a concept is complex, as is the law that applies to it.

In an attempt to clarify the law as it now stands, the Committee has developed a definitional framework that incorporates charities and related entities without overlap. Within that framework the Committee recommends a definition of charity that offers enhanced clarity and certainty while retaining the quality of flexibility that has proved of great value in the development of the law over the years.

¹ The diagram does not represent the relative size or population of each category.

The charitable and related sector

Charities and related entities impact on many aspects of our lives. Over 90 per cent of employment in charities is in the provision of health, welfare and education services.² However, charities and related entities also provide religious services and cultural facilities, and are involved in the protection of animals and the natural environment.

Charities and related entities are very diverse and include philanthropic foundations, large institutions that are involved in the provision of a wide range of services, community-based entities providing services for the specific needs of a community, and self-help groups.

The overall size of the wider not-for-profit sector, and charities within that, is significant. The Australian Nonprofit Data Project has estimated that in June 1996, the most recent data published by the Project:

- there were nearly 32,000 nonprofit entities that employed staff, and nearly 19,000 of those were charities; and
- the nonprofit sector employed 6.9 per cent of all people employed in Australia and charities accounted for about 4.8 per cent of people employed.³

Experimental data from the Global Nonprofit Information Systems Project indicates that nonprofit institutions serving households⁴ contributed \$15 billion to gross value added in Australia in 1998-99.⁵

These numbers would rise if nonprofit entities and charities that relied on volunteers were included. For example, about 2.3 million people undertook volunteer work in the third sector in 1996.⁶ ATO data indicates that since 1 July 2000 over 40,000 entities have been endorsed as income tax exempt charities.

2 Lyons, M and Hocking, S 2000, *Dimensions of Australia's Third Sector*, Centre for Australian Community Organisations and Management, University of Technology, Sydney, p 89.

3 Lyons and Hocking, pp 27-51, 77 and 81.

4 Nonprofit institutions serving households are nonprofit institutions that provide goods and services to households. It includes charities but also includes other nonprofit community and member organisations.

5 Data provided to the Inquiry by the Australian Bureau of Statistics.

6 The 'third sector' is broader than the nonprofit sector and also includes finance mutuals and trading cooperatives. See Lyons and Hocking pp 14-15. Lyons and Hocking estimate that there might have been as many as 700,000 third sector organisations in 1996.

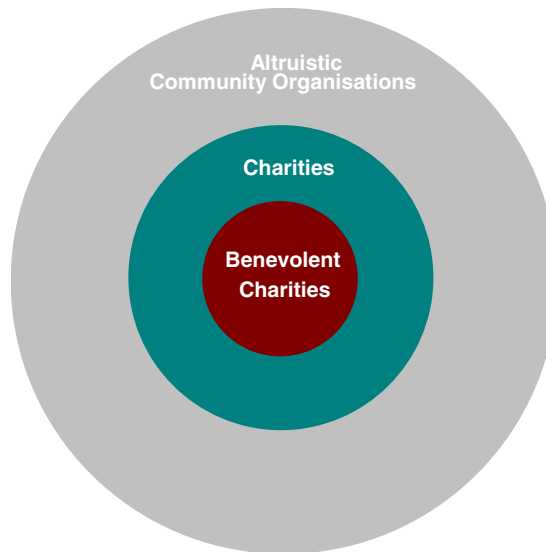
The environment in which charities and related entities operate is changing. Their focus is shifting from the provision of relief to those in need to prevention and early intervention and developing the capacity of communities to address their own needs. They are facing increasing competition for funds and changed arrangements for government funding. Some are in competition with the for-profit sector. The common law meaning of charity and the meaning given by the courts to some of the related terms has sometimes hampered the ability of charities and related entities to respond to these changes.

A definitional framework

The Committee recommends a definitional framework with three distinct categories of Altruistic Community Organisations, Charities and Benevolent Charities. The meaning to be given to each of these terms is spelt out in detail below.

The framework, illustrated in Figure 2, includes only altruistic entities and allows them to be distinguished from other not-for-profit entities such as mutual entities. It provides a mechanism that governments can use to make decisions about the type and level of support they choose to provide to the charitable and related sector.

Figure 2: Altruistic Community Organisations, Charities and Benevolent Charities



A new definition of charity

The Committee recommends that the definition of a charity be set down in legislation. Under the common law approach, the meaning of charity can be clarified and modernised only through litigation. Modern Australian charities have shown a disinclination to litigate and this limits the capacity of the law to respond to changes in the social and economic environment. A legislative definition can more readily provide certainty to the law and bring it up to date.

The recommended definition of a charity builds on the principles that have been developed from the common law, but provides greater clarity and certainty, while maintaining flexibility.

The Committee recommends that a charity be:

- a not-for-profit entity;
- that has a dominant purpose or dominant purposes that are:
 - charitable;
 - altruistic; and
 - for the public benefit.

Not-for-profit entity

The Committee is of the view that the structure of a charity should not generally affect its status and so a charity can be a body corporate, a corporation sole, any association or body of persons whether incorporated or not, or a trust. However, a charity cannot be an individual, a partnership, a superannuation fund, a political party or a government or government body.

Dominant purpose

Dominant purpose or purposes is defined to mean that any other purposes of the entity must further, or be in aid of, the dominant purpose, or be incidental or ancillary to the dominant purpose. However, a charity's purposes must not be illegal, against public policy, or promote a political party or candidate for political office. A charity's activities must further, or be in aid of, the dominant purpose and must not be illegal, against public policy, or promote a political party or candidate for political office.

Applying these principles, the Committee considers that advocating on behalf of those the charity seeks to assist, or lobbying for changes in law or policy that have direct effects on the charity's dominant purpose, are consistent with furthering a charity's dominant purpose. We therefore recommend that such purposes should not deny charitable status provided they do not promote a political party or a candidate for political office.

Commercial purposes or activities of charities aimed at raising funds for a charity's dominant purpose or purposes should also, in the Committee's view, be seen as furthering, or in aid of, the charity's dominant purpose. As a result, such purposes and activities should not deny charitable status. Any issues of competitive neutrality that arise between charitable and for-profit providers of services are not relevant to the definition of a charity but are appropriately a matter for consideration in establishing taxation policy.

Charitable, altruistic and for the public benefit

The recommended definition of a charity is that it must have a dominant purpose that is charitable, altruistic and for the public benefit.

Statute of Elizabeth

One of the Committee's key recommendations is that the definition of a charitable purpose should no longer require that a purpose falls within the 'spirit and intendment' of the Preamble to the Statute of Elizabeth. It seems to us that the Preamble has been valuable but has now outlived its usefulness. The process of determining whether a purpose is within the 'spirit and intendment' of the Preamble or is analogous to a charitable purpose is ambiguous and could lead to inconsistencies. Removing reference to the Preamble to the Statute of Elizabeth has been recommended in England by the Nathan Report in 1952 and the Goodman Report in 1976. The High Court of Australia has commented that 'Perhaps the law is in need of reform' in this respect.⁷

Options for defining charitable purpose

The Committee examined five options that it considers could be used to determine charitable purpose in the absence of the requirement that a purpose fall within the 'spirit and intendment' of the Preamble. The options are:

⁷ *Royal National Agricultural and Industrial Association v Chester* [1974] ALJR 304 at 306.

1. to leave the determination of charitable purpose to the courts, relying on guidance provided by Lord Macnaghten's four heads of charity;⁸
2. to define charitable purpose as any purpose beneficial to the community;
3. to list charitable purposes that fall, or in the Committee's view should fall, within charity;
4. to list broad categories of charitable purpose; and
5. to include the purposes listed in Option 3, as appropriate, under the broad categories set out in Option 4.

The Committee considers that Options 3, 4 and 5 are viable but it recommends Option 5 as providing a principled approach that offers greater certainty and consistency while retaining flexibility.

Under Option 5, charitable purposes shall be:

- the advancement* of health, which without limitation includes:
 - the prevention and relief of sickness, disease or of human suffering;
- the advancement* of education;
- the advancement* of social and community welfare, which without limitation includes:
 - the prevention and relief of poverty, distress or disadvantage of individuals or families;
 - the care, support and protection of the aged and people with a disability;
 - the care, support and protection of children and young people;
 - the promotion of community development to enhance social and economic participation; and
 - the care and support of members or former members of the armed forces and the civil defence forces and their families;
- the advancement* of religion;

8 Lord Macnaghten's four heads of Charity is discussed in Chapter 2.

- the advancement* of culture, which without limitation includes:
 - the promotion and fostering of culture; and
 - the care, preservation and protection of the Australian heritage;
- the advancement* of the natural environment; and
- other purposes beneficial to the community, which without limitation include:
 - the promotion and protection of civil and human rights; and
 - the prevention and relief of suffering of animals.

(* Advancement is taken to include protection, maintenance, support, research, improvement or enhancement.)

The categories of charitable purpose and the specific charitable purposes listed do not attempt to refer specifically to all groups that charities seek to benefit nor all the activities that charities undertake. It is not appropriate for the definition to include a specific reference to a purpose where that purpose is adequately covered by a general reference. For example, charities that assist indigenous peoples, refugees or migrants are readily encompassed under purposes such as the advancement of health or the advancement of education or the advancement of social and community welfare.

The definition clarifies the inclusion in charity of certain purposes that are currently in doubt, such as child care services and community development. It also acknowledges the role of preventative activities and a broad range of activities and approaches that are included in the definition applied to the term 'advancement'.

Strengthened public benefit test

The Committee recommends that the principles developed through the common law to determine whether a purpose is for the public benefit should remain. That is, the purpose must be aimed at achieving a universal or common good, it must have practical utility and it must be for the benefit of the general community or a sufficient section of it. However, we are of the view that the public benefit 'test' should be strengthened by emphasising that a charity's dominant purpose must also be altruistic.

The strengthened public benefit test was applied to a number of issues that came before the Committee. For example, we recommend that self-help groups that have open and non-discriminatory membership be regarded as having met the public benefit test. Government bodies are not altruistic and so should continue to be excluded from charity. Mutual groups and certain other groups whose members are linked by family or employment ties are also not altruistic and should be excluded from charity.

Definition of Benevolent Charity

The Committee acknowledges that governments may, due to limited resources, seek a targeted approach to the support they provide to the sector. The framework recommended by the Committee provides a mechanism to assist government decision making by including a subset of charity.

The Committee has examined the current definition of public benevolent institution, the category that currently receives more favourable treatment, and we consider that it has significant shortcomings. The restriction that public benevolent institutions be limited to the 'direct' provision of assistance is clearly out of date. It accords neither with the needs of those that charity seeks to assist nor with the accepted best practice of how to meet those needs. The requirement that public benevolent institutions provide assistance to those requiring 'pity and compassion' appears paternalistic and demeaning. Relying on such a concept is too subjective an approach to engender clarity in any definition. We consider that the recommendation that charities be altruistic is a more than adequate replacement for 'pity and compassion'.

The Committee recommends that there be a subset of charity, to be known as Benevolent Charity, that would replace public benevolent institutions. Benevolent Charities are entities that meet all the requirements to be a charity and whose dominant purpose is to benefit, directly or indirectly, those whose disadvantage prevents them from meeting their needs. The category of Benevolent Charity distinguishes charities whose dominant purpose is to benefit the disadvantaged from other charities whose dominant purpose is to provide benefits to the community more broadly.

The category of Benevolent Charity does not distinguish between charities on the basis of whether their purpose is to benefit the disadvantaged directly or indirectly. It is therefore wider than the category of public benevolent institution which is restricted to the provision of direct relief.

Definition of Altruistic Community Organisation

The definitional framework also includes a category broader than charity, to be known as Altruistic Community Organisations, to replace community service organisations. Altruistic Community Organisations are entities that are not-for-profit and have a main purpose that is altruistic. That is, they can have secondary purposes that are not altruistic and that do not further, or aid, the altruistic purpose or are not incidental or ancillary to the altruistic purpose. This category is wider than the current category of community service organisation because it does not require the entity to have community service purposes. The category of Altruistic Community Organisations would include all charities as well as entities that have charitable and some non-charitable purposes, such as social purposes, or that have altruistic as well as membership purposes. It cannot have purposes or activities that are illegal, are against public policy or promote a political party or a candidate for political office.

Other categories

The Committee also considered whether to retain the separate categories of religious institutions, scientific institutions and public educational institutions, in addition to charities, within its proposed framework. Where entities have purposes such as the advancement of religion, education and science and those entities are altruistic and for the public benefit, they will readily fall within the scope of charity and so be part of the framework. The Committee is of the view that entities whose purposes are religious, scientific and educational but are not altruistic and not for the public benefit should not be included in the framework.

Administration

An issue that emerged during the course of the Inquiry was administration.

The ATO expressed the view that 'administration would be better served by a single, independent common point of decision making on definitions leading to conclusions about whether organisations are charitable or non-profit, or not'. This view was mirrored in a number of submissions from charities and related entities that sought greater transparency and accountability. Other submissions raised some concerns about consistency of decision making by the ATO and argued that decisions on charitable and related status should be

separate from decisions about taxation liability. The Committee has not sought a response from the ATO on particular claims raised and so does not comment on the merits of any of them.

Under the approach recommended in this Report, the definitions of charity, Benevolent Charity and Altruistic Community Organisation will need to be applied on a case-by-case basis and determined on the facts of each case. The administration of those principles will therefore be an important factor in ensuring greater consistency. The Committee recommends that an independent administrative body be established to determine the status of charities and related entities. Its decisions would be binding on the ATO. The independent body would be the central point for ensuring the accountability of charities to the public. A clear and consistent accountability framework would help to maintain and enhance public confidence in the integrity of charity and provide scope to develop a common framework of reporting requirements to meet the needs of all relevant government agencies.

The Inquiry's terms of reference asked that it provide options that can be applied at the Commonwealth level. The definitional framework recommended by the Committee meets that requirement. However, State and Territory Parliaments and Governments also rely on the common law definition of charity and have adopted some of the terms used in Commonwealth revenue Acts, namely religious institution and public benevolent institution. The Committee is of the view that clarity and consistency can be further enhanced if a common approach to defining charities and related entities were to be taken by all levels of government. We therefore recommend that the Commonwealth seek the agreement of the States and Territories to the adoption nationally of the definitional framework recommended here. We also recommend that the agreement of the States and Territories be sought to the establishment of an independent administrative body to oversee charities and related entities.

