

FIERCE EXTREMES: WILL TAX ENDORSEMENT STYMIE MORE NUANCED ENFORCEMENT BY THE AUSTRALIAN CHARITIES AND NOT-FOR-PROFITS COMMISSION?

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The Australian Charities and Not-for-profits Commission Act 2012 (Cth) commenced on 3 December 2012, delivering Australia a federal regulator for not-for-profits, the Australian Charities and Not-for-profits Commission (ACNC). The ACNC is expected to effect a 'fundamental change' from the current system where the Australian Taxation Office, as the 'default Commonwealth regulator', has been 'unable to take action commensurate to the circumstances being addressed'. However, the ACNC's achievement of its regulatory goals, especially by means of proportional enforcement action, may be stunted by regulatory overlap with the Commissioner of Taxation. This overlap is primarily engendered by additional tax endorsement requirements for charities to access tax concessions, such as income tax exemption. In particular, the extension of endorsement special conditions under the Tax Laws Amendment (2013 Measures No 2) Act 2013 (Cth) raises the possibility that charities may face 'fierce extremes' between milder, more nuanced, ACNC compliance action and revocation of income tax endorsement by the Commissioner of Taxation.

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*Feel by turns the bitter change
Of fierce extremes, extremes by change more fierce¹*

1. INTRODUCTION

The *Australian Charities and Not-for-profits Commission Act 2012* (Cth) (*ACNC Act*) and associated legislation commenced on 3 December 2012, delivering Australia a federal regulator for not-for-profits (NFP), the Australian Charities and Not-for-profits Commission (ACNC). The issue is whether the ACNC baby will develop into a healthy adult which effects a ‘fundamental change’ from the current system where the Australian Taxation Office (ATO), as the ‘default Commonwealth regulator’, is ‘unable to take action commensurate to the circumstances being addressed’.² The prime concern is that the ACNC’s achievement of its regulatory goals, especially by means of proportional enforcement action, will be stunted by regulatory overlap with the Commissioner of Taxation.

The overlap is primarily engendered by additional tax endorsement requirements for charities to access tax concessions, such as income tax exemption. Due to the ACNC’s jurisdiction, the issue of intersecting regulation is initially limited to charities, with non-charity NFPs seeking tax endorsement appropriately subjected to a layer of regulation by the Commissioner of Taxation. However, the problem for charities is that there is the possibility of ‘fierce extremes’ between milder, more nuanced, compliance action by the ACNC and revocation of income tax endorsement by the Commissioner

¹ John Milton, *Paradise Lost* (Oxford University Press, 2005) 62 (book 2, line 598).

² Revised Explanatory Memorandum, Australian Charities and Not-for-profits Commission Bill 2012 (Cth) and Australian Charities and Not-for-profits Commission (Consequential and Transitional) Bill 2012 (Cth) (*ACNC Revised Explanatory Memorandum*) 120 [9.25].

TAX ENDORSEMENT AND THE ACNC

of Taxation. The danger of such extremes is especially marked in light of the extension of endorsement special conditions under the *Tax Laws Amendment (2013 Measures No 2) Act 2013* (Cth) (*TLA 2013 Measures No 2 Act*), as well as the further rewrite that may be implemented if the *Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012* (Cth) (Special Conditions Bill) is reintroduced into Parliament.³ For instance, the Commissioner of Taxation may be able to, or required to, revoke endorsement for breaches of a charity's governing rules, even where charity controllers have acted honestly and reasonably, but inconsistently, with the purposes of the charity, or involving the derivation of personal benefits from charitable funds.⁴ The issue is significant, given that over 56,000 charities are registered with the ACNC.⁵

The ACNC's role, including its gatekeeper function of determining an entity's charitable status and satisfaction of the other registration requirements, is outlined in Part 2 of this paper. The broad range of enforcement powers provided to the ACNC Commissioner are examined, along with the government's desire for a tailored use of those powers in a harmonised way with other regulators, where feasible.

In considering the overlap between the ACNC Commissioner's enforcement function and that of the Commissioner of Taxation, this paper focuses on income tax exempt endorsement rules for charities. Part 3.1 sketches the current income tax endorsement conditions, as well as discussing the considerably expanded requirements as a result of the *TLA 2013 Measures No 2 Act* and proposed under the Special Conditions Bill. The limited responses available for

³ The Special Conditions Bill lapsed with the proroguing of Parliament on 5 August 2013.

⁴ See below Parts 3.2 and 4.3.

⁵ ACNC, 'First 10 New Charities Registered' (Media Release, No 018, 11 January 2013)

<https://www.acnc.gov.au/ACNC/Comms/Med_R/MR_018.aspx>.

breach of the tax endorsement conditions are considered in Part 3.2, demonstrating the restricted options, despite the Commissioner of Taxation's preferred 'pyramid' compliance model.

Part 4 examines how the tax endorsement conditions overlay the ACNC registration requirements and, hence, how the ACNC Commissioner and the Commissioner of Taxation continue to serve separate, but overlapping, roles in relation to the regulation of charities. Although it is too early in the development of the ACNC to confidently predict whether fierce extremes will occur between ATO and ACNC enforcement action, this examination demonstrates a real risk of potential divergence. More fundamentally, the analysis demonstrates a risk in the structure of the regulatory scheme that the Commissioner of Taxation's revocation power might stymie the aim of achieving proportional supervision of charities due to the *TLA 2013 Measures No 2 Act* changes. It also identifies that the regulatory regime creates uncertainty for charities about the manner in which coordination of enforcement responses will occur and, indeed, about the Commissioner of Taxation's power to do so. These risks are then evaluated against the regulatory goals of the overlapping provisions to see whether they are justified.

Finally, several preliminary reform options are outlined for further investigation in the Conclusion. While the purpose of this article is focussed on an evaluation against stated regulatory goals, such further investigation could incorporate broader regulatory theory in designing the reforms.⁶

⁶ For a discussion of regulatory theory in the NFP context, see, eg, Not-for-Profit Project Tax Group, *Regulating the Not-for-profit Sector Working Paper* (July 2011) University of Melbourne <<http://www.law.unimelb.edu.au/files/dmfile/MicrosoftWord-RegulatingtheNot-for-ProfitSectorWorkingPaperfinalversion2.pdf>> (and the sources cited therein); Jonathan Garton, 'The Future of Civil Society Organisations: Towards a Theory of Regulation for Organised Civil Society'

TAX ENDORSEMENT AND THE ACNC

2. GRADUATED & HARMONISED ENFORCEMENT BY THE ACNC COMMISSIONER

On 3 December 2012, Australia's nascent independent statutory regulator for NFPs⁷ launched its website and sent its first email.⁸ Initially, the ACNC governs charities, but in the longer term, potentially all NFPs.⁹ As well as establishing the ACNC, the *ACNC Act* creates a 'regulatory framework' for registered entities, with the goals of supporting 'public trust and confidence' in not-for-profits; 'support[ing] and sustain[ing]' the sector; and championing a decrease in 'unnecessary regulatory obligations'.¹⁰

A key government aim is to ensure that the application of the new framework provides an appropriate level of regulation (by reference to 'size' and 'risk') and that this is achieved in a

in Myles McGregor-Lowndes and Kerry O'Halloran (eds), *Modernising Charity Law* (Edward Elgar Publishing, 2010) 207-27.

⁷ The term 'not-for-profit' can cover a broad range of entities, see, eg, Productivity Commission, 'Contribution of the Not-for-Profit Sector' (Research Report, 11 February 2010) 3-8. For the purposes of this paper, the term covers 'entities that seek to achieve a community, altruistic or philanthropic purpose' such that an entity 'is not operating for the profit or gain of its individual members' and 'does not provide any private benefit' to related parties or associates except by way of 'reasonable remuneration for services provided or re-imbursment of related costs': ACNC Revised Explanatory Memorandum 7 [1.5], 32 [3.33]-[3.34].

⁸ ACNC, 'ACNC Open for Business' (Media Release, No 010, 3 December 2012) <http://www.acnc.gov.au/ACNC/Comms/Med_R/MR_010.aspx>. For a general description of the ACNC amendments, see, eg, Yat To Lee, 'Charities and NFPs: Tax Concessions and Reform' (2012) 47 *Taxation in Australia* 217; Kylie Maxwell, 'Reducing Red Tape: A New Regulator for the Charities Sector' (2012) 26 *Commercial Law Quarterly* 7. See also Ann O'Connell, 'The Not-for-profit Sector and the Tax Forum' (2012) 27 *Australian Tax Forum* 287, 293-4.

⁹ *ACNC Act* ss 15-5, 25-5(5); ACNC Revised Explanatory Memorandum 7 [1.2]-[1.3], 13 [1.48].

¹⁰ *ACNC Act* s 15-5(1); ACNC Revised Explanatory Memorandum 3-4.

harmonised fashion across regulators, where feasible.¹¹ This approach also applies to the ACNC Commissioner's compliance powers, with the ACNC Revised Explanatory Memorandum emphasising that the broad scope of powers should enable 'proportionate, balanced and effective' action.¹² The reason is that, ultimately, the reforms are intended to promote 'a robust, vibrant, independent and innovative Australian NFP sector'.¹³

2.1 Role of the ACNC

The role of the ACNC and the ACNC Commissioner is to administer the regulatory framework created by the *ACNC Act* in furtherance of the regulatory goals identified above, with the chief tasks of acting as gatekeeper by determining charity status and then registering such eligible entities; followed by regulating registered charities.¹⁴ The regulation function involves:¹⁵

- acting as educator to aid registered charities to comply with the *ACNC Act*;¹⁶
- a monitoring and enforcement function to ensure compliance by registered charities where education is insufficient;¹⁷
- maintaining a public register with a range of information on registered charities;¹⁸ and
- cooperating with other regulators and government agencies to reduce regulatory duplication.¹⁹

¹¹ ACNC Revised Explanatory Memorandum 8 [1.12]-[1.13].

¹² *Ibid* 17 [1.79].

¹³ *Ibid* 8 [1.14], 21 [1.111].

¹⁴ *ACNC Act* s 15-5(2).

¹⁵ *Ibid* ss 15-5(2), 15-10(f), 105-15.

¹⁶ *Ibid* ss 15-5(2)(b)(iii), 110-10(1).

¹⁷ *Ibid* s 15-5(2)(b)(ii), ch 3, ch 4.

¹⁸ *Ibid* pt 2-2.

¹⁹ *Ibid* s 15-10(f).

TAX ENDORSEMENT AND THE ACNC

2.2 Registration

As noted above, the ACNC Commissioner is responsible for ‘registering’ NFPs. Registration is the codeword required to enter the new regime. While it entails a number of obligations, it unlocks access to a range of other government benefits, including tax concessions, and programs, so that even though voluntary,²⁰ many NFPs will have no practical choice but to register.

In broad terms, the ACNC Commissioner is obliged to register an entity if it:

- is a charity;²¹
- is a not-for-profit entity;
- has an Australian Business Number;
- complies with specified governance and external conduct standards (the external conduct standards are yet to be promulgated), with some exceptions for basic religious charities;²² and
- is not included in a written decision of an Australian government agency under an Australian law relating to the characterisation of entities as engaging in or supporting terrorist or criminal activities.²³

²⁰ *ACNC Act* ss 15-5(3)-(4), 20-5(2)-(3); ACNC Revised Explanatory Memorandum 17-8 [1.82]-[1.83].

²¹ The registration process also allows the ACNC Commissioner to record any relevant ‘subtype’ of charity that describes the NFP, for instance, that it is a public benevolent institution: *ACNC Act* ss 25-5(2), (5). This potentially enables charities to access tax or other concessions which are specific to that subtype.

²² *ACNC Act* s 45-15(5).

²³ *ACNC Act* ss 25-5(1), (3), (5); ACNC Revised Explanatory Memorandum 31 [3.24]. It appears intended that the range of NFPs which can be registered will, in time, be expanded beyond charities: ACNC Revised Explanatory Memorandum 31 [3.23].

The registration process therefore charges the ACNC Commissioner with determining whether an entity is a charity or not, a task which is initially to be conducted by applying the common law concept of charity as expanded by the *Extension of Charitable Purpose Act 2004* (Cth).²⁴ From 1 January 2014, the codified definition of charity contained in the *Charities Act 2013* (Cth), will apply.²⁵ The concessions referred to above are then ‘unlocked’ because the determination also applies for the purposes of other federal agencies, including the ATO, which administer charity concessions.²⁶ Transitional rules mean that charities which are endorsed as income tax exempt by the Commissioner of Taxation, will be automatically registered with the ACNC.²⁷

²⁴ ACNC Revised Explanatory Memorandum 35 [3.50]. The common law concept of charity requires, first, that the entity’s purposes be charitable in the technical sense (that is, the ‘relief of poverty’, the ‘advancement of education’, the ‘advancement of religion’, or ‘other purposes beneficial to the community’). Second, the entity must be for the public benefit (unless it is for the relief of poverty, where such benefit is presumed). This means that the entity must bestow an actual benefit, and must do so in relation to the public or a section of the public rather than a private class of individuals. For the common law meaning of charity, see, eg, G E Dal Pont, *Law of Charity* (LexisNexis Butterworths, 2010) 16-29 [2.1]-[2.22]; ATO, *Income Tax and Fringe Benefits Tax: Charities*, TR 2011/4, 12 October 2011. For a comprehensive literature review of the meaning of charity, see Not-for-Profit Project Tax Group, *Defining Charity: A Literature Review* (20 February 2011) University of Melbourne <<http://www.law.unimelb.edu.au/tax/research/current-research-projects/defining-taxing-and-regulating-not-for-profits-in-the-21st-century/publications>>.

²⁵ While the *Charities Act 2013* (Cth) does make some adjustments to the common law concept of charity, those adjustments are not relevant to the analysis of regulatory overlap explored in this paper.

²⁶ ACNC Revised Explanatory Memorandum 35 [3.52].

²⁷ *Australian Charities and Not-for-profits Commission (Consequential and Transitional) Act 2012* (Cth) (*Consequential and Transitional Act*) sch 1 items 2(2), 3(2), 4(2).

TAX ENDORSEMENT AND THE ACNC

Once registered, a charity has to comply with the record keeping, reporting and notification²⁸ requirements of the *ACNC Act* and also the governance standards and external conduct standards created under it.²⁹ At the date of writing, governance standards were in force,³⁰ but despite earlier Government announcements,³¹ no external conduct standards had been made. The governance standards enshrine minimum outcomes in respect of the ‘practices and procedures’ adopted by an entity to govern its operations so as to enable it to carry out its purposes.³² The standards are also intended to engender public confidence that, amongst other things, registered charities will ‘minimise the risk of mismanagement and misappropriation’ and will ‘pursue their purposes’.³³ External conduct standards are aimed at things done outside Australia by registered entities (such as activities or the provision of funds) as well as things which are ‘closely related to’ or which ‘will have a significant impact on’ such external matters.³⁴

2.3 Enforcement

The *ACNC Act* provides the ACNC Commissioner with a spectrum of responses where a registered NFP fails to meet its

²⁸ For instance, notification is required if a significant contravention of the entity’s obligations renders it ineligible for continued registration: *ACNC Act* ss 65-5(1)-(2). Ineligibility for registration will not mean that the ACNC Commissioner will automatically terminate registration, since another regulatory action may be more appropriate: ACNC Revised Explanatory Memorandum 89 [7.19].

²⁹ *ACNC Act* ch 3.

³⁰ *Ibid* s 45-10(1), *Australian Charities and Not-for-profits Commission Regulation 2013* (Cth) (*ACNC Regulations*) div 45.

³¹ David Bradbury, Assistant Treasurer and Minister Assisting for Deregulation and Mark Butler, Minister for Social Inclusion, ‘Staging the Introduction of Regulatory Reform for the Not-for-profit Sector’ (Media Release No 32, 17 May 2012).

³² ACNC Revised Explanatory Memorandum 57 [5.5], 63 [5.43]. See also *ACNC Regulations* s 45.1.

³³ *ACNC Act* s 45-5(1).

³⁴ *Ibid* ss 50-5(2), 50-10(3).

obligations, or where it is more likely than not that it will fail to do so in the future.³⁵ These include:³⁶

- revocation of registration (also available where, amongst other reasons, the entity is no longer entitled to be registered as a charity);³⁷
- the ability to issue a warning about compliance action to a registered entity;³⁸
- issuing a direction to do or refrain from doing an act;³⁹
- accepting an ‘enforceable undertaking’ from a registered entity to do or refrain from doing an act and to enforce that undertaking.⁴⁰ In this case, there is no requirement that a contravention have occurred or be more likely than not to occur, although the undertaking is intended to address current or future non-compliance or potential non-compliance;
- seeking an injunction;⁴¹ and
- suspending, removing and appointing acting ‘responsible entities’.⁴²

³⁵ Alternatively, where the entity is ‘proposing’ to do so, in the case of an injunction; *ibid* ss 95-15(1)-(2), 95-20(1).

³⁶ Other than the power to revoke an entity’s registration, the other compliance powers can generally only be exercised in relation to a ‘federally regulated entity’. This term covers constitutional corporations; trusts if the trustee is a constitutional corporation; and entities which are sufficiently linked to the Northern Territory or the Australian Capital Territory; *ACNC Act* ss 205-15, 205-20.

³⁷ *Ibid* s 35-10(1).

³⁸ *Ibid* ss 80-5(1)-(2).

³⁹ *Ibid* ss 85-5(1), 85-10(1).

⁴⁰ *Ibid* ss 90-10(1)-(2), 90-15(1).

⁴¹ *Ibid* ss 95-15(1)-(2), 95-20(1).

⁴² *Ibid* ss 100-5(1), 100-10(1), 100-15(1), 100-30. A responsible entity is alone or jointly ‘responsible for the decision-making, day-to-day management and compliance of a registered entity’ and would include directors of a company or the trustee of a trust (and the directors of the trustee, if a corporate

TAX ENDORSEMENT AND THE ACNC

In performing this compliance function, the ACNC Commissioner is intended to consider principles of ‘regulatory necessity, risk and proportionality’ so that the Commissioner’s ‘actions are suitable and relative to individual circumstances’.⁴³ In accordance with its *ACNC Statement: Regulatory Approach*,⁴⁴ the ACNC will employ the regulatory principles of ‘Fairness, Accountability, Independence, Integrity and Respect’, with ‘Fairness’ involving proportionate action on the part of the ACNC.⁴⁵ The concept of ‘Fairness’ therefore envisages the use of different compliance tools in different circumstances, depending on the seriousness of the issue.⁴⁶ In accordance with the principles of responsive regulation, the ACNC’s general starting position is to provide charities with ‘a chance to address [the ACNC’s] concerns, and use the least intrusive powers that are sufficient to address those concerns’.⁴⁷

trustee): ACNC Revised Explanatory Memorandum 221 [13.68]-[13.72]; *ACNC Act* s 205-30.

⁴³ ACNC Revised Explanatory Memorandum 21 [1.105]. See also at 21 [1.108], 117 [9.2]-[9.5].

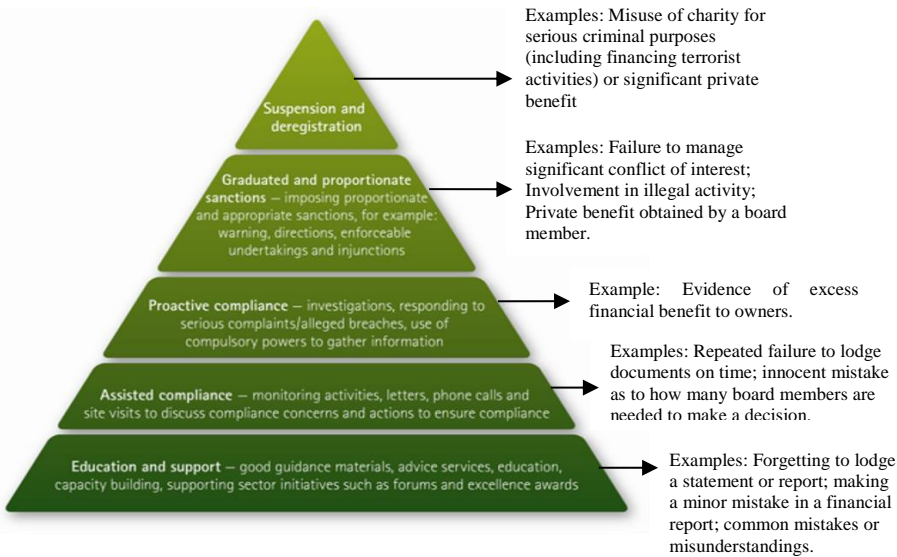
⁴⁴ ACNC, *ACNC Statement: Regulatory Approach* (May 2013).

⁴⁵ *Ibid* 5-6, 10.

⁴⁶ *Ibid* 5.

⁴⁷ *Ibid* 9.

The following ‘regulatory pyramid’ summarises and ranks the ACNC’s compliance responses to accord with this principle:⁴⁸



Specific guidelines mandating the above goals have also been built into each of the chief compliance powers. For instance, before deciding to revoke an entity’s registration, the ACNC Commissioner must generally give the entity an opportunity to respond to the proposed revocation and must consider the following factors:⁴⁹

- the ‘nature, significance and persistence of any contravention’ of an obligation;

⁴⁸ Ibid 11.

⁴⁹ ACNC Act ss 35-10(2), 35-15.

TAX ENDORSEMENT AND THE ACNC

- whether the ACNC Commissioner or the registered charity could do or have done anything to resolve the failure, or to prevent such a failure occurring again;
- the benefits of making certain that ‘contributions’⁵⁰ are applied to the entity’s purpose and in accordance with its charitable status;
- the objects of any pieces of federal legislation for which status as a registered charity is relevant;
- the degree to which the registered charity’s actions may ‘jeopardise ... public trust and confidence in the not-for-profit sector’;
- the ‘welfare’ of those who directly benefit from the registered charity’s activities; and
- any other relevant matter.

The same list of factors must also be considered for each of the other compliance powers listed above, other than those in relation to enforceable undertakings.⁵¹

The ACNC Revised Explanatory Memorandum states that these factors require the ACNC Commissioner to consider the use of other regulatory responses as alternatives to revocation.⁵² For instance, education measures, a warning notice or an enforceable undertaking. A registered entity’s ‘compliance track record’ is also relevant.⁵³ Indeed, the ACNC Revised Explanatory Memorandum suggests that revocation should be

⁵⁰ In broad terms, the provision of money, property or other benefits, including government concessions: *ACNC Act* s 205-40.

⁵¹ *Ibid* ss 80-5(3), 85-5(2), 100-10(9), 100-15(6). The factors are also only indirectly relevant for injunctions: s 95-35.

⁵² ACNC Revised Explanatory Memorandum 43 [3.99]-[3.100], 48 [3.127]. This approach seems permitted, primarily, by the second factor which looks at what the Commissioner could do to resolve the failure or prevent future failures: at 44 [3.107], 44 [3.110].

⁵³ *Ibid* 120 [9.29].

resorted to only for ‘prolonged non-compliance with a governance or external conduct standard’.⁵⁴

Overall, the ACNC Revised Explanatory Memorandum describes this approach to compliance as:

a fundamental change from the sector’s current regulatory framework where the default Commonwealth regulator, the ATO, only has the power to remove an entity’s access to tax concessions and is unable to take action commensurate to the circumstances being addressed.⁵⁵

Indeed, Chia, Harding, O’Connell and Stewart especially ‘welcomed’ the ‘proportional’ approach when Treasury released its 2011 final report on a national regulator.⁵⁶ Further, Turnour and McGregor-Lowndes refer to the ACNC regime as encompassing ‘modern light touch surgical regulation’.⁵⁷ This article examines whether the benefits of such an approach may be lost due to the enforcement of overlapping tax endorsement requirements.

3. ENFORCEMENT OF TAX ENDORSEMENT CONDITIONS BY THE COMMISSIONER OF TAXATION

This Part examines the endorsement conditions charities must meet to maintain income tax exempt status, as well as the compliance tools available to the Commissioner of Taxation where those conditions are breached. As will be expanded further in Part 4, this analysis demonstrates a degree of regulatory duplication with the ACNC Commissioner, especially due to the *TLA 2013 Measures No 2 Act* reforms; but a narrower

⁵⁴ Ibid 60 [5.24].

⁵⁵ Ibid 120 [9.25].

⁵⁶ Not-for-Profit Project Tax Group, *Regulating the Not-for-profit Sector*, above n 6, 24.

⁵⁷ Matthew Turnour and Myles McGregor-Lowndes, ‘Taxing Charities: Reform Without Reason?’ 47(2) *Taxation in Australia* 74, 75.

TAX ENDORSEMENT AND THE ACNC

breadth of enforcement options for the Commissioner of Taxation.

3.1 Endorsement

For charities to be eligible for income tax exemption, they must fall within the categories of charitable entity listed in s 50-5 of the *Income Tax Assessment Act 1997* (Cth) (*ITAA97*).⁵⁸ Until 3 December 2012, the categories included a ‘charitable institution’ and a ‘fund established in Australia for public charitable purposes by will or instrument of trust’ (charitable fund).⁵⁹ From 3 December 2012, the *Consequential and Transitional Act* makes some significant reforms.⁶⁰ One of the reforms is that the distinction between charitable institutions and charitable funds has been removed in most cases,⁶¹ such that only one class of charities remains: a ‘registered charity’.⁶² Whether a charity is a ‘registered charity’ for the purposes of the *ITAA97* is based on whether the entity has been registered as a charity under the *ACNC Act*.⁶³

The registered charity category is then subject to several additional special conditions that must be satisfied. These have recently been revised several times, so that there are now four

⁵⁸ *ITAA97* s 50-1.

⁵⁹ *Ibid* s 50-5 items 1.1, 1.5B. As to charitable funds, see also items 1.5 and 1.5A as at 2 December 2012.

⁶⁰ Note that the following ruling has not yet been updated: ATO, *Income Tax and Fringe Benefits Tax: Charities*, TR 2011/4, 12 October 2011.

⁶¹ Separate categorisation of ‘religious institutions’ has also been removed.

⁶² See especially *Consequential and Transitional Act 2012* (Cth) sch 2 items 20, 30, 31, 35. This appears to be based on the unified special conditions expected to be introduced upon the passage of the Special Conditions Bill (some of which have now been implemented by the *TLA 2013 Measures No 2 Act*): ACNC Revised Explanatory Memorandum 260 [15.44]-[15.45].

⁶³ *Consequential and Transitional Act 2012* (Cth) sch 2 items 20, 30. To avoid any doubt about the need for ACNC registration, see *ITAA97* ss 50-47, 50-110(5) (as amended by the *TLA 2013 Measures No 2 Act* sch 11 pt 1).

that broadly apply to all charities.⁶⁴ First, the conditions continue to require that the entity be endorsed by the Commissioner of Taxation,⁶⁵ which in turn means the charity must fall within the identified category,⁶⁶ have applied for endorsement in the approved way,⁶⁷ have an ABN,⁶⁸ and have met the other special conditions.⁶⁹ Second, in somewhat circular fashion, registered charities are required (again) to be registered under the *ACNC Act*.⁷⁰ Third, all charities must now meet one of the following conditions derived from s 50-50 of the *ITAA97*, which in general terms apply a geographic nexus test:⁷¹

- the entity ‘has a physical presence in Australia and, to that extent, incurs its expenditure and pursues its objectives principally in Australia’ (the ‘in Australia’ test);⁷²
- it is an institution that is a deductible gift recipient referred to in item 1 of the table in s 30-15(2) of the *ITAA97* (deductible gift recipients generally have to pass a separate in Australia test, unless individually named and permitted or

⁶⁴ *Ibid* sch 2 items 30, 33, 37, sch 4 items 4-7. However, charitable funds established before 1 July 1997 continue to be accorded concessional exclusions from the special conditions; *ibid* sch 2 item 40.

⁶⁵ *ITAA97* s 50-52(1).

⁶⁶ *Ibid* s 50-110(2).

⁶⁷ *Ibid* s 50-105.

⁶⁸ *Ibid* s 50-110(3).

⁶⁹ *Ibid* s 50-110(5)(a). A ‘reasonable grounds’ test applies to entities which have not yet carried on activities as a charity at the time of application for endorsement: s 50-110(5)(b) (including as amended by *Consequential and Transitional Act 2012* (Cth) sch 2 item 38 and as the provision will be amended from 1 January 2014 by the *Charities (Consequential Amendments and Transitional Provisions) Act 2013* (Cth) sch 1 item 33).

⁷⁰ *Ibid* s 50-47 (as introduced by the *TLA 2013 Measures No 2 Act* sch 11 pt 1).

⁷¹ *Consequential and Transitional Act 2012* (Cth) sch 2 items 30, 37. It is unclear why the requirement that the entity be an ‘institution’ has not been removed from two of the three conditions.

⁷² See, eg, ATO, *Endorsement to Access Charity Tax Concessions: Income Tax Exemption* (3 December 2012)

<<http://www.ato.gov.au/nonprofit/content.aspx?menuid=0&doc=/content/13267.htm&page=5&H5>>.

TAX ENDORSEMENT AND THE ACNC

under certain externally focussed deductible gift recipient categories)⁷³; or

- it is prescribed by name in regulations and is a foreign institution which is exempt from income tax in its home jurisdiction or is an institution with a ‘physical presence in Australia but which incurs its expenditure and pursues its objectives principally outside Australia’.⁷⁴ This is referred to as the ‘prescribed by law’ test.⁷⁵

This is the same test as that which previously applied for charitable institutions.⁷⁶ While it could be interpreted as implicitly requiring that a charity pursue its objectives, the test is predominantly focussed on a geographic nexus with Australia rather than with the use of funds for non-charitable purposes.⁷⁷

Finally, for income years commencing on or after 30 June 2013, the *TLA 2013 Measures No 2 Act* adds a fourth requirement under s 50-50 of the *ITAA97*. That is, that every charity must ‘comply with all the substantive requirements in its governing rules’ and ‘apply its income and assets solely for the

⁷³ See, eg, ATO, *The Endorsement Process for Deductible Gift Recipients: What Does In Australia Mean?* (4 December 2012)

<<http://www.ato.gov.au/nonprofit/content.aspx?menuid=0&doc=/content/13268.htm&page=7&H7>>.

⁷⁴ These entities are prescribed on a case by case basis in accordance with government policy; ATO, *Endorsement to Access Charity Tax Concessions: Prescribed by Law Test* (3 December 2012)

<<http://www.ato.gov.au/nonprofit/content.aspx?menuid=0&doc=/content/13267.htm&page=8&H8>>.

⁷⁵ *Ibid.*

⁷⁶ The constraint which formerly applied to charitable funds, that a fund be ‘applied for the purposes for which it was established’, has been removed; *Consequential and Transitional Act 2012* (Cth) sch 3 item 6. Now see new *ITAA97* s 50-50(2), as introduced by *TLA 2013 Measures No 2 Act* sch 11 item 41.

⁷⁷ See, eg, the focus in ATO, *Endorsement to Access Charity Tax Concessions: In Australia Test* (3 December 2012)

<<http://www.ato.gov.au/nonprofit/content.aspx?menuid=0&doc=/content/13267.htm&page=6&H6>>.

purpose for which the entity is established'.⁷⁸ The Explanatory Memorandum acknowledges that an entity's activities can be relevant to a determination of its purpose,⁷⁹ which is consistent with the approach adopted in the case law to determine whether an entity continues to be a 'charitable institution'.⁸⁰ However, the endorsement conditions are intended to go further. For instance, even where activities do not demonstrate a non-charitable purpose, they may still breach the conditions where there has been failure to observe 'rules of core importance to the operation of the entity' such as 'those related to an entity's object and purpose and those relating to an entity's not-for-profit status'.⁸¹ This would not include 'minor procedural irregularities'.⁸² These amendments have been extracted from a broader set of endorsement special conditions contained in the Special Conditions Bill.⁸³

In addition, the Special Conditions Bill would have obliged a charity seeking income tax exempt status to be a 'not-for-

⁷⁸ *TLA 2013 Measures No 2 Act* sch 11 item 41 (new *ITAA97* s 50-50(2)).

⁷⁹ Explanatory Memorandum, Tax Laws Amendment (2013 Measures No 2) Bill 2013 (Cth) 224 [11.58].

⁸⁰ *FCT v Word Investments Ltd* (2008) 236 CLR 204 (*Word Investments*), 236-237 [70] (Gummow, Hayne, Heydon and Crennan JJ); *FCT v Bargwanna* (2012) 244 CLR 655, 668 [36] (French CJ, Gummow, Hayne and Crennan JJ) (*Bargwanna*).

⁸¹ Explanatory Memorandum, Tax Laws Amendment (2013 Measures No 2) Bill 2013 (Cth) 224-5 [11.59]-[11.62].

⁸² Explanatory Memorandum, Tax Laws Amendment (2013 Measures No 2) Bill 2013 (Cth) 224 [11.61].

⁸³ The measures in the Special Conditions Bill formed part of a package that was initially aimed at updating the 'in Australia' tests following *Word Investments* (2008) 236 CLR 204; Explanatory Memorandum, Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 (Cth) 10 [1.34]. For the mirror provisions and their corresponding explanation, see Special Conditions Bill sch 1 item 38; Explanatory Memorandum, Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 23-4 [1.96]-[1.100]. The Special Conditions Bill lapsed with the proroguing of Parliament on 5 August 2013.

TAX ENDORSEMENT AND THE ACNC

profit entity'.⁸⁴ A 'not-for-profit entity' was defined as an entity which is not carried on for the profit or gain of owners or members and as being prohibited from distributing (and which does not distribute) profits or assets to owners or members.⁸⁵ Finally, the Special Conditions Bill would also have restated the current s 50-50 *ITAA97* geographic nexus condition, primarily to tighten its rules, especially in relation to conduit funding of offshore activities, which may satisfy the current test.⁸⁶ If not endorsed as a deductible gift recipient or prescribed in regulations, a charity would generally have to satisfy a rewritten in Australia test, which would require the entity to 'operate principally in Australia' and 'pursue its purposes principally in Australia'.⁸⁷

It should be acknowledged that some endorsement requirements in the *TLA 2013 Measures No 2 Act* (and in the Special Conditions Bill) for income tax exempt status, apply to a broader range of entities than charities.⁸⁸ In circumstances where the ACNC currently applies only to charities, such additional endorsement requirements may be necessary for these entities. However, the focus of this paper is on the overlapping requirements for charities and the *TLA 2013 Measures No 2 Act* requirements discussed above are expressly directed toward 'registered charities'.⁸⁹

⁸⁴ Special Conditions Bill sch 1 item 38.

⁸⁵ *Ibid* sch 1 item 44.

⁸⁶ *Ibid* sch 1 item 38; Explanatory Memorandum, Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 (Cth) 12, 14 [1.55], 14 [1.59]-[1.60], 19-22 [1.74]-[1.89].

⁸⁷ Special Conditions Bill sch 1 item 38.

⁸⁸ *TLA 2013 Measures No 2 Act* sch 11 pt 5; Special Conditions Bill sch 1 item 38.

⁸⁹ *TLA 2013 Measures No 2 Act* sch 11 items 38, 40, 41.

3.2 Enforcement

The Commissioner of Taxation is responsible for endorsing charities as income tax exempt.⁹⁰ Any failure to meet the special conditions means, for an entity that is not yet endorsed, that it cannot be so endorsed;⁹¹ and, for an entity that is endorsed, that it must notify the Commissioner of Taxation.⁹² The Commissioner also has the power to require an endorsed entity to provide information that would enable the Commissioner to check the entity's entitlement to endorsement.⁹³

However, what can the Commissioner of Taxation do if an entity ceases to meet the endorsement conditions? There are two matters relevant to this question. First, while the *Consequential and Transitional Act* and the *TAA 2013 Measures No 2 Act* effect a number of changes to the Commissioner of Taxation's endorsement process under the *TAA*,⁹⁴ they do not introduce a series of enforcement measures which would enable a proportionate response. Accordingly, unlike the ACNC Commissioner, the Commissioner of Taxation's only primary regulatory responses are, generally,⁹⁵ to ignore the loss of entitlement, revoke endorsement,⁹⁶ or seek prosecution of a charity for failing to notify the Commissioner of Taxation of loss of endorsement in some circumstances.⁹⁷ This is despite the fact that the Commissioner of Taxation's overall approach to

⁹⁰ *ITAA97* ss 50-105; *Taxation Administration Act 1953* (Cth) (*TAA*) sch 1 div 426.

⁹¹ *ITAA97* ss 50-110(1), 50-110(5)(a).

⁹² *TAA* sch 1 s 426-45(1).

⁹³ *Ibid* sch 1 s 426-40(1).

⁹⁴ The changes relate predominantly to the removal of the distinction between institutions and funds and to the inclusion of information about ACNC registration in the Australian Business Register.

⁹⁵ If a backdated revocation of endorsement means that tax has been underpaid, then the Commissioner should also be able to issue an assessment to recover this amount and may be able to impose penalties and interest.

⁹⁶ *TAA* sch 1 s 426-55(1).

⁹⁷ Failure to notify is likely to constitute a tax offence; *ibid* s 8C(1).

TAX ENDORSEMENT AND THE ACNC

compliance is grounded in responsive regulation and adopts a 'pyramid' shaped model which relies on facilitative measures at the bottom of the pyramid and more coercive and intrusive regulatory action for taxpayers at the top.⁹⁸

Second, it is unclear whether the Commissioner has any choice about revoking endorsement when the conditions are not satisfied, or is permitted to take account of as broad a range of factors as the ACNC Commissioner. The revocation power says that the Commissioner 'may' revoke endorsement.⁹⁹ However, the use of the word 'may' does not necessarily mean that the Commissioner has a discretion about revocation, rather than an obligation.¹⁰⁰ Indeed, the revocation power was not identified as an administrative discretion in the discussion paper, *Review of Discretions in the Income Tax Law*.¹⁰¹ Ultimately, it is a matter of construction.

Due to the meaning of 'may', the starting point is that the provision is discretionary.¹⁰² However, the purpose of the endorsement provisions is also highly relevant, given some uncertainty over the word, as one can test whether a discretion or obligation would be inconsistent with that purpose.¹⁰³ While the purpose is a little difficult to discern, it appears the endorsement requirement was introduced to 'ensure that the

⁹⁸ ATO, *Compliance in Focus 2013-14* (2013) 3; ATO, *Compliance Model* (25 May 2013) <<http://www.ato.gov.au/About-ATO/About-us/How-we-do-things/Compliance-model/>>.

⁹⁹ TAA sch 1 s 426-55(1).

¹⁰⁰ D C Pearce and R S Geddes, *Statutory Interpretation in Australia* (LexisNexis Butterworths, 7th ed, 2011) 346 [11.1], 350 [11.7].

¹⁰¹ The Treasury (Cth), 'Review of Discretions in the Income Tax Law' (Discussion Paper, June 2007).

¹⁰² Pearce and Geddes, above n 100, 349 [11.5], 354-5 [11.13]; *Acts Interpretation Act 1901* (Cth) s 33(2A) (Pearce and Geddes note at 354-5 that s 33(2A), which appears to entrench a discretionary interpretation of the word 'may', is subject to a contrary intention and so has been relatively narrowly interpreted).

¹⁰³ *Ibid* 347-8 [11.3]. See also *Julius v Lord Bishop of Oxford* (1880) 5 App Cas 214, 222-3 (Earl Cairns LC).

taxation concessions provided to charities are not abused'¹⁰⁴ and to 'protect the integrity of the taxation system in respect of deductible gift recipients and income tax exempt charities'.¹⁰⁵ The very existence of an endorsement requirement in a self-assessment system also supports such a purpose.

Further, in terms of context,¹⁰⁶ the endorsement provisions also provide for the fact of endorsement to be made available to the public by way of the Australian Business Register¹⁰⁷ which has the associated purpose of 'allow[ing] greater scrutiny of the use of taxation concessions by charities ... and improv[ing] public confidence in the provision of taxation support to the charitable sector'.¹⁰⁸ While not entirely clear, it is possible to construe the revocation provision as discretionary, even in light of these purposes, if the width of the discretion is narrowed by the integrity and public confidence concerns. For instance, this might permit some flexibility in situations where charity controllers have made an honest mistake or where the failure to meet endorsement conditions is very minor. Similar flexibility may not be available in the case of dishonest actions.

In any event, seeking to apply s 426-55(1) of the *TAA* so as to take account of a range of mitigating factors which are not expressed in the legislation raises the risk that the Commissioner of Taxation is acting outside power or taking irrelevant

¹⁰⁴ In particular, through the use of commercial activities: Explanatory Memorandum, Tax Laws Amendment (2004 Measures No 1) Bill 2004 (Cth) 77 [10.3] referring to Peter Costello, Treasurer (Cth), 'Government Response to Charities Definition Inquiry' (Press Release, No 49, 29 August 2002).

¹⁰⁵ Explanatory Memorandum, A New Tax System (Tax Administration) Bill 1999 (Cth) 106 [6.7].

¹⁰⁶ See, eg, Pearce and Geddes, above n 100, 353-4 [11.12].

¹⁰⁷ *TAA* sch 1 sub-div 426-C.

¹⁰⁸ Explanatory Memorandum, Tax Laws Amendment (2004 Measures No 1) Bill 2004 (Cth) 77 [10.4].

TAX ENDORSEMENT AND THE ACNC

considerations into account, or that the decision could otherwise be subject to challenge on administrative law grounds.¹⁰⁹

4. REGULATORY CROSSOVER

This Part identifies that the income tax endorsement conditions apply in addition to the ACNC registration requirements and that each set of conditions is separately administered by the Commissioner of Taxation and the ACNC Commissioner, respectively. Further, it compares the scope of the obligations monitored by each of the Commissioners, and considers whether there is likely to be a difference in outcomes where regulatory duplication exists. Finally, this Part examines whether the potential for different enforcement outcomes and the uncertainty over the Commissioner of Taxation's enforcement options might be justified by reference to the regulatory goals of the duplicated provisions.

4.1 Tax Endorsement Conditions Overlay ACNC Registration Requirements

It is the Commissioner of Taxation, not the ACNC Commissioner, who determines and monitors the income tax exempt endorsement of entities.¹¹⁰ However, the ACNC Commissioner determines and monitors a necessary condition for income tax exempt charities: registered charity status.

¹⁰⁹ See, eg, Bruce Quigley, Second Commissioner (Law), 'The Commissioner's General Powers of Administration: How Far Can He Go?' (Paper presented at the 24th Tax Institute of Australia National Convention: Bright Lights – Big City, Sydney, 12 March 2009); *Giris v FCT* (1969) 119 CLR 365, 374 (Barwick CJ), 384 (Windeyer J); W B Lane and Simon Young, *Administrative Law in Australia* (Lawbook, 2007) 143-50, 180-94.

¹¹⁰ *ITAA97* ss 50-52(1), 50-105; *TAA* sch 1 div 426; ACNC, *ACNC and Other Regulators* (2012) <http://www.acnc.gov.au/ACNC/About_ACNC/ACNC_role/ACNC_regulators/ACNC/Edu/ACNC_regulators.aspx>. Historically, the Commissioner of Taxation determined charitable status for entities seeking tax concessions: ACNC Revised Explanatory Memorandum 9 [1.20].

Unsurprisingly then, several commentators have expressed concern about the potential for cross-over between the regulatory role of the ACNC and other federal and state and territory regulators, including the ATO.¹¹¹ As noted by MacDonald and Duggan, the worry is that an uncoordinated approach where multiple regulators have a role, may result in an increased ‘compliance burden’, lessening support for the sector, but without any countervailing increase in public trust and confidence.¹¹² Similarly, duplicative regulation will not necessarily improve tax system integrity. The Productivity Commission, while acknowledging that the Commissioner of Taxation may still have a role to play in relation to tax requirements, has also highlighted the critical nature of a ‘consolidated regulatory framework’ to reduce confusion and the regulatory ‘burden’ for the NFP sector.¹¹³

At a more fundamental level, the problem with permitting the Commissioner of Taxation and the ACNC Commissioner to respond in a broadly overlapping range of circumstances is that the Commissioner of Taxation’s overarching regulatory goal is to safeguard tax revenue, which is potentially inconsistent with a goal of supporting charities and their activities. Chia, Harding, O’Connell and Stewart make a similar point in the context of the ACNC being housed within the ATO as a separate statutory office.¹¹⁴ Moreover, perceptions of a conflict of interest are likely to be just as relevant to achieving support for the sector, given the need for an independent regulator was a principle strongly supported by most participants in the consultation

¹¹¹ Nathan MacDonald and Phoebe Duggan, ‘Not-for-profit Organisations to Finally Have Dedicated Regulator (2011) 63 *Keeping Good Companies* 264, 264; Kylie Maxwell, ‘Reducing Red Tape: A New Regulator for the Charities Sector’ (2012) 26 *Commercial Law Quarterly* 7, 9.

¹¹² MacDonald and Duggan, above n 111, 264.

¹¹³ Productivity Commission, above n 7, XXXIII, XXXVI, XLIII-XLIV, 113-14, 144-5, 152.

¹¹⁴ Not-for-Profit Project Tax Group, *Regulating the Not-for-profit Sector*, above n 6, 15.

TAX ENDORSEMENT AND THE ACNC

process leading up to the formation of the ACNC,¹¹⁵ in part due to such a ‘perceived conflict of interest’.¹¹⁶

Given the nascent nature of the ACNC, it is not yet clear how significant a concern the regulatory overlap poses. However, as explained in Parts 4.2 and 4.3, there is a structural risk with the regulatory scheme for charities as the Commissioner of Taxation’s revocation power has the potential to stymie the aim of achieving proportional supervision of charities. Further, as discussed in Part 4.4, the uncertainty inherent in the Commissioner of Taxation’s available or preferred enforcement measures and the extent of coordination with the ACNC Commissioner also creates a structural detriment for charities and could work to reinforce conflict of interest perceptions. Part 4.5 evaluates whether these structural risks are justified by reference to the regulatory goals of the relevant tax and ACNC provisions.

4.2 Scope Comparison – Circumstances for Enforcement

As a result of the *TLA 2013 Measures No 2 Act*, there will be a material duplication of the matters considered by the two Commissioners. If the further conditions proposed by the Special Conditions Bill are also introduced, the duplication will be exacerbated. The following table summarises the overlap.

¹¹⁵ Parliamentary Joint Committee on Corporations and Financial Services, Parliament of Australia, *Inquiry into the Australian Charities and Not-for-profits Commission Bill 2012; the Australian Charities and Not-for-profits Commission (Consequential and Transitional) Bill 2012; and the Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012* (2012) 32 [2.90]-[2.91].

¹¹⁶ The Treasury (Cth), ‘Scoping Study for a National Not-for-profit Regulator’ (Final Report, April 2011) 66. See also Productivity Commission, above n 7, 144 (citing submission received from Australian Women’s Health Network). See also Not-for-Profit Project Tax Group, *Regulating the Not-for-profit Sector*, above n 6, 15.

Table: Regulatory Overlap from *TLA 2013 Measures No 2 Act* Reforms and Potential Reforms in the Special Conditions Bill

Tax Endorsement Conditions (ATO)	Overlapping ACNC Requirements	Comment
Must apply its income and assets solely for the purpose for which the entity was established.	Must maintain its status as a charity (deregistration power applies); or notify the ACNC Commissioner of a significant contravention of ACNC obligations which has caused the entity to stop being a charity (failure to notify enlivens the range of enforcement powers).	If a charitable institution engaged in conduct such as that in <i>Commissioner of Taxation v Bargwanna</i> ¹¹⁷ of applying approximately 50 per cent of the charity's assets in an income year to a purpose other than the institution's charitable purpose, this would likely breach the tax endorsement requirements as well as bring the institution's charity status into question. ¹¹⁸ However, not all misapplications of assets will result in the entity ceasing to be a charity, ¹¹⁹ so there may

¹¹⁷ (2012) 244 CLR 655.

¹¹⁸ As to charity status, see above n 80. See also *Brookton Co-operative Society Ltd v FCT* (1981) 147 CLR 441, 451 (Mason J): the 'purpose for which a company is established may change in the course of time'.

¹¹⁹ See, eg, Ian Murray, 'Charity Means Business: *Commissioner of Taxation v Word Investments Ltd*' (2009) 31 *Sydney Law Review* 309, 321; Explanatory

TAX ENDORSEMENT AND THE ACNC

	<p>See also ACNC governance standards below, to the extent they relate to acting in accordance with charity status (enlivens the range of enforcement powers).</p>	<p>not be overlap with the ACNC charity status obligations.</p> <p>However, the ACNC governance standards are likely to require on-going administration in accordance with core rules, such as the use of funds for charitable purposes (see below). This would generate overlap.</p>
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<p>Must comply with substantive requirements in governing rules.</p>	<p>Must comply with ACNC governance standards (enlivens the range of enforcement powers).</p>	<p>There is extensive duplication between the two sets of requirements, although the breadth of the ACNC governance standards (eg accountability to members and compliance with Australian laws, amongst others)¹²⁰ means that the ACNC governance standards are likely to be wider in many respects.</p> <p>The governance standards are focussed on the systems that an entity has in place to govern its operations so as to reduce maladministration and to enable it to carry out its purposes. Governance standard 1 would require a registered charity to comply with its charitable purposes and its not-for-profit character on an on-going basis.¹²¹ Similarly,</p>
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¹²⁰ ACNC Regulations sub-div 45-B.

¹²¹ Ibid.

TAX ENDORSEMENT AND THE ACNC

		‘substantive requirements’ in governing rules appear to be interpreted broadly for tax endorsement purposes ¹²² and look to ‘rules of core importance to the operation of [an] entity’ such as ‘those related to an entity’s object and purpose’ and its ‘not-for-profit status’. ¹²³
Must comply with one of the ‘in Australia’, ‘deductible gift recipient’ or ‘prescribed by law’ tests. The focus of these tests is on determining whether a charity has a sufficient geographic link with Australia or whether alternative	Must comply with ACNC external conduct standards (enlivens the range of enforcement powers). The focus of these standards is to be on whether funds are used for ‘legitimate purposes’ and reach ‘legitimate beneficiaries’ rather than supporting terrorist or	Although the ACNC external conduct standards have not been finalised, it appears likely that there will be some overlap between requirements relating to activities or the provision of funds outside Australia and a test which focuses on whether an entity operates and pursues its purposes principally in Australia.

¹²² The Explanatory Memorandum suggests that they do not include ‘minor procedural irregularities’; Explanatory Memorandum, Tax Laws Amendment (2013 Measures No 2) Bill 2013 (Cth) 224-5 [11.61] [1.99].

¹²³ See above n 81; Explanatory Memorandum, Tax Laws Amendment (2013 Measures No 2) Bill 2013 (Cth) 225 [11.62].

<p>reasons and conditions exist for income tax exemption in the absence of such a link.</p>	<p>criminal activities.¹²⁴</p>	<p>However, to the extent it can be predicted in the absence of the standards, it appears the foci of the two requirements are quite disparate, so the degree of overlap may be small.</p>
<p><i>Potential reform under the Special Conditions Bill.</i></p> <p>Must be and maintain its status as a not-for-profit entity as defined under the Special Conditions Bill.</p>	<p>Must maintain its status as a not-for-profit entity (deregistration power applies); or notify the ACNC Commissioner of a significant contravention of ACNC obligations which has caused the entity to stop being not-for-profit (failure to notify enlivens the range of enforcement powers).</p>	<p>Although the term ‘not-for-profit entity’ is not defined in the <i>ACNC Act</i>, but will be defined under the Special Conditions Bill, it is likely to have largely similar content.¹²⁵</p>

¹²⁴ *ACNC Act* s 50-5(1).

¹²⁵ See, eg, above n 7; Explanatory Memorandum, Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 (Cth) 25 [1.106].

TAX ENDORSEMENT AND THE ACNC

	See also ACNC governance standards above, to the extent they relate to maintenance of not-for-profit status (enlivens the range of enforcement powers).	
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A rider to the intersecting circumstances set out above is that the ACNC Commissioner may use the ACNC enforcement provisions *before* a registered entity has breached its obligations. As noted in Part 2.3, the test for the majority of enforcement actions is whether a reasonable person (in the position of the ACNC Commissioner) would believe that ‘it is more likely than not that the registered entity will contravene [its obligations]’.¹²⁶ This could provide the ACNC Commissioner with exclusive space to undertake regulatory action and, for instance, would allow a milder, preventative, enforcement response.

However, there is some ambiguity about the extent of this additional scope. Unfortunately, it is not assisted by the main examples provided in the ACNC Revised Explanatory Memorandum. A likely contravention due to illness on the part of controllers seems a genuine broadening of the circumstances

¹²⁶ *ACNC Act* ss 35-10(1)(c), 80-5(1), 85-5(1), 100-5(1), 100-10(1), 100-15(1). The test for an injunction requires consideration of whether a person is ‘proposing to engage’ in contravening conduct or ‘proposing to refuse or fail... to do a thing’ where that refusal or failure would be a contravention: *ACNC Act* ss 95-15(1)-(2), 95-20. Further, there is no such test that must be satisfied before the Commissioner can accept an enforceable undertaking: *ACNC Act* ss 90-10(1)-(2).

in which the ACNC Commissioner might act.¹²⁷ However, the key illustrations in the ACNC Revised Explanatory Memorandum refer to the test being satisfied where a charity enters into a contract to transfer assets in breach of its charitable purposes, if the ACNC Commissioner acts before the contract is completed.¹²⁸ It is likely that entry into the contract would itself amount to a breach of the governance standards (that the entity ‘comply with its purposes and its character as a not-for-profit entity’).¹²⁹ That is because it is difficult to see how the act of entering into the contract would be ‘to act in accordance with’,¹³⁰ the entity’s purposes or, if the contract is for the transfer of assets to members, the required not-for-profit provisions in the governing rules of the entity. For similar reasons, entry into such a contract is also likely to be a breach of the proposed ‘compliance with substantive requirements in governing rules’ tax endorsement condition, so that the Commissioner of Taxation could also act.¹³¹

4.3 Enforcement Outcomes

As identified in Parts 4.1 and 4.2, the ACNC Commissioner and Commissioner of Taxation may be separately required to respond to the same set of compliance circumstances for an endorsed charity, especially due to the endorsement conditions introduced by the *TLA 2013 Measures No 2 Act*. Given the ACNC Commissioner’s greater range of enforcement powers and increased ability to consider a variety of matters,¹³² including the possibility of less intrusive regulatory action, in

¹²⁷ ACNC Revised Explanatory Memorandum 122-3 [9.43] (although the Commissioner may choose not to act where the illness is likely to cause only a temporary delay in complying with obligations).

¹²⁸ ACNC Revised Explanatory Memorandum 41 [3.93]; 122 [9.42].

¹²⁹ *ACNC Regulations* s 45.5(2)(c).

¹³⁰ Susan Butler (ed), *Macquarie Dictionary Online* (Macquarie Dictionary Publishers Pty Ltd, 2013) (‘comply with’).

¹³¹ On the basis that the substantive requirements include rules setting out the entity’s purpose; see above n 81 and accompanying text.

¹³² In fact, the ACNC Commissioner is required to do so.

TAX ENDORSEMENT AND THE ACNC

selecting the appropriate power the potential exists that the Commissioners may employ different enforcement options. As explored in Parts 2.2 and 2.3, it may be expected that the ACNC Commissioner will adopt enforcement action which is tailored to the risk involved and the severity of the breach. This approach is not directly open to the Commissioner of Taxation, whose enforcement powers are less diverse.

Bargwanna provides a useful case study.¹³³ The reason the case remains relevant, despite amendment of the ‘applied for the purposes for which it was established’ tax endorsement provision on which it was based, is that the revised special conditions contained in the *TLA 2013 Measures No 2 Act* are apparently intended to be consistent with the High Court’s interpretation of that provision.¹³⁴ The Court’s approach in *Bargwanna* leaves open the question whether honesty or corrective action on the part of charity controllers are relevant factors for the Commissioner of Taxation to consider for tax endorsement purposes. Heydon J expressly left this issue at large and the plurality judgment did not specifically address corrective action, though their Honours did note that having acted ‘honestly and reasonably’ under the relevant trustee legislation would be insufficient in relation to breaches of the type considered in the case.¹³⁵

The decision suggests that there may be a relatively broad range of circumstances where loss of entitlement to endorsement would be engendered by failure to meet the ‘compliance with

¹³³ For a discussion of the case, see, eg, Dianne Sisak, ‘Trustee Obligations for the Due Administration of Charitable Trust Funds’ 46(11) *Taxation in Australia* 525.

¹³⁴ Explanatory Memorandum, Tax Laws Amendment (2013 Measures No 2) Bill 2013 (Cth) 225 [11.64].

¹³⁵ *Bargwanna* (2012) 244 CLR 655, 669 [41]-[42] (French CJ, Gummow, Hayne and Crennan JJ), 673 [62] (Heydon J). The plurality judgment did not comment on whether the trustees had actually acted honestly and reasonably for the purposes of exculpation under trustee legislation.

governing rules’ and ‘application of income and assets’ conditions contained in the *TLA 2013 Measures No 2 Act*. *Bargwanna* involved several breaches of trust relating to the administration of a charitable fund, with the issue being whether the breaches meant that the charitable fund had not been ‘applied for the purposes for which it was established’. This requirement has been removed as part of the ACNC reforms, but the reasoning in the case remains relevant to the *TLA 2013 Measures No 2 Act* changes.

The key breaches of trust spanned a number of income years and constituted:

- Mixing relatively significant amounts¹³⁶ of trust funds with non-trust funds, coupled with a failure to obtain interest on those trust funds.¹³⁷ An amount in compensation was apparently added to the trust fund in a later income year.¹³⁸
- Transferring an amount of AUD 210,000, representing just under 50 per cent of the trust funds at the relevant time, into a personal mortgage offset account of the trustees so as to reduce the interest paid by the trustees on their personal home loan.¹³⁹ The principal amount was subsequently largely refunded to the trust, along with an amount in respect of interest foregone.¹⁴⁰

The High Court found that the breaches resulted in the trust being ineligible for endorsement in the relevant income years and the reasoning suggests that, unless a *de minimis*

¹³⁶ Minor amounts in the income years ending in 2002 to 2005. Thereafter, 10 per cent, 20 per cent and 25 per cent, respectively, of the trust’s total funds.

¹³⁷ *Bargwanna* (2012) 244 CLR 655, 661-2 [10], 670 [45] (French CJ, Gummow, Hayne and Crennan JJ).

¹³⁸ *FCT v Bargwanna* (2009) 72 ATR 963, 973 [33] (Edmonds J).

¹³⁹ *Bargwanna* (2012) 244 CLR 655, 661-2 [10], 670 [45] (French CJ, Gummow, Hayne and Crennan JJ).

¹⁴⁰ *Bargwanna* (2012) 244 CLR 655, 663-4 [18] (French CJ, Gummow, Hayne and Crennan JJ).

TAX ENDORSEMENT AND THE ACNC

misapplication,¹⁴¹ a charitable fund would not continue to qualify for endorsement under the old test where:

- a breach of trust has occurred which results in trust funds being used for a purpose other than the charitable purposes of the charity;¹⁴²
- there has been a mixing of trust funds with other funds;¹⁴³ or
- the trustee has not administered the trust in accordance with the trust deed or the law such that it cannot be said that the administration of the trust is ‘referable’ to achieving its charitable purposes; for instance, where ‘benefits are derived personally by the trustees or a third party’.¹⁴⁴

On one view of the evidence, the charity controllers did not ‘deliberately’ misapply trust funds,¹⁴⁵ but nevertheless caused the charity to breach its governing rules by misapplying funds for non-charitable purposes which resulted in a personal benefit to the controllers. The controllers also applied funds other than

¹⁴¹ *Bargwanna* (2012) 244 CLR 655, 669 [41]-[42] (French CJ, Gummow, Hayne and Crennan JJ), 673 [62] (Cf Heydon J). The term was not expanded upon. However, it seems clear that it does not apply where a ‘significant part of the assets’ of the trust have been misapplied, or where the trust fund has been ‘substantially applied’ or ‘on the whole applied’: 669 [39], 669 [42], 669-70 [44]. (French CJ, Gummow, Hayne and Crennan JJ).

¹⁴² *Bargwanna* (2012) 244 CLR 655, 669 [39], 669 [41]-[42], 670 [45] (French CJ, Gummow, Hayne and Crennan JJ).

¹⁴³ *Bargwanna* (2012) 244 CLR 655, 669 [40]-[42], 670 [45] (French CJ, Gummow, Hayne and Crennan JJ).

¹⁴⁴ *Bargwanna* (2012) 244 CLR 655, 669 [41]-[42], 670 [45] (French CJ, Gummow, Hayne and Crennan JJ).

¹⁴⁵ The Commissioner of Taxation seems to have accepted that the charity controllers did not ‘deliberately’ misapply the relevant funds: *Bargwanna* (2012) 244 CLR 655, 673-4 [63] (Heydon J); *Bargwanna v FCT* (2010) 191 FCR 184, 209[68], 211 [75] (Dowsett, Kenny and Middleton JJ). See also the Administrative Appeal Tribunal’s acceptance of good faith reasons for the breaches of trust: *Re TACT and FCT* (2008) 71 ATR 827, 844-56 [56]-[105] (Senior Member Taylor). At first instance, Edmonds J appears to have accepted that the controllers acted carelessly: *FCT v Bargwanna* (2009) 72 ATR 963, 973 [32].

for charitable purposes by mixing the charity's funds with the money of others and failing to obtain interest. Given the multiple breaches of fiduciary duties over a number of years, Turnour and McGregor-Lowndes' description of the circumstances as involving 'significant maladministration' seems apt.¹⁴⁶ Accordingly, this would be a failure to meet the 'compliance with governing rules' or 'application of income and assets' conditions imposed as a result of the *TLA 2013 Measures No 2 Act*, which would permit revocation of endorsement.

However, indirectly, via a related party, the charity controllers attempted to rectify the breaches to the extent possible by repaying misapplied amounts, plus compensation. In addition, in *Bargwanna*, over the relevant years, the charity had distributed somewhere between 25 to 40 per cent of the funds it received or generated to other charities.¹⁴⁷ Nevertheless, the decision in *Bargwanna* demonstrates that revocation is available to the Commissioner of Taxation and may well be applied.

In contrast, despite the level of breaches involved, the ACNC Commissioner may well not deregister the charity. The *ACNC Act* encourages 'self-correction' by registered NFPs.¹⁴⁸ Further, example 9.6 from the ACNC Revised Explanatory Memorandum suggests that where there is no suggestion of dishonesty, self-correction, following informal notification from

¹⁴⁶ Turnour and McGregor-Lowndes describe the case as involving a trust 'substantially administered in accordance with the terms of the trust' but also involving 'significant maladministration': Turnour and McGregor-Lowndes, above n 57, 76.

¹⁴⁷ It appears that between 2002 and 2007 the charitable trust received, or generated as income, AUD 707,198 (*Bargwanna* (2012) 244 CLR 655, 663 [17] (French CJ, Gummow, Hayne and Crennan JJ)) and distributed somewhere between AUD 176,821 and AUD 293,915 to charities (HELP International, several churches and retired ministers of religion) (*Re TACT and FCT* (2008) 71 ATR 827, 836-7 [32]-[34], 844 [54]-[55] (Senior Member Taylor)).

¹⁴⁸ ACNC Revised Explanatory Memorandum 128 [9.76]; *ACNC Act* s 35-10(2)(b). See also ACNC Revised Explanatory Memorandum 126 [9.60].

TAX ENDORSEMENT AND THE ACNC

the ACNC Commissioner that an entity is using its funds for a purpose not permitted by its rules, albeit charitable, may mean no formal enforcement action is necessary.¹⁴⁹ Admittedly, example 9.6 relates to an isolated incident and *Bargwanna* concerns breaches over a number of years and in respect of a significant portion of the charity's funds, which is a relevant factor for the ACNC Commissioner.¹⁵⁰ Yet, example 3.8 indicates that even in cases of fraud, the ACNC Commissioner may still attempt to use lesser enforcement measures before moving to deregistration.¹⁵¹

4.4 Inherent Uncertainty for Charities

The legislative package creating the ACNC does explicitly provide for a level of coordination between the ACNC Commissioner and the Commissioner of Taxation. For instance, cooperation will be assisted by the information disclosure provisions introduced with the creation of the ACNC. ACNC officers are permitted to disclose information about registered entities to the ATO¹⁵² if the information would 'enable or assist the [ATO] to perform or exercise any of the functions or powers of the [ATO]', the disclosure is for that purpose and is also 'reasonably necessary to promote the objects of [the *ACNC Act*]'.¹⁵³ Likewise, the Commissioner of Taxation or another taxation officer may now disclose information to the ACNC Commissioner where this is 'for the purpose of administering the [*ACNC Act*]' or where it relates to the failure of a charity to comply with a law and is made for 'the purpose of the

¹⁴⁹ ACNC Revised Explanatory Memorandum 128 [9.76].

¹⁵⁰ *ACNC Act* s 35-10(2)(a).

¹⁵¹ ACNC Revised Explanatory Memorandum 40-1 [3.87]. Example 3.13 does not seem pertinent as the personal benefits were obtained without deliberate misapplication of funds in *Bargwanna*; at 46-7 [3.120].

¹⁵² Disclosure is permitted to an 'Australian government agency' which includes 'an authority of the Commonwealth' and so would apply to the ATO; *ACNC Act* s 300-5 (definition of 'Australian government agency'). See, eg, ACNC Revised Explanatory Memorandum 182 [11.30].

¹⁵³ *ACNC Act* s 150-40.

administration of a law governing trusts and charities'.¹⁵⁴ Accordingly, it is to be expected that the ACNC Commissioner and the Commissioner of Taxation will keep each other informed of their respective regulatory actions and of instances where charities have breached obligations.¹⁵⁵

Further, the ACNC has taken the administrative step of providing a joint application form to charities, which it will process for registration purposes and then pass on to the ATO to consider for tax endorsement.¹⁵⁶ The ACNC Commissioner and the Commissioner of Taxation have also entered into a Memorandum of Understanding which is intended to set out an overarching framework for entry into 'Subsidiary Arrangements' for the provision of 'services', 'exchanges of information', or 'other activities'.¹⁵⁷ The Memorandum also contains high level administrative, operative, data-exchange, activity and payment provisions. However, the only provision of direct relevance to coordinated regulation is the mutual assistance clause which provides that '[t]he parties will be open, honest, cooperative and responsive to each other, respecting each other's functions and roles, and providing each other with positive assistance whenever possible'.¹⁵⁸

¹⁵⁴ *Consequential and Transitional Act* sch 3 items 15, 16.

¹⁵⁵ Provision has also been made for the joint consideration of administrative review of, or court appeal from, objection decisions of the ACNC Commissioner or Commissioner of Taxation; *ACNC Act* ss 165-55, 170-30; *Ibid* sch 3 items 3-14.

¹⁵⁶ *ACNC, ACNC and Other Regulators*, above n 110.

¹⁵⁷ Memorandum of Understanding between the Commissioner of Taxation and the Commissioner Australian Charities and Not-for-profits Commission, 12 December 2012, cl 2.

¹⁵⁸ *Ibid* sch cl c7. The intent of this 'aspirational' goal is reflected in the ACNC Revised Explanatory Memorandum, which states that 'administrative decisions of the Commissioner of Taxation and the ACNC will in practice be interlinked and jointly considered'; ACNC Revised Explanatory Memorandum 262 [15.56].

TAX ENDORSEMENT AND THE ACNC

Nevertheless, the two regulators have separate and on-going roles to fulfill in relation to charities seeking income tax exemption. The amendments introduced as part of the ACNC legislative package certainly do not provide for the referral of matters from one regulator to the other such that the first regulator can decline to act. As noted by Baldwin and Cave, ‘coordinating regulation’ is not easy, even with goodwill, and there are likely to be a number of factors which undermine the translation of the intent into practice.¹⁵⁹ For instance, reluctance to accept ‘new procedures’ (particularly on the part of the ATO as an existing regulator with established practices), opposition to a ‘transfer of powers’ from the ATO to the ACNC, attachment to ‘regulatory traditions’ and problems measuring regulatory ‘rigour’ or ‘equivalence’ in enforcement.¹⁶⁰

Of themselves, these factors generate uncertainty for charities about the manner in which coordinated enforcement will be undertaken. More fundamentally, however, it does not seem best practice that the principles underlying any such coordinated response have not, to the author’s knowledge, been made public. The release of the Memorandum of Understanding is to be welcomed, along with the ACNC’s commitment to disclosing ‘Subsidiary Arrangement’ memoranda with the Commissioner of Taxation.¹⁶¹ Nevertheless, the reference in the Memorandum to the goal of ‘mutual assistance’ is very general. It is too general to amount to a meaningful statement of the principles underlying a coordinated ACNC and ATO regulatory response which could be used by charities for guidance.

Further, as discussed in Part 3.2 above, the Commissioner of Taxation may not have any discretion over whether to revoke a

¹⁵⁹ Robert Baldwin and Martin Cave, *Understanding Regulation: Theory, Strategy and Practice* (Oxford University Press, 1999) 187.

¹⁶⁰ *Ibid* 187-188.

¹⁶¹ ACNC, *Memoranda of Understanding* (2012)

<<http://www.acnc.gov.au/ACNC/Pblctns/Pol/MOU/ACNC/Publications/MOU.aspx?hkey=6dc20099-799a-4d17-b3bd-0921d6f10c50>>.

charity's endorsement if it ceases to meet the requirements. This would obviously render a coordinated approach far more difficult to achieve. Even if the Commissioner of Taxation does have a discretion, it is unlikely to permit the Commissioner of Taxation to take account of the range of matters considered by the ACNC Commissioner, or to accord too much weight to the ACNC Commissioner's proposed regulatory response. Again, both these factors intensify uncertainty for charities about the extent and manner of coordinated enforcement.

4.5 Evaluation

As discussed in Parts 4.2 and 4.3, due to the enactment of the *TLA 2013 Measures No 2 Act*, the structure of the regulatory regime for charities enables both the ACNC Commissioner and the Commissioner of Taxation to respond to the same circumstances in a broad range of situations. This is an overlap that would potentially be increased if the Special Conditions Bill is reintroduced into Parliament. As the Commissioner of Taxation has a relatively restricted range of enforcement options, this structure poses an inherent risk to the achievement of proportionate regulatory action. Further, Part 4.4 demonstrates that the new regulatory regime creates a level of uncertainty for charities about the way in which coordinated enforcement will occur (if at all).

Are the risks worth bearing? This paper seeks to answer the question by reference to the regulatory goals of the *ACNC Act* and the income tax endorsement provisions. As enunciated in Part 3.2, the endorsement requirements appear to have been introduced to prevent abuse of tax concessions and to 'protect the integrity of the taxation system in respect of ... income tax exempt charities', as well as to shore up public confidence in the granting of tax benefits to charities.¹⁶² By reason of the *ACNC Act* objects discussed in Part 2, the goals to be achieved by use of the ACNC Commissioner's enforcement powers are:

¹⁶² See above nn 104-107.

TAX ENDORSEMENT AND THE ACNC

furthering ‘public trust and confidence’ in charities, ‘support[ing] and sustain[ing]’ the charitable sector, and championing a decrease in ‘unnecessary regulatory obligations’.¹⁶³ While the ACNC Commissioner is generally required, when exercising enforcement authority, to consider the objects of the income tax legislation, since it refers to registration under the *ACNC Act*,¹⁶⁴ this is not an overarching goal and is only one of several relevant matters.

The need for revenue protection for tax purposes as compared with the broader focus of the ACNC regulatory goals suggests that different enforcement responses may be appropriate in some circumstances. Indeed, stricter measures on the part of the Commissioner of Taxation may be warranted by the fact that the endorsement provisions are intended to apply on top of the ACNC registration requirements. However, for many charities, a key reason for applying for ACNC registration is to access tax concessions.¹⁶⁵ Accordingly, loss of income tax exemption, which could occur through revocation of endorsement by the Commissioner of Taxation or from

¹⁶³ *ACNC Act* s 15-5(1); *ACNC’s Role* (2012)

<http://www.acnc.gov.au/ACNC/About_ACNC/ACNC_role/ACNC/Edu/ACNC_C_role.aspx?hkey=88635892-3c89-421b-896d-d01add82f4fe>.

¹⁶⁴ See above Part 2.3.

¹⁶⁵ The three most prominent and specific of the reasons to register suggested by the ACNC all relate to tax concessions: ACNC, *Why Register* (2012) <http://www.acnc.gov.au/ACNC/Register_my_charity/Why_register/ACNC/Edu/Why_reg.aspx?hkey=f1345f59-0774-41b7-82ff-833fe79ed207>. See also, ACNC Revised Explanatory Memorandum 29 [3.2], 30 [3.10]. In addition, registration may result in exemption from a range of Commonwealth legislation, including in relation to unsolicited communications and discrimination; enables the dissemination of information about a charity via the public register maintained by the ACNC Commissioner; and building trust in members of the public that the entity’s charitable status has been vetted: ACNC, *Why Register*. In terms of building trust, the author notes that donors will be key members of the public that charities might seek registration to reassure. Registration with the ACNC also offers the potential, though not the certainty, of reduced reporting requirements across government agencies, for some charities; ACNC, *Why Register*.

deregistration by the ACNC Commissioner, may be the ultimate sanction for many charities. If the Commissioner of Taxation wields this sanction in circumstances where the ACNC Commissioner considers a milder regulatory response is desirable, the benefits of a proportionate compliance response will not be achieved.

If the ACNC Commissioner can tailor a regulatory response to be ‘commensurate to the circumstances addressed’,¹⁶⁶ the risk of a more extreme response, or even the perceived potential of a different response, by the Commissioner of Taxation detracts from the goal of supporting and sustaining the charity sector, since a more extreme response would not be ‘commensurate’ and so would impose too high a cost for the relevant charity. As noted in Part 3.2, the Commissioner of Taxation may not have any discretion about revocation of endorsement, which would mandate a disproportionate response. Further, if not ‘commensurate’, nor would the response provide any additional integrity, or public trust and confidence, benefits, unless the particular tax system integrity concern was somehow separate to that of public confidence.

In addition, the ACNC Commissioner’s role is to determine whether an entity is, and continues to act in accordance with its status as, a charity and this determination and monitoring function was intended to replace duplicative determinations on the same matters by other federal regulators.¹⁶⁷ That is surely the reason why the income tax endorsement requirements now refer to a registered charity under the *ACNC Act* – they are intended to impose *additional* requirements. Accordingly, the risk of different enforcement approaches to the same core issue adds to, rather than reducing, ‘unnecessary regulatory obligations’. If there are additional tax system integrity concerns, then the goal of reducing duplication suggests that they should be more

¹⁶⁶ See above n 55.

¹⁶⁷ See, eg, ACNC Revised Explanatory Memorandum 257-8 [15.17]-[15.21].

TAX ENDORSEMENT AND THE ACNC

specifically identified, so as to maximise regulatory obligations only to the extent necessary. While not the focus of this paper, generally applicable regulatory design principles also indicate that the regulation should be the ‘minimum necessary to achieve objectives’.¹⁶⁸

In terms of the uncertainty generated for charities, ambiguity about what enforcement measures the Commissioner of Taxation is permitted to take and, to the extent permitted, might choose to take in coordination with the ACNC Commissioner, is likely to increase compliance costs. It may also exacerbate a perceived conflict of interest on the part of the ATO. Accordingly, this would lessen support for charities and would increase the perceived level or complexity of regulatory obligations, again without improving tax system integrity or public trust and confidence in the charitable sector. It is also inconsistent with regulatory design principles that regulation be ‘accessible, transparent and accountable’ (which includes that the rules be ‘available’ and able to be understood) and ‘integrated and consistent with other laws’.¹⁶⁹

5. CONCLUSION

Although the ACNC regime is still in its infancy, this paper submits that the potential regulatory overlap with the Commissioner of Taxation over income tax endorsed charities should be clarified due to the risks that it poses. As a result of the *TLA 2013 Measures No 2 Act* changes, the ACNC Commissioner and Commissioner of Taxation are separately

¹⁶⁸ As to the principles, see, eg, The Allen Consulting Group, *Improving Not-for-profit Law and Regulation: Options Paper* (1 December 2005) <<http://www.allenconsult.com.au/resources/acgnfplawregulation2005.pdf>> 36-37. See also, Not-for-Profit Project Tax Group, *Regulating the Not-for-profit Sector*, above n 6, 6-7.

¹⁶⁹ See, eg, The Allen Consulting Group, above n 168, 36-37. See also, Not-for-Profit Project Tax Group, *Regulating the Not-for-profit Sector*, above n 6, 6-7.

required to respond to the same set of compliance circumstances for endorsed charities in a broad range of situations, potentially with a ‘fierce extreme’ of compliance measures. The situation could be exacerbated if the Special Conditions Bill is reintroduced into Parliament. The risks of potentially divergent enforcement action and of uncertainty about the extent and manner of coordination between the Commissioner of Taxation and the ACNC Commissioner will detract from proportionate regulation of charities and, more fundamentally, from achievement of the regulatory goals of the ACNC. Based on these concerns, the following reform proposals are raised for further investigation.

First, the regulatory overlap could be addressed by returning to the tax endorsement special conditions for charities that were in place immediately before the commencement of the *TLA 2013 Measures No 2 Act* (that is, applying a geographic nexus test), with the *ITAA97* and the Special Conditions Bill amended to implement only those special condition changes relevant to this nexus test. Of course, the additional endorsement requirements would be relevant for non-charity NFPs which are not currently regulated by the ACNC and should remain to that extent. As demonstrated by Part 4.2, duplication for charities would then primarily be limited to the ACNC external conduct standards and the income tax endorsement geographic nexus test. The different goals of these requirements should then justify separate regulators and separate responses. This approach bears some resemblance to the removal of a number of *Corporations Act 2001* (Cth) governance requirements for charities which are registered with the ACNC, so as to ‘eliminate the need for [ASIC] to continue to regulate [them]’.¹⁷⁰

An approach like this has the benefit that it avoids cutting across the principle that the ACNC Commissioner is the

¹⁷⁰ *Consequential and Transitional Act* sch 3 pt 3; ACNC Revised Explanatory Memorandum 261 [15.49].

TAX ENDORSEMENT AND THE ACNC

independent statutory regulator of charities and, eventually, the broader NFP sector. Its importance would be emphasised if the ACNC's regulatory role moves beyond charities to other NFPs in the future, as is envisaged, because the *TLA 2013 Measures No 2 Act* and potential Special Conditions Bill requirements may then lead to a regulatory overlap applying to a broader range of NFPs than just charities. However, the problem is that it may not sufficiently achieve the revenue integrity goal of the income tax endorsement provisions, since the ACNC Commissioner need only consider this object as one of many factors relevant to the exercise of the ACNC Commissioner's discretion.

Accordingly, a second and preferable alternative for investigation would be to allow the Commissioner of Taxation to retain a broader role in relation to charity regulation, for instance, by including the type of income tax endorsement special conditions contained in the *TLA 2013 Measures No 2 Act* and proposed in the Special Conditions Bill. However, the Commissioner of Taxation's discretion whether or not to revoke endorsement could be confirmed and the Commissioner of Taxation could be obliged to consider any regulatory action or proposed regulatory action of the ACNC Commissioner in exercising the discretion. Arguably, this would bolster a whole of government proportionate and responsive approach to enforcement, while still permitting the Commissioner of Taxation to emphasise revenue protection.

Further, to address concerns about the level of uncertainty for charities and unnecessary regulatory duplication, the Commissioner of Taxation could be compelled to cooperate with the ACNC Commissioner and to publically release the detailed principles upon which such regulatory cooperation would occur. Ideally, the principles would be included with the endorsement administration provisions in the *TAA*, in order to prescribe the appropriate ambit for each commissioner and to ensure that the Commissioner of Taxation's revocation discretion is not exercised inconsistently with the principles.

The second proposal is recommended for further assessment, which would likely be assisted by observation of how the relationship between the ACNC Commissioner and the Commissioner of Taxation develops in practice. Accordingly, it is hoped that the ACNC will release further information on its regulatory coordination with the ATO, including details of the various Subsidiary Arrangements between the two regulators.