Should Tax Incentives for Charitable Giving Stop at Australia’s Borders?

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Abstract

Around the world, philanthropic gifts are increasingly crossing borders, driven by globalisation and facilitated by liberalised cross-border tax incentives. Australia is considered to have one of the strictest regimes for the tax treatment of cross-border donations. With bipartisan political support for a significant reduction in the amount and scope of Australian foreign aid, the nation’s international presence through the ‘soft power’ of aid will fall increasingly upon private philanthropy. Are the current tax incentives for Australian cross-border philanthropy and the supervision of those incentives appropriate to both facilitate and regulate international giving? To address this question, this article analyses the amount of Australian cross-border philanthropy and explains the current legislative architecture affecting the tax deductibility of cross-border gifts. It then examines the Australian Government’s proposed ‘in Australia’ reform agenda against the underlying fiscal and regulatory policy imperatives, and makes recommendations for the future tax treatment of Australian cross-border philanthropy.

I Introduction

The Australian Treasurer’s 2015 tax discussion paper stated that ‘[g]lobalisation provides opportunities for a more prosperous future, but also challenges Australia’s tax system’¹. The challenges presented by globalisation are particularly acute for the tax laws affecting cross-border philanthropy. Significant advances in communications technology, borderless social media, and an increasingly mobile international workforce have converged with deeply integrated global markets² and free-trade zones to usher in an era of philanthropic globalisation.³ In the 20 years

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from 1991 to 2011, cross-border philanthropy from Organisation for Economic Co-operation and Development (‘OECD’) donor countries to the developing world grew from approximately US$5 billion to US$32 billion, with some estimates for 2011 as high as US$59 billion. This dramatic increase in international giving has brought widespread benefits, while at the same time raising fiscal and regulatory concerns for governments around the world. As national boundaries around philanthropy start to blur, the traditional framework for the tax treatment of cross-border donations is being challenged.

Most OECD countries have fiscal incentives to encourage domestic philanthropy, usually by lowering the price of giving through tax incentives such as deductions or credits. These tax incentives are typically characterised as a government subsidy or tax expenditure to promote charitable activities having a public benefit. The extent to which they succeed in encouraging giving depends on how responsive donors are to price incentives, measured by economists as the price elasticity of giving. Studies on domestic giving have shown that these tax incentives can potentially increase the amount donated and the number of individuals donating.

While there have been no studies estimating the price elasticity of cross-border giving, a comparative study of private charitable giving to developing countries conducted by the Center for Global Development concluded that ‘[c]itizens in countries with stronger targeted income tax incentives appear to give more private charity to poor countries’. This finding indicates a high price elasticity for taxpayers who give overseas, highlighting the importance of domestic tax incentives for encouraging individuals to engage in cross-border philanthropy. At the same time, it sheds light on the role of domestic tax policy as an instrument of foreign aid policy, with tax incentives facilitating the delivery of ‘private’ aid to developing countries. In this sense, tax policies that promote cross-border

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11 Ibid.
philanthropy can be considered ‘de facto aid policy’, with private international
giving serving as a complement to (rather than a substitute for) official foreign aid.12

Until recently, most OECD nations had not considered tax incentives for
cross-border philanthropy to the same extent as domestic giving, but this is
changing. A series of decisions by the European Court of Justice has affected the
ability of Member States of the European Union to impose territorial fiscal
restrictions on charitable tax relief.13 As a result, the majority of Member States
now grants the same type of tax relief available for domestic donations to
‘European’ cross-border donations.14 A recent comparative study measuring the
state of philanthropic freedom in 64 countries found that the two countries with the
lowest barriers to cross-border philanthropy were Sweden and the Netherlands.15
Each country has extended its tax relief beyond Europe, applying the same tax
treatment to domestic and cross-border donations. Of the OECD countries included
in the study, Australia was found to have the highest barriers to cross-border
philanthropy.16

Scholars have also located Australia at the restrictive end of the
cross-border charitable tax concession spectrum.17 Australia allows tax deductions
for donations encouraging domestic charitable activities and organisations,
however there is no specific provision for gift deductions to organisations both
located and operating outside Australia. Such organisations could register with the
Australian Taxation Office (‘ATO’) as a Deductible Gift Recipient (‘DGR’), but
unless they fall within one of the limited classes of exceptions, their donors would
not be entitled to claim a tax deduction for gifts.

While it may be possible for an Australian donor to effect a tax-deductible
cross-border gift using an Australian resident organisation as a giving intermediary
(a common workaround in some other jurisdictions),18 this avenue is limited, since
the organisation has to qualify for and maintain income tax exemption and DGR
status. Recent judicial decisions have addressed the use of such workarounds and,
in doing so, have challenged the geographic restrictions on the gift deduction, \(^{19}\) but have yet to be formally acknowledged by the ATO. The Government’s response to these decisions has been to propose a reform agenda that seeks to further limit the ability of Australian donors to obtain a tax deduction for cross-border donations.

This state of affairs is based on two primary policy reasons advanced by the Australian Government. The first questions whether Australian taxpayers should subsidise the provision of public goods for another country’s population to consume, without tangible and measurable benefits for Australia. \(^{20}\) This sentiment was articulated by an Assistant Treasurer when introducing a Bill seeking to tighten the Australian tax laws around cross-border giving, \(^{21}\) noting the ‘longstanding policy of successive governments that DGRs should operate only in Australia, for the benefit of the Australian public’. \(^{22}\) The Bill’s Explanatory Memorandum further elaborated that restrictions were necessary to protect the ‘large amounts of revenue that would otherwise be forgone’, \(^{23}\) although there was no quantification of such revenue loss. The Bills Digest merely referred back to the Tax Expenditures Statement, which provided an estimate of the revenue forgone resulting from deductions to all DGRs, without specifying the portion of the tax expenditure allocated to charitable activities overseas. \(^{24}\) The Explanatory Memorandum also cited a second policy reason for limiting the geographical reach of the gift deduction, which focused on the difficulties of supervising philanthropy outside the jurisdiction, where funds may be channelled into terrorist financing or money laundering, \(^{25}\) or otherwise used as an avenue for tax abusive behaviour. \(^{26}\)

While these oversight issues are particularly acute where funds are channelled overseas through DGRs serving as giving intermediaries, the Explanatory Memorandum did not provide any supporting evidence regarding the extent of the tax abuse risk.

The Government’s policy position has been criticised by Philanthropy Australia, the umbrella association for philanthropic trusts and foundations, in a

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21 Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 (Cth) (‘In Australia Bill’).

22 Commonwealth, Parliamentary Debates, House of Representatives, 23 August 2012, 9728 (David Bradbury, Assistant Treasurer).

23 Explanatory Memorandum, Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 (Cth) 4.

24 Department of Parliamentary Services (Cth), Bills Digest, No 24 of 2012–13, 12 December 2012, 24 (attachment A).


26 Explanatory Memorandum, Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 (Cth) 6 [1.7], 11 [1.49]. See also Federal Commissioner of Taxation v Arnold (No 2) (2015) 324 ALR 59.
letter to the Prime Minister detailing concerns ‘with Australia’s regulatory and taxation framework for international philanthropy, which imposes some of the highest barriers to international philanthropy in the world’. Philanthropy Australia’s letter noted its members’ inability ‘in a time of budget constraint’ to respond to the Government ‘seeking to promote the role of private sector initiatives which support international development’ and specifically encouraged the Government to consider more facilitative taxation provisions in relation to cross-border philanthropy.

At a time when the Australian Government has a policy of significantly reducing foreign aid, the argument for using the tax laws to facilitate private international giving is particularly compelling. The year 2012 marked the end of a bipartisan political commitment to increase Australia’s aid and the then Labor Government announced significant funding cuts from the Australian aid program. In 2014, the new Liberal-National Coalition Government went further, announcing in its first budget that foreign aid would be capped to realise an estimated saving of A$7.6 billion over five years. At the same time, Australia’s stated foreign aid policy goals contracted to focus on the Indian Ocean Asia-Pacific region. In the 2015 budget, foreign aid was cut by a further A$1 billion, with aid to Africa discontinued completely.

Given increased globalisation, domestic fiscal restraint significantly reducing government-funded overseas aid, and the desire of private philanthropy to step into this role, is Australia’s policy framework to both facilitate and regulate cross-border giving appropriate? We tackle this issue by first reviewing the scant evidence on the size and nature of Australian cross-border giving, which informs both the level of call upon the fisc (or public purse) for subsidy, as well as the potential tax abuse risk profile. This is followed by a comprehensive description of Australia’s tax treatment of cross-border donations, to understand the range of options available for Australian donors who seek to engage in tax-effective cross-border philanthropy. We then examine the Government’s proposed reform agenda against the underlying revenue and policing concerns. To conclude, we provide observations on the potential outcomes of the proposed reforms and make recommendations for the future.

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28 Letter from Philanthropy Australia to Prime Minister Tony Abbott, above n 27, 2.


II  How Extensive is Australian Cross-border Philanthropy?

Understanding the current level of cross-border philanthropy in Australia is foundational to any policy analysis of the charitable tax concessions as they apply to international giving and the exposure of the fisc. This was recognised in 1991 by the House of Representatives Standing Committee’s *Follow the Yellow Brick Road* report that, in part, addressed allegations of wealthy Australians using various tax abusive gift deduction schemes involving foreign tax havens. The report noted the lack of data on the cross-border philanthropic tax concessions and specifically recommended that statistics should be kept in order to inform policy development and provide a basis for ATO audit activity. This recommendation has not been implemented. As a result, the amount of charitable giving flowing out of Australia has remained a mystery, as well as how much of this outflow is classified as tax-deductible gifts.

Australian non-profit organisations (also referred to as ‘not-for-profits’) do not generally file tax returns and, as a result, there is no convenient and reliable data source for measuring the amount of the charitable tax concessions. The total measured non-profit tax concessions at all levels of government is approximately A$4 billion, with unmeasured fiscal concessions estimated to be double this amount. The Australian Tax Expenditures Statement does not provide estimates for tax expenditures of many mainstream non-profit concessions, let alone those for cross-border philanthropy.

The annual published ATO statistics do include private and public ancillary funds, which file annual audited financial statements with the ATO. These funds enable Australian taxpayers to make tax-deductible gifts to private and community foundations respectively. Such funds report their distributions by area of allocation, including those made to ‘international affairs’. In the 2012–13 tax year, private ancillary funds distributed A$19.57 million and public ancillary funds distributed A$7.97 million to Australian international affairs DGRs, representing 8% and almost 3%, respectively of total distributions for each of these philanthropic vehicles. While this data provides some indication of cross-border philanthropic flows, it represents 25% of all tax-deductible giving and just 7% of total giving.

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33 House of Representatives Standing Committee on Finance and Public Administration, Parliament of Australia, *Follow the Yellow Brick Road — The Final Report on an Efficiency Audit of the Australian Taxation Office: International Profit Shifting* (1991) (‘*Follow the Yellow Brick Road*’).
34 Ibid 51, 55–6.
35 An exception is private and public ancillary funds, which report to the ATO annually. However, other than a summary, these returns are not made public. See ATO, *Ancillary Fund Returns* (20 July 2015) <https://www.ato.gov.au/non-profit/statements-and-returns/ancillary-fund-returns/>.
39 Ibid. This is calculated based on ‘total donations received’ by private and public ancillary funds in 2012–13.
There are other sources that provide indications of the size of Australian cross-border charitable flows and activities. The Australian Bureau of Statistics (‘ABS’) found that charitable giving in Australia amounted to A$8614 million (8% of total sector income and 0.57% of gross domestic product).40 It shed light on the amount of outgoing charitable funds based on a sub-population of nearly 57 000 ‘economically significant’ non-profits (of the ABS’s estimated 177 000) that have an active tax role.41 The ABS estimated that of A$5.684 billion in grants and other payments made by non-profits to others, A$1.03 billion (18%) went to ‘non-resident organisations’, defined as any organisation domiciled overseas.42 While this figure includes DGRs that have been sanctioned to provide support for international charitable activities, a significant component also includes intermediary giving, where qualified Australian DGRs channel tax-deductible funds overseas for other charitable entities.

Another source indicating the extent of Australian cross-border charitable activities is the recently established Australian Charities and Not-for-profits Commission (‘ACNC’), which has begun collecting information as part of its remit to publish annual returns from charities. The first analysis of the 2013 ‘Annual Information Statements’ (‘AIS’) noted that

[c]harities could indicate that they were involved with countries outside of Australia in three ways; by nominating ‘international activities’ as one of their activities, by nominating ‘communities overseas’ as one of their beneficiaries, or by advising that they operate outside of Australia. In total, 6476 charities or 17% of all reporting charities indicated they were involved in someway internationally. This could include sending donations or other aid or more active involvement.43

A total of 218 charities indicated that their main activity was ‘international activities’.44 While the amount transferred across borders was not collected by the annual returns, it serves as another guide to the potential number of charitable entities that are involved in cross-border activities.45

Finally, Australia’s membership of the OECD Development Assistance Committee (‘DAC’)46 requires Australia to provide annual estimates of private philanthropic flows to developing countries. OECD figures show that, in 2012, the Australian Government reported just over US$1.4 billion in private giving to

41 This includes all market non-profit organisations (approximately 21 000) and significant non-market non-profits (approximately 36 000): ibid table 4.
42 Ibid table 10.1. Foreign branches and foreign subsidiaries of Australian organisations are regarded as non-resident organisations.
43 Penny Knight and David Gilchrist, ‘Australian Charities 2013’ (First Report on Charities Registered with the Australian Charities and Not-for-profits Commission, Curtin University Not-for-profit Initiative, 24 September 2014) 38.
44 Ibid 31.
45 It is possible that non-charities may have gift deductibility status, but these would be small in number.
46 A forum to discuss issues surrounding aid, development and poverty reduction in developing countries.
developing countries.\textsuperscript{47} However, we believe a more accurate figure is US$897 million because of data calculation errors,\textsuperscript{48} representing approximately 10\% of total charitable giving. This is consistent with a recent analysis of financial data from the Australian Council for International Development (‘ACFID’), the peak council for Australian aid and development organisations, showing total private support to ACFID members of A$832 million\textsuperscript{49} (or US$862 million) in 2012.\textsuperscript{50} Because most private international giving is channeled to developing countries through relief and development non-government organisations (‘NGOs’),\textsuperscript{51} the ACFID’s data represents a significant component of Australian cross-border giving. Australians also support overseas activities and beneficiaries for purposes other than relief or development, so the total cross-border philanthropy numbers would have to be added to the revised DAC calculations.

It is also possible to use the ACFID’s private giving data to make a crude estimate of the cost to the fisc of the tax deduction for cross-border donations. That data is derived from donations to international relief and development organisations, the majority of which are tax deductible and would therefore be included in Treasury’s annual tax expenditures statement under ‘deduction for gifts to DGRs’. The 2014 Tax Expenditures Statement shows that, in 2012–13, the deduction for gifts to DGRs cost A$1.01 billion.\textsuperscript{52} Based on the ACFID data, approximately 10\% of these gifts are directed to DGRs operating overseas, resulting in a relatively minor cost to Treasury of approximately A$101 million for cross-border donations. Any calculation of the cost to Treasury of the deduction for cross-border gifts also needs to consider the return in the form of benefits that the Government receives for the public funds expended. We will return to this issue of the deduction’s impact later in the article.

Existing data points to Australian non-profit organisations being involved in cross-border charitable activities. However, Australia’s tax regime effectively places geographic barriers around charitable tax relief for their donors. Understanding the restrictions that exist in Australian tax laws, and the extent to


\textsuperscript{48} The data is collected from the ACFID. In the ACFID’s survey for the financial year 2011–12, total revenues to the sector amounted to A$1.4 billion, comprising: A$424 million in government grants (30\% of total revenue); A$108 million in investment income and income from other sources (7\%); and A$871 million in community support (63\%) including donations (monetary and non-monetary), fundraising, legacies and bequests. It appears that the Australian Government may have reported the total revenue provided by the ACFID, not just the community income component: email from Garth Luke (Policy Lead, Official Development Assistance, World Vision Australia) to Natalie Silver, 7 July 2014 (on file with authors).

\textsuperscript{49} Based on a data analysis of ACFID members’ financial statements. See Michael Booth, A Framework That Will Assist Not-for-Profit Boards and Managers to Discharge Their Accountability for Achieving Organisational Financial Sustainability (PhD Thesis, QUT, forthcoming).

\textsuperscript{50} Based on the 2012 average AUD:USD exchange rate of 1.035937.

\textsuperscript{51} Roodman and Standley, above n 10, 5–6.

\textsuperscript{52} Treasury (Cth), above n 37, 7, item A54. Compare the US, where this tax expenditure was US$38 billion in 2012, about 4\% of federal personal income tax revenues: see Jon Bakija, ‘Tax Policy and Philanthropy: A Primer on the Empirical Evidence for the United States and Its Implications’ (2013) 80(2) Social Research 557, 558–9.
which the laws provide scope to work around these limitations, becomes critical for organisations and their donors engaging in charitable activities overseas.

III Australian Tax Laws Affecting Cross-border Philanthropy

Under div 30 of the *Income Tax Assessment Act 1997* (Cth) ("ITAA 1997"), only organisations that are DGRs are entitled to receive gifts and contributions that are tax deductible. The gift deductibility provisions in div 30 are extensive and detailed. Australian residents can deduct from their taxable income the value of donations of A$2 or more made to a fund or organisation that is endorsed by the ATO as a DGR or listed by name in the *ITAA 1997* as a DGR. To be eligible for DGR endorsement, an organisation must satisfy a number of conditions, one of the most critical being that the organisation must be ‘in Australia’.

The ‘in Australia’ requirements for DGR status have been interpreted strictly by the ATO. In its 2003 public ruling on Public Benevolent Institutions (‘PBIs’, a class of DGR), the ATO set out the ‘in Australia’ special conditions:

129. To be in Australia a public benevolent institution must be established, controlled, maintained and operated in Australia and its benevolent purposes must be in Australia. Because the purpose of public benevolent institutions is to provide direct relief to persons in need, this will mean that relief will be provided to people located in Australia.

130. However, we accept that where a public benevolent institution conducts an activity outside Australia that is merely incidental to providing relief in Australia, or is insignificant, it will not disqualify the institution from endorsement. For example, if a public benevolent institution provides medical assistance to children in Australia with a particular disability but, to a minor extent, it also brings children from other countries to receive treatment in Australia, it still meets this condition for endorsement.

This strict interpretation was reflected in the ATO’s taxation guide for DGRs and donors, which stated that the ‘in Australia’ condition required that funds, institutions and authorities ‘be established and operated in Australia (including control, activities and assets)’ and ‘have their purposes and beneficiaries in Australia’.

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53 *ITAA 1997* s 30-227.
54 Ibid sub-div 30-BA.
55 The ‘in Australia’ requirements for DGR endorsement are set out in s 30-15 of the *ITAA 1997* under ‘Special conditions’, which include that ‘the fund, authority or institution must be in Australia’.
56 ATO, *Income Tax and Fringe Benefits Tax: Public Benevolent Institutions*, TR 2003/5, 4 June 2003 (‘TR 2003/5’). Note that the recent case of *Hunger Project* (2014) 221 FCR 302 decided that the ATO view about ‘direct relief’ was incorrect and that fundraising proceeds to be given to others to relieve the poor did satisfy the directness test.
More recently, the ATO’s position appears to be shifting. Since 2012, the wording of the ATO’s taxation guide has altered, now stating that ‘[f]or funds, institutions and authorities to be in Australia, they must be established and operated in Australia’. The guide then lists those ‘funds’ for which the ‘purposes or beneficiaries’ must also be in Australia and those for which the purposes and beneficiaries do not have to be in Australia. The ATO’s website reflects the changes made to the guide. Further evidence of the shifting ATO position was provided in August 2015 when the ATO issued an ‘in Australia’ discussion paper to the Not-for-Profit Advisory Group (‘Advisory Group’), the purpose of which was to provide greater clarity of the ATO view of the meaning of “in Australia” in Divisions 30 and 50 of the Income Tax Assessment Act 1997 and provide input to a public ruling or other guidance products covering the meaning of “in Australia”.

The Advisory Group met in December 2015 to consider the extensive feedback received on the discussion paper. Based on the Advisory’s Group’s recommendations, the ATO is currently drafting a new ‘in Australia’ ruling. As a result, it seems likely that the ATO will withdraw TR 2003/5 in the near future.

For now, the current ‘in Australia’ test for DGRs remains that enunciated by the Commissioner in TR 2003/5. This test is stricter than the ‘in Australia’ test for income tax exemption set out in div 50 of the ITAA 1997. Under div 50, the test for income tax exempt entities (‘ITEEs’) requires that an entity has ‘a physical presence in Australia and, to that extent, incurs its expenditure and pursues its objectives principally in Australia’. In adopting this language, the Government explained that having a ‘physical presence’ in Australia is to be broadly interpreted. It does not require that the organisation be ‘established, controlled, maintained and operated’ in Australia as provided by TR 2003/5. In addition, the use of the term ‘principally’ provides further scope for ITEEs to pursue their objectives outside Australia as compared to the provisions for DGRs, which contain no such modifying language.

The practical consequences of the strict ‘in Australia’ requirements for DGRs are that donations by Australian taxpayers made directly to an organisation outside Australia are never tax deductible. Donations made to an Australian DGR that uses the gift for its own programs outside Australia are also not tax deductible.

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59 See above n 57.
61 Formed by the ATO in November 2013, the Not-for-Profit Advisory Group was established as a stewardship committee to consider matters of strategic importance to the non-profit sector.
63 ITAA 1997 s 50-50(1)(a) (emphasis added).
64 ‘Principally’ means mainly or chiefly. Less than 50% would not be considered to meet the ‘principally’ requirement: see Explanatory Memorandum, Taxation Laws Amendment Bill (No 4) 1997 (Cth) [5.29].
65 Explanatory Memorandum, Taxation Laws Amendment Bill (No 7) 1997 (Cth) [3.14].
unless its activities outside Australia are ‘merely incidental’ or the organisation obtained its DGR status pursuant to one of the exceptions to the ‘in Australia’ requirements discussed below.

The law is not clear as to whether donations directed overseas through an Australian organisation that has obtained its DGR status pursuant to an exception to the ‘in Australia’ requirements are tax deductible. The use of these qualified DGRs as domestic giving intermediaries is a mechanism widely employed by Australian charities and their donors to circumvent the strict ‘in Australia’ requirements. These channelling or conduit arrangements, known as ‘auspicing’, typically involve contractual (and less formal) agreements, where a servicing fee is paid to the intermediary DGR ‘in the range of 7–10% of the amount distributed’. This workaround appears to be less than beneficial for the paying organisations and their donors, the beneficiaries who receive their funds net of administrative fees, and the Australian regulators whose oversight is compromised. It is also unclear to what extent serving as a giving intermediary for a fee is permissible under current Australian law, particularly if this servicing fee is accounted for as part of a tax-deductible donation. It is also questionable whether a donation to an intermediary DGR with conditions attached specifying where those funds are to be directed constitutes a tax-deductible gift or a bargain. Some more recent exceptions explicitly prohibit an approved organisation acting as a mere conduit for donations.

Because the exceptions to the ‘in Australia’ requirements are so critical for organisations and their donors who wish to engage in tax-effective cross-border charitable activities, we will examine them in detail. There are four exceptions to the ‘in Australia’ requirements, dispersed throughout div 30 of the ITAA 1997, which provide scope for DGRs that are established and administered in Australia to pursue their purposes and have their beneficiaries overseas. These are:

- overseas aid funds;
- developed country disaster relief funds;
- public funds on the Register of Environmental Organisations; and
- DGRs specifically listed by name in the ITAA 1997 under the ‘international affairs’ category.

It is important for any policy analysis to examine the effectiveness of these four exceptions in facilitating and regulating Australian organisations (and their donors) engaged in tax-effective charitable activities overseas. This involves determining the legal and administrative requirements for each exception, as well as the extent to which Australian organisations have qualified as DGRs and maintained their DGR status under each exception.

66 TR 2003/5, above n 56, [130].
67 See below Part VIIIIA.
68 There is a prohibition on non-profits acting as ‘mere conduits’ in other jurisdictions such as the US, Canada and the Netherlands.
69 Letter from Philanthropy Australia to Prime Minister Tony Abbott, above n 27, 1.
71 ATO, Income Tax: Overseas Aid Gift Deduction Scheme, TR 95/2, 1 June 1995, [1] (‘TR 95/2’).
IV Overseas Aid Funds

Australian organisations undertaking relief and/or development work outside Australia can apply to establish an overseas aid fund under the Overseas Aid Gift Deduction Scheme (‘OAGDS’) administered by the Australian Government Department of Foreign Affairs and Trade (‘DFAT’).72 If the application is successful, the organisation can then apply to the ATO to be endorsed as a DGR under the general category of ‘developing country relief fund’.73 The Government has stated that this exception to the ‘in Australia’ requirement is ‘in recognition that although some organisations are not operating in Australia, it is considered that they nonetheless further Australia’s overseas aid objectives and therefore contribute to Australia’s broad public benefit’.74

Overseas aid funds are provided for in sub-div 30-B of the ITAA 1997 under the category of ‘international affairs’.75 There are four requirements under the ITAA 1997 that must be met in order to qualify as an overseas aid fund. The fund must be:

1. a public fund;
2. a charity registered with the ACNC or operated by such a charity;
3. established by an organisation declared by the Australian Government Minister for Foreign Affairs to be an ‘approved organisation’; and
4. established and maintained solely for the relief of people in a country declared by the Minister for Foreign Affairs to be a developing country.76

The second requirement that the fund is a charity registered by the ACNC or is operated by a registered charity ensures that the fund will be subject to ACNC regulation and monitoring, including reporting through the ACNC’s AIS. At present however, the AIS contains minimal information on cross-border activities and donations. In addition, while the Australian Charities and Not-for-profits Commission Act 2012 (Cth) makes provision for a set of minimum standards to regulate registered charities sending funds or engaging in activities outside of Australia, to date these ‘external conduct standards’ have not been developed.77

The third requirement that the applicant seeking to establish the overseas aid fund be an ‘approved organisation’ is difficult to meet in terms of substance

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72 The OAGDS was administered by the Australian Agency for International Development (‘AusAID’) prior to the integration of AusAID into DFAT.
73 TR 95/2, above n 71, [2]–[3], [4]–[6].
74 Explanatory Memorandum, Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 (Cth) 30 [1.133]. See also Commonwealth, Parliamentary Debates, House of Representatives, 23 August 2012, 9728 (David Bradbury, Assistant Treasurer).
75 ITAA 1997 ss 30-80(1) item 9.1.1, 30-85.
76 See DFAT, List of Developing Countries as Declared By the Minister for Foreign Affairs (February 2015) <http://dfat.gov.au/about-us/publications/Documents/list-developing-countries.pdf>. This list is based on the OECD DAC’s list of countries and territories eligible to receive official development assistance.
and process. Under the OAGDS Guidelines, the applicant must complete a submission to DFAT containing evidence that it is:

- a legal entity;
- voluntary, not-for-profit and non-government;
- a community-based organisation accountable to its membership;
- demonstrably Australian,\(^78\)
- focused on development and/or relief\(^79\) activities covering at least one year;
- conducting overseas activities on a partnership basis with indigenous in-country partners,\(^80\) and
- together with its in-country partners, effective in conducting their activities.\(^81\)

The fourth \textit{ITAA 1997} requirement that the fund be established and maintained solely for the relief of people in a developing country requires that the fund ‘be governed by a constitution or set of rules from which it is clear that its exclusive purpose is to provide relief to persons in certified developing countries’.\(^82\) This differs from DFAT’s OAGDS Guidelines’ ‘approved organisation’ condition that ‘[t]he organisation’s mission statement or purpose and its project objectives should reflect a focus on development and/or relief’.\(^83\) The OAGDS Guidelines define ‘relief’ as the short-term provision of basic support in emergency situations,\(^84\) while ‘development’ is a long-term process focused on breaking the cycle of poverty.\(^85\) The inconsistency between the OAGDS Guidelines and the \textit{ITAA 1997} has created uncertainty for organisations seeking DGR status through the overseas aid exception.

In addition to the four substantive requirements in the \textit{ITAA 1997}, there are also significant administrative hurdles to overcome. The process of becoming an overseas aid fund is lengthy. The first step is applying for ‘approved organisation’ status through DFAT, which then recommends to the Minister for Foreign Affairs that the applicant be an ‘approved organisation’. Once this is established, the ATO assesses the application for DGR endorsement to ensure that the four requirements in the \textit{ITAA 1997} have been met. The ATO then seeks approval from the Treasurer.

\(78\) ‘An organisation needs to show how recipient communities know that the assistance they are receiving comes from Australian sources’ and, if the organisation belongs to an international network, how it distinguishes its Australian work and funding: DFAT, \textit{Overseas Aid Gift Deduction Scheme: Guidelines for Obtaining Tax Deductibility} (2014) 7.

\(79\) Ibid 9–11. DFAT makes it clear in their guidelines that, for the purposes of tax deductibility, relief and development do not include ‘welfare, evangelism, missionary or political activities’: ibid 9. If the organisation engages in these activities they must be distinguished from relief and development activities and managed separately.

\(80\) This requires that the organisation be ‘more than just a fundraising arm’ of its overseas partners: ibid 12. However, the opposite conclusion was reached in the Federal Court case of \textit{Hunger Project} (2014) 221 FCR 302.

\(81\) Ibid 12–13. What constitutes ‘effective’ is primarily the applicant organisation’s monitoring and evaluation of overseas activities and partners.

\(82\) TR 95/2, above n 71, [6(a)] (emphasis in original).

\(83\) DFAT, \textit{Overseas Aid Gift Deduction Scheme}, above n 78, 8.

\(84\) Ibid 9.

\(85\) Ibid 8.
that the fund be declared a developing country relief fund.\textsuperscript{86} While DFAT estimates that the entire approval process takes 9–12 months,\textsuperscript{87} an efficiency audit determined that it can take up to two years to complete\textsuperscript{88} and that, as a result, some lawyers are advising their clients not to pursue endorsement under this category.\textsuperscript{89} This appears to be reflected in the numbers: at 31 October 2014, there were 235 overseas aid funds, representing just 0.84% of all active DGRs.\textsuperscript{90}

In May 2015, DFAT announced a review of the OAGDS Guidelines and processes in an attempt to ‘reduce red tape, streamline the process for applicants, and provide greater clarity’.\textsuperscript{91} As part of this review, DFAT invited written submissions and held roundtable discussions in mid-2015.\textsuperscript{92} Key findings of the review included that the guidelines should be less prescriptive and more flexible, and that a number of outdated and inconsistent requirements should be revised, such as those related to the definitions of development and relief.\textsuperscript{93} The findings were also critical of the OAGDS process, notably the time it took to apply for and assess the application, the complexity of the application process and the resourcing toll it took on organisations, particularly when compared to the process of obtaining tax-deductible status in other OECD countries.\textsuperscript{94} The onerous process was also found to be disproportionate to the risks associated with working overseas.\textsuperscript{95} Following this public consultation, DFAT is expected to issue revised guidelines in 2016.

Organisations seeking to qualify as overseas aid funds are required to overcome significant legal and administrative hurdles, serving as a deterrent for organisations that would otherwise pursue endorsement under this exception. However, once an organisation has achieved DGR status (while subject to ACNC monitoring), there appears to be minimal ongoing regulation of cross-border activities and donations. Indeed, evidence suggests that overseas aid funds are engaged in auspicing — entering into third-party arrangements to assist other non-profit organisations to channel tax-deductible donations overseas often for a servicing fee.\textsuperscript{96}

\begin{itemize}
\item 86 Ibid 1–2.
\item 87 Ibid 16–17. DFAT also notes that ‘there may be an interval of several months between [the Minister for Foreign Affairs and the Treasurer’s] decisions’. This may explain the difference between the Auditor-General’s estimate and DFAT’s estimate.
\item 89 Ibid 108 [4.38].
\item 90 ATO, Taxation Statistics 2012–13: Charities, above n 38, table 3.
\item 92 Ibid. Submissions were received from 22 organisations and more than 100 participants attended roundtables.
\item 93 Ibid 11–17.
\item 94 Ibid 7–8.
\item 95 Ibid 8.
\item 96 See above n 42 and accompanying text.
\end{itemize}
V Developed Country Relief Funds

Developed country relief funds are provided for in sub-div 30-B of the *ITAA 1997* under the category of ‘international affairs’ and enable Australian donors to make tax-deductible donations to developed countries that have experienced natural disasters. To qualify as a developed country relief fund, the fund must satisfy three requirements under the *ITAA 1997*. The fund must be:

1. a public fund;
2. set up and controlled by a registered PBI; and
3. established and maintained solely for providing money for relief for people who are in distress as a result of a disaster in a country outside Australia that has not been declared by the Minister of Foreign Affairs as a developing country.

The disaster must be recognised by a Treasury Minister as a disaster. The Minister may declare a disaster if satisfied that it developed rapidly and resulted in the death, serious injury or other physical suffering of a large number of people, or in widespread damage to property or the natural environment. The DGR entitlement is limited to two years from the date of the disaster in the Minister’s declaration. The ATO maintains a list of disasters that have been recognised by the Treasury since this provision was enacted in 2006. At the time of writing, there were 10 disasters on this list.

Developed country relief funds represent a particularly limited exception to the ‘in Australia’ requirements, applying for a specific period to a very small number of natural disasters overseas. It also creates policy inequity by focusing on disasters in developed countries, with organisations providing support to victims of disasters in developing countries having to meet the far more onerous requirements of the OAGDS, even where a particular disaster affects both developed and developing countries.

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97 *ITAA 1997* ss 30-80(1) item 9.1.2, 30-86.
100 *ITAA 1997* s 30-86(4).
102 Ibid.
VI  Public Funds on the Register of Environmental Organisations

Administered by the Australian Government Department of the Environment in consultation with the ATO, the Register of Environmental Organisations (‘REO’) was established in 1992 to enable deductions for gifts made directly to an environmental organisation. While the *ITAA 1997* does not specify that organisations on the REO are able to operate outside Australia, the Commissioner of Taxation has taken the position that these organisations do not need to have their purposes or beneficiaries in Australia. The only requirement is that ‘the actual public fund must be in Australia’.

For an organisation to be entered on the REO, it must be a public fund and satisfy six requirements in sub-div 30-E of the *ITAA 1997*. The fund must:

1. be a body corporate, a co-operative society, a trust, or an unincorporated body established for a public purpose by the Commonwealth, a state or a territory;
2. have a principal purpose of protecting and enhancing the natural environment or a significant aspect of it, or providing information or education, or carrying out research about the natural environment or a significant aspect of it;
3. maintain a public fund to receive gifts for its principal purpose and comply with any Ministerial rules to ensure that gifts made to the fund are used only for its principal purpose;
4. not give any of its property, profits or financial surplus to its members, beneficiaries, controllers or owners;
5. have a policy of not acting as a mere conduit for the donation of money or property; and
6. provide statistical information about donations and gifts to the Environment Secretary each financial year.

In addition to these legislative requirements for inclusion on the REO, there is a lengthy admission process. The first step is applying to the Department of the Environment, which carries out an initial assessment of all applications to ensure that the organisations meet the legal requirements in the *ITAA 1997* and the

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106 The Explanatory Memorandum to the Bill introducing the provisions for the REO in the *Income Tax Assessment Act 1936* (Cth) was also silent on this issue.
108 TR 95/27, above n 107, [14].
109 *ITAA 1997* s 30-260.
110 Ibid s 30-265(1).
111 Ibid ss 30-265(2), (4).
112 Ibid s 30-270(1).
113 Ibid s 30-270(2).
114 Ibid s 30-270(4).
administrative requirements in the *REO Guidelines*. Once the Department has determined that the applicant has met these requirements, it is passed to the Treasurer for ATO approval.\(^{115}\) The Auditor-General has found that this process can take more than 18 months, which may serve to discourage applications.\(^{116}\) As of 31 October 2014, there were 590 funds on the REO,\(^{117}\) representing just over 2% of all active DGRs.\(^{118}\)

Like overseas aid funds, organisations seeking to be on the REO are required to overcome significant entry barriers. These impediments have served to discourage qualifying organisations. Once listed, these environmental organisations are required to submit an AIS,\(^{119}\) including audited financial statements,\(^{120}\) providing some ongoing regulation. In addition, pursuant to the requirement in s 30-270(2) of the *ITAA 1997*, they are prohibited from serving as a conduit to channel funds for another entity operating overseas, limiting the use of this workaround.

In March 2015, the House of Representatives Standing Committee on the Environment began an inquiry into the REO examining the definition of ‘environmental organisation’ and the activities undertaken.\(^{121}\) International activities have not been an area of focus for this inquiry, indicating that this ‘in Australia’ exception is not under scrutiny.

**VII Deductible Gift Recipients Listed by Name under the ‘International Affairs’ Category**

Parliament may amend the *ITAA 1997* specifically to list individual organisations by name as a DGR.\(^{122}\) As a general rule, DGRs listed by name in the *ITAA 1997* remain subject to the strict ‘in Australia’ requirements. However, those that are listed as DGRs under the category of ‘international affairs’ in s 30-80(2) are exempt from the conditions requiring that their purposes and beneficiaries be in Australia.\(^{123}\) There is currently an eclectic collection of 23 DGRs listed by name, representing a diverse range of activities and countries.\(^{124}\) Some of these

\(^{115}\) *REO Guidelines*, above n 104, 4.

\(^{116}\) ANAO, above n 88, 108–9 [4.38]–[4.41].


\(^{120}\) *REO Guidelines*, above n 104, 10–11.


\(^{122}\) *ITAA 1997* s 30-17(1)(a); ANAO, above n 88, 38 [1.7].

\(^{123}\) See TR 95/27 above n 107, [14(b)]. There is a similar provision in ss 50-50(1)(c)–(d) of the *ITAA 1997* for ITEEs that are exempt from income tax despite conducting most of their work overseas.

\(^{124}\) *ITAA 1997* s 30-80(2).
organisations have time limits on their gift deductibility and, at the time of writing, the time limits for seven organisations had expired.\textsuperscript{125}

While these DGRs represent less than 1\% of all active DGRs (at 31 October 2014),\textsuperscript{126} the privileges of being in this select group are noteworthy. These DGRs are not only exempt from the strict ‘in Australia’ requirements, but also within the four exceptions they have the lowest level of restrictions. Their overseas activities are not limited to development or relief work, and their beneficiaries are not confined to particular countries, so long as they ‘continue to operate for their principal purpose and comply with any rules or conditions made by the government on listing as a DGR’.\textsuperscript{127} Once approved by the government of the day, these organisations are able to attract tax-deductible donations for their overseas activities with relatively little oversight.\textsuperscript{128} Like overseas aid funds, there is evidence that DGRs specifically listed under international affairs engage in auspicing to assist other Australian non-profits channel tax-deductible donations overseas.

Scant information exists regarding the process of becoming listed by name in the tax laws. Treasury brings the legislative amendments to government, in consultation with the ATO.\textsuperscript{129} The ATO does not process an inquiry for listing by name. Instead, requests are directed to the Treasurer in writing.\textsuperscript{130} This is a political process with a successful application requiring ‘the support of the Commonwealth Government minister responsible … for the type of activities and purposes of the organisation seeking listing’.\textsuperscript{131} Politicians from across the political spectrum have acknowledged the problems associated with the listing process. In a fascinating parliamentary debate on this issue in 1989, the Minister for Finance declared that ‘there is an element of semi- or quasi-arbitrariness in the selection of charity lists which qualify for tax deductions. It is very difficult for anybody unequivocally to support or condemn any particular organisation’s inclusion on the list’.\textsuperscript{132} One Senator suggested in response that

\textquote{to ensure that organisations are not left out just because they do not have a voice in this chamber or someone advocating for them … the Government look at those voluntary organisations that have a valid claim for tax deductibility and are like other organisations that do get it.}\textsuperscript{133}

\begin{thebibliography}{9}
\bibitem{125} Ibid.
\bibitem{127} \textit{GiftPack 2012}, above n 58.
\bibitem{128} DGRs listed by name are subject to s 353-20 of the \textit{Taxation Administration Act 1953} (Cth), which enables the Commissioner to require a specifically listed DGR to provide information relevant to its status as a DGR in order to determine if it continues to be eligible for DGR status. The Commissioner is to advise the Minister if the entity is or is not operating consistently with the obligations as a DGR.
\bibitem{129} ANAO, above n 88, 38 [1.7].
\bibitem{130} See Thomson Reuters, \textit{Not-For-Profit Best Practice Manual}, vol 1 (at Service 2) [5.1.607].
\bibitem{131} Ibid.
\bibitem{132} Commonwealth, \textit{Parliamentary Debates}, Senate, 9 June 1989, 3766 (Peter Walsh).
\bibitem{133} Ibid 3766 (Kay Patterson). In response, Senator Macklin concurred that there ought to be a general review of this legislation, but that nothing had eventuated: at 3767.
\end{thebibliography}
More recently, the Not-for-Profit Sector Tax Concession Working Group found that the process of being listed in the tax laws suggests ‘that some entities are more deserving of assistance than others’.  

The very small number of organisations that have obtained DGR status under this ‘in Australia’ exception face barriers to entry that are extremely high. Entry into this exclusive group appears to be largely political. Organisations that succeed are able to offer their donors the ability to make tax-deductible donations overseas, as well as serving as giving intermediaries for a fee, without being subject to ongoing supervision by the authorities. The result is an exception to the ‘in Australia’ requirements that offers little transparency, accountability or equity.

**A Summary of the Tax Laws Affecting Cross-border Philanthropy**

We have determined the options available for Australian donors who wish to make tax-deductible cross-border gifts from the complex ad hoc policy responses provided by the Australian Government. The current legislative architecture starts from the position of a flat prohibition and then allows for a few specific exceptions. An examination of these exceptions reveals the limited extent to which Australian organisations and their donors can engage in tax-effective giving overseas. It appears that, due to the significant legal and administrative barriers to entry, relatively few organisations have obtained DGR status through one of these exceptions.

This finding was confirmed in a recent report examining Australian charities involved overseas, using AIS submitted to the ACNC. The report noted that just 16% of charities involved overseas were endorsed as DGRs compared with 40% of all charities. There also appears to be an absence of equity considerations in the policy underlying some of these exceptions. For those organisations that succeed in overcoming the high entry barriers, there is little oversight and monitoring by the authorities. This problematic combination of high entry barriers and a lack of ongoing regulation has resulted in organisations and their donors using workarounds to circumvent the tax laws in order to engage in tax-effective cross-border charitable activities, presenting further challenges for regulators in monitoring the flow of charitable funds overseas.

Recent judicial decisions addressing the use of such workarounds have challenged the geographic restrictions on tax laws affecting cross-border philanthropy. The Australian Government’s response to these decisions has been to propose a reform agenda that seeks to further limit the ability of Australian organisations and their donors to engage in tax-effective activities overseas. We now turn to an examination of these proposals and their genesis.

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134 Not-for-Profit Sector Tax Concession Working Group, ‘Fairer, Simpler and More Effective Tax Concessions for the Not-for-Profit Sector’ (Final Report, Treasury (Cth), May 2013) 23.

VIII The Proposed ‘in Australia’ Reform Agenda

A Judicial Decisions Precipitating Reform

The ‘in Australia’ requirements came under judicial scrutiny in the landmark case of *Word Investments*,136 which enshrined the destination-of-profits test for income tax exemption and approved the channelling of funds abroad in relation to such provisions. Apart from a few commentators,137 the academic discourse on the *Word Investments* decision has largely ignored cross-border issues.138

The applicant (Word Investments) was a fundraising arm that distributed funds to Wycliffe Bible Translators Australia, an Australian charity conducting missionary work overseas. Word Investments applied for income tax exemption under sub-div 50-B of the *ITAA 1997*, which was refused. The Commissioner argued that there were four issues precluding Word Investments from receiving tax exempt status, one of which was that it did not meet the s 50-50(a) *ITAA 97* ‘in Australia’ requirement that an entity have a physical presence in Australia and, to that extent, incur its expenditure and pursues its objectives principally in Australia. A majority of the High Court of Australia139 determined that Word Investments met the ‘in Australia’ requirements, as it had a physical presence in Australia, incurred its expenditure and pursued its objectives principally in Australia; the decisions to pay were made in Australia, the payments were made in Australia to Australian organisations and its objectives included providing financial assistance to those organisations.140

In reaching its conclusion, the majority examined the ‘in Australia’ test in s 50-50(a) as it applied to Word Investment’s role as a charitable intermediary. The majority found that

> [s]ection 50-50(a) does not impose a prohibition on distributing to other charitable institutions. Nor does it require the money, when ultimately expended by Wycliffe and the other institutions, to be expended in Australia.

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139 Gummow, Hayne, Heydon and Crennan JJ.
Section 50-50(a) could have imposed a requirement of that latter kind, but it did not. It only imposed a requirement that Word incur its expenditure and pursue its objectives principally in Australia — not that Wycliffe and the other institutions do so. No doubt the ultimate benefit to charity which Word causes is effected by Wycliffe indirectly and to some extent outside Australia, not directly and in Australia: but s 50-50(a) draws no distinction between direct and indirect effects.\(^{141}\)

As a result, the ‘in Australia’ test in s 50-50(a) is confined to ‘the place where the relevant conduct occurs, not to that where the ultimate purpose of that conduct is given effect, or its objective realised, by a donee’s actual use of the money it receives’.\(^{142}\) That is, a channel was available to send charitable funds abroad through a suitably qualified organisation.

This position was recently affirmed in the Full Federal Court of Australia decision in *Hunger Project*.\(^{143}\) In that case, the question was whether Hunger Project Australia (‘HPA’) qualified as a PBI in Australia. HPA was part of a global network of entities, centrally administered in the US, whose purpose was to relieve hunger in a number of developing countries. While HPA was primarily a fundraising arm for the Hunger Project entities engaged in the direct provision of hunger relief, it had some involvement in global and program decision-making, as well as in determining where to direct the funds it raised.\(^{144}\) The Court did not specifically address the ‘in Australia’ requirements, most likely because HPA was an overseas aid fund and therefore came under one of the exceptions to the ‘in Australia’ requirements.\(^{145}\) However, in finding HPA to be a PBI, the Court determined that

\[\text{[t]he ordinary contemporary meaning or understanding of a public benevolent institution is broad enough to encompass an institution, like HPA, which raises funds for provision to associated entities for use in programs for the relief of hunger in the developing world. The fact that such an institution does not itself directly give or provide that relief, but does so via related or associated entities, is no bar to it being a public benevolent institution.}\]

The ‘in Australia’ test for ITEEs enunciated in *Word Investments* and affirmed in *Hunger Project* had immediate and significant implications for the ATO’s strict interpretation of the ‘in Australia’ requirements for DGRs. By interpreting the ‘in Australia’ requirement for ITEEs such that the ultimate purposes or beneficiaries were not required to be in Australia and such that charitable funds could be distributed through qualified Australian entities operating overseas, the *Word Investments* test suggested that a DGR’s purposes or beneficiaries may similarly no longer be required to be ‘in Australia’ and that it could raise funds in Australia and send those tax-deductible funds overseas through a qualified Australian giving intermediary (such as an overseas aid organisation or

\(^{141}\) Ibid 239 [73].


\(^{143}\) (2014) 221 FCR 302.

\(^{144}\) Ibid 303–4.


\(^{146}\) *Hunger Project* (2014) 221 FCR 302, 314 [67].
an organisation specifically listed in the *ITAA 1997* under international affairs). Indeed, the recent ATO ‘in Australia’ discussion paper evidences a shift in the ATO’s position towards DGRs in accordance with the *Word Investments* test. However, it remains unclear to what extent this test permits the practice of auspicing, whereby qualified organisations enter into third-party arrangements to assist others channel tax-deductible donations overseas for a servicing fee.¹⁴⁷

As a result of the decision in *Word Investments*, the Australian Government determined that reforming the ‘in Australia’ requirements was necessary to reduce uncertainty around charitable intermediary arrangements and to ensure that the ATO’s original strict ‘in Australia’ position prevailed. We now turn to those reform proposals.

**B  The Government’s Reform Proposals**

In its 2009–10 budget, the Australian Government announced that it would amend the ‘in Australia’ special conditions in div 50 of the *ITAA 1997* in response to

> [a] recent High Court of Australia decision [that] held that charities may be pursuing their objectives *principally* ‘in Australia’ even where they merely pass funds within Australia to another charitable institution that conducts its activities overseas.¹⁴⁸

In 2011, as part of a series of measures to reform the tax law and regulation of charities, the Government introduced an exposure draft of a bill seeking to clarify the law by codifying the Commissioner of Taxation’s strict definition of the ‘in Australia’ requirements for both income tax exemption and gift deductibility.¹⁴⁹ Regarding income tax exemption of charities, the Explanatory Material noted that

> [i]gnoiring minor overseas activities, the intent of the original law was only to allow a charity to be able to pass funds to an overseas charity that was endorsed as a deductible gift recipient (operating a developing or developed country relief fund), or an entity specifically prescribed in the regulations. The High Court’s decision on *Word Investment* highlighted that the law is not achieving those objectives.¹⁵⁰

The exposure draft received 109 submissions, drawing attention to some drafting defects. In its submission, the ACFID summarised many of these objections:

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¹⁴⁷ See above Part III.


The problems have arisen through the complexity of the various legal structures to which the legislation relates and as a result of the multiple avenues that the Government provides for tax free and tax deductible status. The proposed legislation attempts to apply simple tests, the result of which would be to create intractable clashes amongst the various legal statuses of the aid funds and their parent entities. In addition, the problem with the proposed legislation is that it seems to have been drafted without an understanding of the most practical considerations as to how charitable agencies go about doing their work.\textsuperscript{151}

A revised exposure draft was introduced and opened for further consultation in 2012, receiving 47 submissions.\textsuperscript{152} The new exposure draft addressed some of the concerns raised, including allowing some medical research institutions and international performing arts organisations to operate outside Australia.

In 2012, the Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 (‘\textit{In Australia Bill}’) was introduced into Parliament,\textsuperscript{153} with the stated purpose of introducing a ‘new law [that] reverses the effect of the decision [in \textit{Word Investments}] that charities and other income tax exempt entities can direct funds to overseas projects outside the current policy intent’.\textsuperscript{154} The Bill proposed a new strict ‘in Australia’ test for DGRs as a new s 30-18 in the \textit{ITAA 1997}, pursuant to which a fund, authority or institution must generally:

- be established in Australia;
- operate \textit{solely} in Australia; and
- pursue its purposes \textit{solely} in Australia.\textsuperscript{155}

According to the Explanatory Memorandum, ‘solely in Australia’ is to be interpreted as requiring DGRs to be established and operated only in Australia (including control, activities and assets) and to have their purposes and beneficiaries only in Australia.\textsuperscript{156} However, overseas activities that are merely incidental to a DGR’s purposes in Australia, and overseas activities that are minor in extent and importance when considered with reference to the operations and pursuit of the organisation’s Australian activities, will not be caught.\textsuperscript{157} At the same time, just as for tax exemption, functioning as a mere conduit for another Australian charitable organisation that operates overseas will not be permitted. If funds are passed to another organisation that is not a DGR, then tracing the use of

\textsuperscript{151} ACFID, Submission to Treasury, \textit{Exposure Draft on Restating the ‘in Australia’ Special Conditions for Tax Concession Entities}, 26 August 2011, 2.


\textsuperscript{153} On 23 August 2012 the Bill was referred to the Senate Community Affairs Legislation Committee and the Parliamentary Joint Committee on Corporations and Financial Services. In September 2012, both committees tabled their reports recommending that the Bill be passed.

\textsuperscript{154} Explanatory Memorandum, Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 (Cth) 10 [1.37].

\textsuperscript{155} \textit{In Australia Bill} s 30-18(1) (emphasis added).

\textsuperscript{156} Explanatory Memorandum, Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 (Cth) 27 [1.128].

\textsuperscript{157} \textit{In Australia Bill} s 30-18(2).
these funds must occur, otherwise the intermediary organisation risks losing its DGR status.\textsuperscript{158}

While the \textit{In Australia} Bill ultimately lapsed when Parliament was dissolved in August 2013 for the federal election, in December 2013 the incoming Government announced that it would proceed with the ‘in Australia’ tax measure.\textsuperscript{159} In March 2014, a new exposure draft was introduced and the consultation process opened. The draft retained almost word-for-word the ‘in Australia’ test for DGRs proposed in the Bill\textsuperscript{160} and the same interpretation of the phrase ‘solely in Australia’.\textsuperscript{161}

With the new exposure draft essentially mirroring the wording of the \textit{In Australia} Bill, both political parties have proposed virtually the same strict ‘in Australia’ policy for DGRs. This policy has prevailed despite a number of submissions on the exposure drafts that such tight controls on cross-border charitable activities are not in Australia’s best interests. Several submissions questioned the wisdom of such restrictive measures that ‘would impose some of the highest barriers to international participation and engagement by not-for-profits in the world’.\textsuperscript{162} In response to these submissions, each successive exposure draft has merely added exemptions and exclusions to various organisational categories and for some specific organisations. The most recent draft bill includes the existing DGR exceptions, and provides for two new categories: certain performing arts organisations\textsuperscript{163} that are approved by the Minister for the Arts as having a genuine need to engage in cross-border activities and enhance Australia’s international reputation;\textsuperscript{164} and a new category of medical research institutions that operate

\textsuperscript{158} Ibid ss 30-18(3)–(4).


\textsuperscript{160} Exposure Draft, Tax and Superannuation Laws Amendment (2014 Measures No 3) Bill 2014 (Cth): In Australia Special Conditions.

\textsuperscript{161} Explanatory Materials, Exposure Draft: Tax Laws Amendment (2014 Measures No #) Bill 2014 (Cth) 26 [1.107].


\textsuperscript{163} Exposure Draft, Tax and Superannuation Laws Amendment (2014 Measures No 3) Bill 2014 (Cth): In Australia Special Conditions, cl 2 ss 30-18(9), 30-19(2)–(3), cl 10 s 30-305(1).

\textsuperscript{164} Explanatory Materials, Exposure Draft: Tax Laws Amendment (2014 Measures No #) Bill 2014 (Cth) 34 [1.137].
outside Australia, in recognition that ‘medical research is an international collaboration activity’. Submissions on the last exposure draft closed on 7 April 2014 and in November 2014 ‘Treasury advised that there is no government decision as yet on whether the “in Australia” measure will go ahead but that there is a desire to resolve this matter by the end of the calendar year’. By April 2015, the Assistant Treasurer stated that the Government was continuing to keep a ‘watching brief’ on the ‘in Australia’ provisions. At the time of writing, the Bill has yet to be formally introduced into Parliament.

C Policy Imperatives Underlying the Proposed Reform Agenda

In the Second Reading Speech introducing the In Australia Bill, the Assistant Treasurer clearly stated the policy rationale underlying the Bill’s tightening of the ‘in Australia’ requirements:

[Publicly funded tax concessions are intended to be used for the broad benefit of the Australian community, with some exceptions. In addition, without appropriate oversight, there is a risk of funds being misdirected to inappropriate and unauthorised activities outside Australia, such as money laundering and terrorist financing.]

From this speech and as further elaborated in the Explanatory Materials to the Bill’s exposure drafts, there are two policy imperatives underlying the proposed ‘in Australia’ reform agenda. These are:

- to protect the national tax base by ensuring that publicly funded tax concessions are used for the broad benefit of the Australian community.
- to prevent non-profit organisations being used for tax abuse purposes of money laundering, offshore avoidance arrangements and terrorist financing.

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165 Exposure Draft, Tax and Superannuation Laws Amendment (2014 Measures No 3) Bill 2014 (Cth): In Australia Special Conditions, cl 7 s 30-80(1).
These two imperatives to restrict cross-border tax concessions come up against the underlying policy rationale for the gift deduction generally, which is to serve as a tax incentive to facilitate philanthropic giving. The Government appears to have reconciled these conflicting policies by limiting the reach of the gift deduction to encouraging philanthropy in Australia. Do the revenue and policing concerns inherent in the two policy imperatives underlying the ‘in Australia’ reform agenda justify the generally prohibitive geographic restrictions placed on the deduction as a policy tool to facilitate giving? Or can other regulatory tools be used to allow legitimate cross-border philanthropy to occur? Each of these policy imperatives is examined to understand both the level of call upon the fisc for subsidy, as well as the potential tax abuse risk profile.

IX Revenue Concerns: Cost to the Fisc

The Government has made it clear that publicly funded taxpayer concessions should be used for the broad benefit of Australians. During the Second Reading of the In Australia Bill, the Assistant Treasurer noted the ‘longstanding policy of successive governments that DGRs should operate only for the benefit of the Australian public’. The Explanatory Materials to the most recent exposure draft and the In Australia Bill added the broader justification of protecting the ‘material amounts of revenue that would otherwise be forgone’. However, none of the Explanatory Memoranda provides an estimate of the revenue costs associated with cross-border giving.

The gift deduction can impact the Treasury through both administrative costs and the cost of the subsidy for donations that are claimed as a tax deduction. Because Australia generally does not require non-profit organisations to file tax returns, the costs of the subsidy are difficult to measure. As a result, the data needed to make a reliable estimate of the revenue impact of deductions to DGRs engaged overseas does not exist.

To date, the Government does not appear to have been challenged on its policy position that strict geographic limits on the deductibility provisions are

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173 Not-for-Profit Sector Tax Concession Working Group, above n 134, 23; Productivity Commission, above n 36, 177.
174 Explanatory Memorandum, Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 (Cth) 5 [1.2], 11 [1.43].
175 Commonwealth, Parliamentary Debates, House of Representatives, 23 August 2012, 9728 (David Bradbury).
176 Explanatory Materials, Exposure Draft: Tax Laws Amendment (2014 Measures No #) Bill 2014 (Cth) 4. This language is slightly different from the ‘large amounts of revenue that would otherwise be forgone’ used in Explanatory Memorandum, Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 (Cth) 4.
177 The Bills Digest for the In Australia Bill referred back to Treasury’s Tax Expenditures Statement, which showed an estimate of the revenue forgone in the line item ‘Deduction of gifts to DGRs’ without specifying the portion of the tax expenditure allocated to charitable activities overseas: Department of Parliamentary Services (Cth), above n 24, 24.
178 According to tax expenditure data on 20 OECD countries, while a number of countries measured charitable tax concessions, none of the countries presented data for cross-border charitable tax concessions: OECD, ‘Choosing a Broad Base — Low Rate Approach to Taxation’ (Tax Policy Studies No 19, 2010) annex A.
necessary due to the significant drain on the fisc. While a lack of reliable data from deductions to DGRs engaged overseas makes it difficult to challenge the Government’s policy focusing on the fiscal impact, we indicated earlier that it is possible nonetheless to make a rough estimate based on the ACFID’s private giving data. Using this data, the resulting cost to the Treasury for the deduction for cross-border gifts is approximately A$101 million, representing a relatively minor cost to Treasury when compared to the total cost of the subsidy for gifts to DGRs of A$1.1 billion.

Whether the floodgates would be opened by liberalising gift deductibility for cross-border philanthropy is also difficult to verify. If cross-border giving statistics had been retained, they might show that channelling accounts for a significant proportion of cross-border charitable activity. Evidence from the liberalisation of tax treatment for cross-border donations in Europe indicates that it has had a minimal revenue impact, supported by tax expenditure data from the Netherlands where there is equal tax treatment for domestic and cross-border donations.

Focusing solely on the deduction’s costs distracts from the need to undertake a cost-benefit analysis of the deduction’s actual impact. Any calculation of the potential cost to the fisc of the deduction for cross-border gifts also needs to calculate the potential benefits that flow from this tax expenditure. That is, the larger social aims of the deduction and the reach of the social benefits it delivers become important. These benefits are often difficult to measure due to their intangible and long-term nature. If quantified, however, they could reveal a significant return for the amount of public funds expended on the subsidy. The extent of the potential return to the fisc flowing from the deduction for cross-border donations is illustrated by two of its principal benefits: the generation of ‘soft power’ for the Australian Government; and the production of global public goods for the benefit of Australians (for example, medical and scientific discoveries) as well as the wider international community.

To the extent that cross-border philanthropy helps to generate soft power for the Australian Government that can be used to improve its global standing and influence, it can serve as a ‘powerful tool of public diplomacy’. ‘Soft power’ as distinguished from ‘hard power’ (for example, military might) is defined as ‘the ability to coopt others to want the same outcomes as you through intangible

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179 See, eg, Stewart, above n 6, 253: ‘The fiscal consequences of extending tax concessions to transnational charitable activities or deductions are unknown, and limits can be justified at the present time’.


attraction to shared values, thereby shaping the preferences of others’. Studies have shown that the Dutch internationalist approach with its ‘focus on multilateral cooperation and its history of commitment to international development agreements, has enhanced Dutch “soft power”’. Recent legislation in the UK commits future governments to annual foreign aid spending of 0.7% of gross national income and was enacted to provide the UK with ‘world-leading soft power capacity’. Generating soft power therefore enables countries to achieve greater effectiveness and influence on the world stage. International philanthropy can uniquely contribute to the Australian Government’s soft power because its independence from the state allows it to ‘leverage altruistic values without being beholden to the government, its policies, or its geopolitical interests’. With bipartisan political support for a significant reduction in the amount and scope of Australia’s foreign aid, the Government could encourage Australian philanthropists to assist in closing this gap through appropriate tax incentives for cross-border giving.

All Australians stand to benefit from cross-border gifts that fund organisations involved in the production of global public goods such as medical and scientific breakthroughs, conflict resolution, human rights initiatives and artistic collaborations; and in the development of solutions for global challenges such as climate change, environmental pollution and infectious diseases. By contributing to the production and financing of these goods, the Australian community also benefits through participation in international partnerships and collaborations generating international goodwill and enhancing its image abroad. Studies have shown that investing in corrective actions to solve provision problems of certain global public goods achieves greater cost-effectiveness than inaction, making it ‘far more appealing to invest in corrective actions than to continue absorbing the costs of inaction’. At the same time, because global public goods suffer from free riding, Australia’s inaction disregards the benefits that its participation would confer on other countries and may result in Australia being worse off in the long term. Cross-border donations that support the provision of global public goods are therefore likely to result in government savings that may

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184 Gabi Spitz, Roeland Muskens and Edith van Ewijk, ‘The Dutch and Development Cooperation: Ahead of the Crowd or Trailing Behind?’ (Report, NCDO, 4 March 2013) 24, citing as an example that ‘the Netherlands is not a G20 member, but has been allowed to join G20 summits’.
186 Jenkins, above n 182, 773, 800.
187 Ibid 790–5; Pozen, above n 182, 581.
188 Pedro Conceição, ‘Assessing the Provision Status of Global Public Goods’ in Inge Kaul, Pedro Conceição and Katell Le Goulven (eds), Providing Global Public Goods: Managing Globalization (Oxford University Press, 2003) 152, 158–9, who estimated that the costs of investing in the issues of international financial stability, the multilateral trade regime, reducing excessive disease, climate stability and peace and security were approximately US$310 billion, whereas the costs of inaction were estimated at approximately US$2586 billion.
not be immediately apparent, but will have a significant impact on the fisc in the long term. Private philanthropy, if appropriately incentivised, can assist in closing this funding gap given that Australia’s foreign aid has been reduced in the areas affecting the production of global public goods and the development of solutions for global challenges.

**X Policing Concerns: Tax Abuse Risk Profile**

The Australian Government has been very clear that the policing concerns of tax avoidance, money laundering and terrorist financing have been a primary driver behind the ‘in Australia’ requirements. In its announcement in the 2009–10 Budget that it would amend these requirements in the *ITAA 1997*, the Government stated that the rationale was ‘to ensure that Parliament retains the ability to fully scrutinise those organisations seeking to pass money to overseas charities and other entities’.\(^{190}\) The Explanatory Memorandum to the *In Australia Bill* states that for DGRs in particular the ‘in Australia’ requirements provide:

additional measures to address possible abuse of not-for-profit entities for the purposes of money laundering and terrorist financing, and ensure the proper operation of not-for-profit entities, their use of public donations and funds, and the protection of their assets. By limiting the use of monies to specified areas, in conjunction with greater regulatory requirements, this ensures those monies are expended appropriately and in a manner consistent with the eligibility for tax concession status.\(^{191}\)

Australia has a formidable armoury of measures to address generally such tax abusive behaviour. Changes to the tax laws that resulted from the avoidance issues of the 1970s were accompanied by legislation directed towards the issue of money laundering,\(^{192}\) including the *Proceeds of Crime Act 1987* (Cth).\(^{193}\) The legislative framework in Australia for combating the financing of terrorism builds on the existing anti-money laundering measures on the basis that organised crime and terrorist organisations typically use similar methods to launder funds and so warrant similar policy responses.\(^{194}\) The *Proceeds of Crime Act 2002* (Cth) and the *Suppression of the Financing of Terrorism Act 2002* (Cth) were enacted in response to the events of 11 September 2001 and subsequent terrorist attacks.\(^{195}\) Australia has introduced further legislation to strengthen its terrorist financing

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\(^{190}\) Swan and Tanner, above n 148, 29.

\(^{191}\) Explanatory Memorandum, Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 (Cth) 12 [1.51].


measures, as well as a list of persons and entities subject to targeted financial sanctions or travel bans under Australian sanctions laws.

The Australian Transaction Reports and Analysis Centre (‘AUSTRAC’) was created as the regulatory body for monitoring and disseminating information on illegal behaviour involving financial transactions. Monitoring is also undertaken by the Attorney-General’s Department. AUSTRAC recently issued a report examining the extent to which Australian non-profit organisations have been involved in terrorist financing activities, finding:

While charities and NPOs (non-profit organisations) are one of the more significant Australian terrorism financing channels, they have not featured in a large number of Australian terrorism financing cases. Rather than representing a sector-wide risk, terrorism financing in Australia has been limited to a handful of charities and NPOs.

This finding is supported by an Australian Institute of Criminology study, which found little evidence of Australian non-profit organisations’ involvement in money laundering and terrorist financing, suggesting that ‘there is not an elevated risk of [money laundering and terrorism financing] exploitation of Australian-based NPOs’.

Australia’s regulatory framework for money laundering and terrorist financing was recently examined by the Financial Action Task Force (‘FATF’), an independent international intergovernmental body that sets standards for combating money laundering and terrorist financing. Australia is a member of the FATF and, as a condition of membership, agrees to comply with the FATF Recommendations. Recommendation 8 focuses on non-profit organisations because the FATF has determined that these organisations are particularly vulnerable to abuse in relation to the financing of terrorism. Recommendation 8 requires countries to identify, prevent and combat terrorist misuse of non-profits through a four-pronged approach involving: outreach to the non-profit sector concerning terrorist financing issues; supervision and monitoring of the sector; information gathering and investigation; and capacity to respond to international requests.

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196 This includes the Anti-Terrorism Act (No 2) 2005 (Cth) and the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (Cth), as well as amendments to existing Commonwealth legislation.
198 Italia, above n 194, 128.
203 Ibid 55 [5(a)].
204 Ibid 55 [5(b)].
205 Ibid 55 [5(c)].
206 Ibid 55 [5(d)].
In 2014, the FATF conducted an examination of Australia’s anti-money laundering and counter-terrorist financing measures, analysing the level of compliance with the FATF Recommendations. This examination culminated in a 2015 report that rated Australia as non-compliant with Recommendation 8. The FATF found that ‘Australia has not implemented a targeted approach nor has it exercised oversight in dealing with non-profit organisations … that are at risk from the threat of terrorist abuse’. The FATF also faulted Australia for not undertaking a comprehensive risk review of the non-profit sector to identify the features and types of non-profit organisations that are at risk of being misused for terrorist financing, and was particularly critical of the ACNC for not collecting information from, conducting outreach to, or adequately monitoring the charitable sector in relation to terrorist financing. Overall, the FATF found the supervisory framework — including the registration and reporting requirements for NPOs and the domestic coordination and information sharing — to be wanting, leaving Australian NPOs ‘vulnerable to misuse by terrorist organisations’.

The regulatory strategy being suggested by the FATF is not a prohibition of all cross-border charitable activity, but rather active prevention, detection and remediation strategies. Following the FATF’s report, the ACNC has issued guidance and a checklist to assist charities to minimise the risk of being used for raising and distributing funds for terrorist financing, as well as a factsheet for overseas aid and development charities. In July 2015, the ACNC held sector briefings for charities, discussing the obligations associated with sending funds overseas.

While the FATF focused its criticisms on the ACNC, the ATO is also responsible (and before the ACNC, was solely responsible) for non-profits’ tax compliance. Even with the regulatory strategy of flat prohibition on tax concessions for cross-border giving (with limited exceptions to minimise ongoing supervisory expenses), the ATO has been found wanting in its oversight and monitoring of DGRs. The Australian National Audit Office (‘ANAO’) conducted an independent performance audit of the ATO’s administration of DGRs immediately prior to the establishment of the ACNC and found that the ATO faced a number of challenges in assessing the extent to which organisations complied with the requirements of DGR status. The main challenges were associated with the limited resources available to assess properly the compliance risks associated

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208 Ibid 6.
209 Ibid 145–6. It is interesting to note that the focus of criticism was the ACNC, rather than the ATO. This is particularly surprising given that the current Australian Government has expressed its desire to disband the ACNC and make the ATO responsible for the regulation of all non-profits: Australian Charities and Not-for-profits Commission (Repeal) (No 1) Bill 2014.
210 Ibid 16.
211 ACNC, Protecting Your Charity against the Risk of Terrorism Financing <www.acnc.gov.au/ACNC/Manage/Protect/ProtectingTF/ACNC/Edu/ProtectTF.aspx>.
with the sector and to undertake an appropriate level of post-endorsement compliance reviews and audits.\textsuperscript{214} Because there was no requirement for most DGRs to report regularly to the ATO, it had very limited internal information on which to assess the compliance risk.\textsuperscript{215} The report concluded that ‘[t]he management of this risk is not commensurate with its assessed level of potential non-compliance’.\textsuperscript{216} The signs are not encouraging for any increased oversight by the ATO of cross-border activities of Australian non-profit organisations in the future. The Government’s 2014 budget announced staff reductions of 4700 from the ATO’s workforce of 25 000 by 2017–18.\textsuperscript{217} With proposed reductions in ATO budget and staff, it is not known what resources the ATO will have to monitor cross-border charity.

XI Recommendations

The legislative architecture in Australia adopted for the regulation of cross-border charity reflects a broader policy of imposing a flat prohibition on tax concessions for cross-border charitable activities, mitigated by special exemptions with high entry barriers. Accordingly, only certain classes of organisations that have been subjected to initial heavy vetting can engage in tax-effective cross-border charity. This limits Australian donors seeking to obtain a tax deduction for donations directed overseas to making gifts through organisations that have succeeded in obtaining DGR status under one of the very limited exceptions. If enacted, the proposed ‘in Australia’ reforms will further tighten the laws surrounding Australian cross-border charity and philanthropy, with stricter ‘in Australia’ tests for both income tax exemption and gift deductibility. The formal policy reasons proffered for the ‘in Australia’ measures are to prevent leakage from the fisc, and to counter tax abuse and terrorist financing. From the available evidence, however, currently there appears to be only minor leakage from the fisc, with limited evidence of the floodgates opening, and a relatively low tax abuse risk profile.

With national boundaries around philanthropy starting to blur, the continued legitimacy of a domestic tax policy that restricts the ability of organisations and their donors to engage in tax-effective cross-border charity is called into question. If the Australian Government ultimately decides to change policy course with respect to the tax relief provided for cross-border donations, we propose reforming the Australian tax regime governing cross-border philanthropy through three measures described below.

\textsuperscript{214} ANAO, above n 88, 20–21 [24].
\textsuperscript{215} Ibid 27 [48].
\textsuperscript{216} Ibid 21 [25].
A Improving Data Collection and Measurement of Cross-border Philanthropic Flows

Understanding the current level of cross-border philanthropy in Australia is foundational for informing policy development because it would provide a data source for measuring the extent of Australian cross-border philanthropy and its associated costs, both direct and indirect. There is some evidence of Australian non-profit organisations being involved in cross-border charitable activities and indications that Australian cross-border giving has been steadily increasing. However, the lack of reliable data on charitable giving, which is exacerbated when attempting to collect and disaggregate data on international giving, means that the amount of philanthropic funds flowing out of Australia and how much of this outflow is classified as tax-deductible donations is unknown. The result is that the Australian Government has no way of measuring the revenue impact of the deduction for cross-border donations, which calls into question its assumption that removing a deduction for cross-border gifts would result in significantly more tax revenue. Further empirical research is needed in this area, including the most appropriate mechanisms for improving data collection around Australian cross-border charitable giving.

As a first step to reform, statistics should be kept that provide an accurate and reliable data source for measuring the amount of the charitable tax expenditures, including those for cross-border philanthropy. This would inform policy development and provide a basis for audit activity, as recommended by a parliamentary committee several decades ago. It would also enable the Australian Government to provide the OECD with more accurate annual estimates of private philanthropic flows to developing countries, along with its official aid data. The ACNC’s AIS provides a basis for the collection of such data for registered charities, although more information on cross-border activities and donations would need to be included in these statements. The annual published ATO statistics could also include cross-border data, which would require non-profits to file annual audited financial statements with the ATO, similar to private and public ancillary funds. With this information, the Australian Tax Expenditures Statement could include specific estimates of the tax expenditures for the deduction for cross-border donations under a new line item ‘deduction for cross-border gifts to DGRs’.

B Establishing an Appropriate Supervisory Framework for Monitoring Cross-border Giving

Regulation is much more than law on the books, and what actually happens in practice can be very revealing. The ‘in Australia’ requirements for DGRs contained in the tax laws and their proposed reforms are only effective if adequate regulatory supervision and enforcement mechanisms are in place. Both the FATF report on Australia’s anti-money laundering and counter-terrorist financing measures and the ANAO audit of DGR regulation identified failures on the part of the authorities to provide appropriate supervision and scrutiny of Australian

218 See Follow the Yellow Brick Road, above n 33, 55–6 [4.21]–[4.25].
non-profit organisations operating overseas, leaving these organisations susceptible to non-compliance and misuse. To reduce some of these vulnerabilities, the tracing provisions contained in the Government’s reform proposals have targeted the opportunistic channelling of donations overseas by organisations with cross-border DGR status. These tracing provisions may persuade some of the organisations currently hosting intermediary giving arrangements for a fee to reconsider their practices. However, without effective ongoing supervision of the hosting organisations, an equally plausible outcome is that the use of these channelling arrangements will continue to flourish as the only means available for many Australian non-profit organisations and their donors to engage in tax-effective cross-border charitable activities.

Addressing the need for an appropriate regulatory framework for charities operating overseas is critical. This requires a coordinated policy response from the relevant bodies and government departments, with one of these bodies undertaking a primary supervisory role. As the independent charity regulator, the ACNC appears best placed to provide much of the necessary supervision. Ideally, registration with the ACNC would automatically entitle a charity to receive DGR status, which would streamline the process of becoming a DGR by obviating the need for separate DGR endorsement by the ATO. The ACNC could undertake responsibility for ongoing monitoring through its AIS, which, as noted above, would need to be modified to obtain more comprehensive information on charities involved overseas and their financing. Further oversight could be provided through the development and implementation of the ACNC’s external conduct standards for regulating charities sending funds or engaging in activities overseas. These regulatory mechanisms would serve to mitigate the risks of charities being used for tax abuse purposes and terrorist financing, and reduce the use of channelling workarounds, providing greater transparency and accountability. The ATO could provide assistance to the ACNC through its auditing capabilities, with AUSTRAC providing additional oversight of cross-border transactions.

The ACNC could also be central to the counter-terrorism investigatory and enforcement process, identifying charities that may be at risk of being involved in terrorist financing and issuing detailed guidance on charities and terrorism. This would require the ACNC being properly resourced to undertake these functions. It may also involve enacting legislation to strengthen the ACNC’s regulatory powers to support the work of AUSTRAC and other law enforcement agencies.

C Amending the Tax Legislation Applicable to the Tax Deductibility of Cross-border Donations

With few options for engaging in tax-effective overseas giving, many Australian non-profit organisations and their donors have resorted to using channelling workarounds, creating a system of cross-border philanthropy that is complicated, inefficient, inequitable and non-transparent. At the same time, this system makes monitoring cross-border fund flows far more difficult for the authorities, increasing

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219 Productivity Commission, above n 36, 177, 184.
220 See ACNC, External Conduct Standards, above n 77 and accompanying text.
the risks that these funds may be used for tax abuse and terrorist financing purposes, and making their impact on the fisc harder to assess.

A better approach would be to have a general rule of allowing Australian charities operating overseas to obtain DGR status and removing the categories of exceptions, in conjunction with increased ongoing monitoring and supervision, making all Australian charities operating overseas subject to the same legal and administrative requirements. This would require the ATO to issue a new taxation ruling — consistent with its updated taxation guide and the decision in Word Investments — clarifying the meaning of ‘in Australia’ in div 30 of the ITAA 1997 as requiring that a DGR be established and operate in Australia (but not that its purposes and beneficiaries be in Australia). At the same time, Treasury could synchronise the ‘in Australia’ tests for DGRs and ITEEs through legislative amendment, which would reduce complexity, particularly given that many tax-exempt organisations operate DGR funds. While the extra effort by the regulatory authorities would not be without short-term administrative costs, in the long term this approach is likely to result in greater transparency of cross-border charitable activities and to enhance Australia’s tax abuse risk profile.

An alternative approach would be to remove the ‘in Australia’ requirement for DGRs altogether, making donations made directly to foreign charities fully deductible for Australian taxpayers. This may seem radical for Australia — in that it would require significant legislative amendments to div 30 of the ITAA 1997 to provide for the equal tax treatment of domestic and cross-border donations. However, there are safeguards that could be put in place to ensure that that the tenets underlying the ‘in Australia’ requirements are respected. These could include a requirement that foreign charities must register with the ACNC in order to obtain Australian charity status, subjecting these charities to the ACNC’s annual reporting requirements (modified to include more information on charitable activities abroad) as well as the ACNC’s external conduct standards (if developed and implemented).

XII Conclusion

Globalisation has created a world where people are financially and socially more interconnected that ever before. In the 21st century this interconnectedness has extended to philanthropy, with charitable gifts increasingly crossing national borders. Australia offers a tax deduction to encourage philanthropy, making charitable gifts less expensive for donors than they would be otherwise. However, due to concerns relating to the fiscal consequences of extending tax concessions to cross-border donations and the ability to regulate charitable funding expended overseas, Australia has placed territorial barriers around this charitable tax relief. As a result, Australia is considered to have one of the strictest legal regimes among OECD countries for the tax treatment of cross-border philanthropy.

As globalisation proceeds at an even faster pace, Australia will increasingly suffer the indirect costs of a restrictive policy that may well outweigh the direct tax expenditure costs. Legal and regulatory reforms could be made to minimise the cost and inconvenience to organisations and their donors who wish to engage in
overseas charity, while still achieving many of the outcomes driving the ‘in Australia’ reforms. The current legal and regulatory strategy of a flat prohibition on tax-effective cross-border charitable activities, with few exceptions, combined with limited ongoing supervision will neither satisfy international benchmarks nor provide long-term benefit for the Australian community. A change in approach would enable the Australian Government to solve the quandary it currently faces of maintaining the appropriate balance between protecting the interest of the fiscal state, while enabling its citizens to contribute fully and effectively to philanthropy’s globalisation.