

14 January 2009

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

Dear Sir/Madam

**Improving the integrity of Prescribed Private Funds (PPFs) – Discussion Paper**

Thank you for the opportunity to make the attached submission in response to your Discussion Paper. We have entered our comments (*highlighted in red*) in the spaces provided in the document itself. (Please note: We have limited the pages to those numbered 1 to 17. The hard copy is being sent to you today).

We at CAF Australia appreciate your initiative and accept the need for improved processes and increased regulation of PPFs. All measures that achieve simplification and certainty in their administration are most welcome.

In our role as the administrator of a number of PPFs with diverse philanthropic objectives, it has been pleasing to witness first-hand the contribution they are making to our community sector. Given that they have been established to operate long term, once the current financial crisis has settled, we feel confident they will grow and increase their already significant contributions.

Please know that we are keen to work with you on this important project. We would be more than happy to provide further feedback and assistance if needed.

You can contact the writer, Marlene MacFarlane, on 02 9929 9633 or on 0418 252 217 at anytime.

Yours sincerely



Marlene MacFarlane  
National Manager Foundation Services  
Phone: 02 9929 9633  
Mobile: 0418 252 217  
Email: [mmacfarlane@cafaustralia.org.au](mailto:mmacfarlane@cafaustralia.org.au)



**Australian Government**

---

**The Treasury**

# **Improving the integrity of Prescribed Private Funds (PPFs)**

Discussion Paper

**(Response by CAF Australia)**

The Treasury

November 2008

# IMPROVING THE INTEGRITY OF PRESCRIBED PRIVATE FUNDS (PPFs)

## INTRODUCTION

1. The Treasurer announced in the 2008 Budget that the Government will legislate guidelines to improve the integrity of Prescribed Private Funds (PPFs) and to provide the trustees of PPFs with greater certainty as to their philanthropic obligations. This commitment is to be achieved by amending and legislating the PPF guidelines to, among other things, ensure regular valuation of assets at market rates and increase the size of compulsory distributions. The Commissioner of Taxation will also be given greater regulatory powers.
2. This Discussion Paper outlines these changes, and provides a point of reference for public submissions on this measure. This measure will have effect from 1 July 2009. A link to the current PPF Guidelines, and Model Trust Deed is at *Appendix A*.
3. The Government intends that the new PPF Guidelines will be drafted using a principles based approach. The principles are outlined later in this discussion paper, and are the Government's views on the essential characteristics of a PPF.
4. It remains a fundamental concept that a PPF is a trust to which businesses, families and individuals can make tax deductible donations, for the purpose of disbursing funds to a range of deductible gift recipients and a PPF cannot distribute to another PPF or to a public ancillary fund.

## PPFs IN CONTEXT

5. PPFs came about as a response to a report on philanthropy in Australia by the Business and Community Partnerships Working Group on Taxation Reform dated 26 March 1999. PPFs are a form of ancillary trust fund designed to encourage private philanthropy by providing private groups, such as businesses, families and individuals, with greater flexibility to start their own trust funds for philanthropic purposes. Donations to PPFs are tax deductible. PPFs are limited to making distributions to other deductible gift recipients (DGRs) that either have been endorsed by the Australian Taxation Office (ATO), or are listed by name in the income tax law as a DGR. A PPF may be entitled to an income tax exemption if it is also endorsed as a charity, or endorsed as an 'income tax exempt fund'.
6. A PPF is one of two types of ancillary trust fund<sup>1</sup> that can qualify for DGR status, and income tax exempt status. The other type is a public ancillary fund (PAF), which is

---

<sup>1</sup> A fund (as distinct from an institution) is a pool, stock or store of assets. A trust is a fiduciary relationship in which one person (the trustee) holds the title to property (the trust estate or trust property) for the benefit of another (the beneficiary). Accordingly, a trust fund comprises trust property (such as securities, cash or other assets) that is merely managed under such a relationship.

distinct from a PPF in that it must establish a public fund<sup>2</sup>. Public ancillary funds are a common structure for community and fundraising foundations. Both types of ancillary fund act only as intermediaries between donors and organisations that can receive tax deductible donations.

7. With the exception that they need not seek and receive contributions from the public, and control requirements, PPFs have the same characteristics as PAFs and accordingly must comply with all the other requirements of a public fund.
8. The current PPF Guidelines outline the process to be followed, and requirements to be met, in order to establish a PPF, including the requirement to establish a trust in accordance with a model trust deed. The current Guidelines are unlegislated and therefore have no legal status in their own right.

## **AREAS FOR IMPROVEMENT IN THE CURRENT ARRANGEMENTS FOR PPFs**

9. The current PPF Guidelines outline the requirements for PPFs in some detail, but not necessarily the objectives of those requirements. Furthermore, in cases of PPFs misusing their funds (for example, providing benefits to the donor) there is currently an 'all or nothing' penalty system. The ATO is generally limited to advising the Treasurer to declare that a particular organisation is no longer a PPF. De-listing of a PPF does not affect the deductions that have already been claimed, nor enable the protection of the PPF's philanthropic funds in the future.
10. This Budget measure to improve PPF integrity will be achieved by:
  - amending the PPF Guidelines to, among other things, ensure regular valuation of assets at market rates and increase the size of compulsory distributions;
  - legislating the PPF Guidelines; and
  - giving the ATO greater regulatory powers.
11. At present, the Treasurer is responsible for prescribing funds as PPFs. To further improve the integrity of PPFs, the Government proposes to bring the full administration of the PPF regime under the authority of the Commissioner of Taxation. This means that PPFs would no longer be 'prescribed' in the relevant legal sense but instead be endorsed by the Commissioner. Conceptually, PPFs are a private version of a PAF, and the ATO already has systems and processes by which PAFs are endorsed, reviewed and administered and these processes can be extended to the administration of PPFs. The Commissioner of Taxation would be made responsible for endorsing and dis-endorsing PPFs, instead of the Treasurer being required to prescribe such funds as PPFs. This would have the effect of giving the ATO full regulatory control over PPFs and allow the ATO to take more timely action to protect the capital of a PPF. ATO

---

<sup>2</sup> Public funds are bound by a number of requirements (set out in Australian Taxation Office Taxation Ruling 5/27). A fund is a public fund where: it is the intention of the promoters or founders that the public will contribute to the fund; the public, or a significant part of it, does in fact contribute to the fund; and the public participates in the administration of the fund. These requirements are intended to ensure that moneys and property donated to the fund, and which attract a taxation concession, are used for the purpose for which the fund has been granted DGR status.

endorsement of PPFs would be reviewable by the Administrative Appeals Tribunal, consistent with other endorsement rules.

12. As such, Prescribed Private Funds may need to be renamed as ‘Private Ancillary Funds’. However, for the remainder of this discussion paper we will continue to use the term PPF.

**PARAGRAPHS 9 to 12    AGREED**

**PRINCIPLES UNDERPINNING THE RULES GOVERNING PPFs**

13. The Government intends that the PPF Guidelines be amended to articulate the principles which will apply to PPFs. This should assist both the trustees and the ATO in understanding the requirements for PPFs. The four principles below outline the Government’s views on what the essential characteristics of a PPF should be:

<b>Principles</b>	
1. PPFs are philanthropic	<p>PPFs are vehicles for acts of philanthropy by donors, and benefit from significant tax concessions on that basis. The distributions of PPFs should therefore be of a quantity and regularity such that the PPF can be characterised as philanthropic. Donors to PPFs, and their associates, should not benefit from their PPFs.</p> <p>PPFs should provide a benefit to the charitable sector that is much more than if the Government had taken the revenue forgone (by way of PPF tax concessions) and given it directly to that sector.</p>
2. PPFs are trusts that: (1) abide by all relevant laws and obligations, and (2) are open, transparent and accountable	<p>PPFs provide money and other assets (that have been donated to the trust fund) to non-ancillary DGRs, and PPF trustees are bound by state trust laws<sup>3</sup>.</p> <p>In setting out to achieve philanthropic goals, PPFs must abide by all relevant laws. The Commissioner will take appropriate action against the trustees of PPFs that do not abide by the rules.</p>
3. PPFs are private	<p>PPFs have been established as a vehicle to encourage private philanthropy. This is in contrast to PAFs, which collect donations from the public. This characteristic necessarily limits who can donate to a PPF.</p>
4. PPFs are ancillary funds	<p>The purpose of a PPF is to assist in the management of money as it is transferred from the donor to non-ancillary DGRs. PPFs are unsuitable for undertaking charitable work in their own right as this would make them ‘institutions’ which are subject to a different regulatory environment.</p>

---

<sup>3</sup> Trustees are subject to both the common law principles of trust law and the relevant Trustee Act of their State or Territory (see paragraphs 44-46 of the PPF Guidelines).

## PROPOSED AMENDMENTS RELATING TO THE PRINCIPLES

14. The Government will amend and legislate the PPF Guidelines. The following section is a more detailed outline of the Government's proposed amendments to the current Guidelines.

### Principle 1 — PPFs are philanthropic

15. The changes proposed under this principle relate to: required distributions; regular valuation of assets at market rates; minimum PPF size; and increased public accountability.

#### 1a Required distributions

16. PPFs should be philanthropic. Transfers by PPFs should therefore be of a regularity and quantity such that the fund is characterised as philanthropic. PPFs should neither be prolonged accumulators of funds, nor sparse distributors of funds.
17. The Government's Budget commitment to increase the size of compulsory distributions by PPFs will be achieved by clarifying the minimum standard of philanthropic behaviour among PPFs. In doing this the Government will give certainty to PPF trustees as to their philanthropic obligations, and also to members of the wider community that PPFs are distributing adequate amounts for them to be characterised as philanthropic.
18. Improvements that could be made to the accumulation and distribution rules governing PPFs in the current Guidelines should be considered ahead of the importance of certain variables in determining the minimum distribution rate (see a summary of the rules at *Appendix B*). The distribution behaviour of PPFs is currently structured according to an accumulation plan, which determines the limits of a PPF's accumulation phase before it moves into its distribution phase. However, the Government is aware that the use of individual accumulation plans makes for a complex system, resulting in PPFs being treated unequally depending upon their designated capital accumulation target<sup>4</sup>.
19. To simplify the current system, the Government proposes to replace accumulation plans with a system that would simply require PPFs to distribute a minimum amount in a given year which is calculated based upon the value of the PPF's net assets at the close of the previous financial year. PPFs would value their assets annually at 30 June, and this 'closing value' would be used to calculate a minimum amount that must be completely distributed over the following 12 months (to the end of the following financial year). The calculated closing value would include all realised and unrealised capital gains. It is expected that these simpler arrangements would reduce the costs of PPF compliance and administration (as there would no longer be a need for individual accumulation plans) and improve certainty for PPF trustees.

---

4 The ATO has indicated that there can also be a degree of uncertainty about whether a trustee is required to distribute only a proportion of donations received, whether it is a proportion of donations and all income generated (less an allowance for CPI indexation of the target corpus) and whether realised or unrealised capital gains are to be included in the distribution calculation of the estimation of the corpus of the PPF.

20. Under these new arrangements, a distribution rate needs to be set that is of an adequate amount such that a PPF can be characterised as philanthropic. The Government intends to consider the following in determining the rate:
- Based on the available data, the ATO has estimated that the long-term proportion of PPF distributions as a percentage of the closing value of the fund is approximately 15 per cent.
  - PPFs should benefit the charitable sector more than if the Government had taken the revenue forgone (by way of PPF tax concessions<sup>5</sup>) and given it directly to the sector.
    - The majority of donors to PPFs are private individuals on the highest marginal tax rate (45 per cent<sup>6</sup>). As the Government effectively provides a subsidy of 45 cents for each dollar donated to a PPF, the Government expects that this revenue forgone will be directed to the charitable sector in a relatively short period of time.
  - Comparable charitable vehicles, such as PAFs, are usually expected to distribute all of their income and gifts in the year that they are received. In some circumstances PAFs have been allowed to accumulate up to 20 per cent of gifts received for a limited period of time.
  - Imposing a distribution rate means that PPFs not continuing to receive donations are eventually wound down. This will prevent the erosion of the fund through negative investments, fees and the like.
  - To maintain philanthropy during all market conditions, and to reduce complexity of administration, the Government considers that the Commissioner should not be given the authority to modify the minimum distribution amount according to market conditions (for example, share market performance).

---

5 PPFs can collect tax deductible donations. Most PPFs also get an income tax exemption and GST charity concessions when they are additionally endorsed as an income tax exempt charity or a tax concession charity.

6 Does not include 1.5 per cent Medicare Levy.

## Consultation questions

- What is an appropriate minimum distribution rate? Why?

Response: CAF supports the proposal contained in Paragraph 19. The concept of delivering equity in the treatment of all PPFs is fully endorsed. However, CAF believes that the annual minimum distribution rate of 15% proposed under Paragraph 20 is too high. Should this rate be applied, in the absence of replacement funds being donated annually, it is likely to have the effect of eroding the capital base of a PPF's fund within a relatively modest timeframe. This would result in a significant number of PPFs being wound up with the obvious consequences.

PPFs are commonly established by their Founders:

- (1) to create and build a culture of giving across the generations of their respective families/workforces/other private associations – in perpetuity; and
- (2) to provide a more efficient and structured way of giving capable of delivering long term support to their chosen charities and causes.

Given the vagaries of the market as has been very clearly demonstrated by the current global financial crisis, the proposed rate of 15% could prove “punitive”.

And going forward, there is every likelihood that the successors of the Founders/Trustees/major donors (commonly their children and grandchildren etc) of a significant number of PPFs will not generate the levels of income needed to make donations of a size that will allow their respective PPFs to remain sustainable. This would have an adverse effect on the continued development of Australia's philanthropic culture.

FURTHER – a rate of 15%:

- (a) would, over time, restrict the funds available to charities/DGRs. One of the great benefits that Foundations/PPFs offer to many vital community organisations is that they provide “reliable” and often substantial recurrent funding for essential charitable programs. The profound social outcomes that result cannot be underscored.

AND

- (b) is likely to operate as a disincentive to the establishment of new PPFs.

### CAF's RECOMMENDATION:

CAF proposes an annual distribution rate of 5%. 5% is a tried and proven number. We refer to the American experience where annual distribution rates of 5%-6% operate. Current evidence demonstrates that this rate delivers effective philanthropic participation while simultaneously satisfying governmental objectives.

- Should the Commissioner have the ability to modify the minimum amount according to market conditions (for example, based on average fund earnings)?

Response: No. Reduction in the complexity of administration and the provision of



certainty delivers real benefits.

- Should a lower distribution rate apply for a period (for example, 1-2 years) to allow newly established PPFs to build their corpus?

Response: No.

### **1b Regular valuation of assets at market rates**

21. PPFs are not bound by the current Guidelines to value their assets. The failure of PPFs to value assets leads to reduced distributions as some PPFs do not determine the value of unrealised capital gains, which the Guidelines say must be distributed if they are in excess of the approved capital base over any two consecutive financial years. The Government's Budget announcement included a commitment to ensure PPFs regularly value their assets at market rates. As discussed above, the Government proposes that PPFs value their assets annually on 30 June of each year, in order to calculate the rate of distribution.

#### **Consultation question**

- Are there any issues that the Government needs to consider in implementing the requirement to ensure PPFs regularly value their assets at market rates?

Response: CAF supports this proposal. The only issue is the cost of each annual revaluation. Before proceeding with this initiative, it is imperative that the ATO devises a universal format which "fixes" the costs of the revaluations at a reasonable level.

Considerations:

Could the ATO and AVO liaise to formulate a process capable of delivering concessional cost treatment?

For example, if we take the valuation of publicly listed shares. Given that their values are a matter of public record, perhaps the ATO could require the PPF's auditor to provide a "certificate" that he has verified the valuation of these shares. As for other asset categories, I feel sure a suitable procedure/formula can be devised that will give the ATO comfort while simultaneously not adding a cost burden to the administration of PPFs.

### **1c Minimum PPF size**

22. Noting that individuals can still make tax deductible donations directly to DGRs, the Government is considering whether a minimum PPF size (for example, \$500,000) should be established to ensure that the values of smaller PPFs are not eroded by operating expenses. As PPFs must be philanthropic, it would be considered inappropriate for a large proportion of a PPF's capital to be eroded through operating expenses.

## Consultation questions

- Is setting a minimum PPF size appropriate?

Response: In concept, this proposal has merit. The only shortfall occurs in the cases – and there are quite a few – where PPFs have been established to capture a substantial bequest or potential windfall.

### SAMPLE CASE STUDY:

- A PPF currently has a capital fund of approximately \$300,000. The Founder/Trustee is 80 years old. He has substantial assets tied up in property and shares, but needs the income during his lifetime to:
  - sustain himself; and
  - make donations to his PPF in compliance with the terms of his PPFs Capital Accumulation Plan.
- He proposes to leave a bequest of approximately \$5 million to his PPF. Under the current Guidelines, he will need to gain approval to the amendment of the Capital Accumulation Plan.
- If he has to wind up his PPF, he will doubtless change his Will and bequeath these assets to a Testamentary Charitable Trust. This action will have the result of limiting the extent to which the ATO will have supervision over the management and reporting of these assets – and indeed, the Trust. CAF believes that it is in the best interests of the sector to have ATO regulation and supervision of charitable structures – unless and until an Australian Charities Commission is established (which ideally would work in tandem/cooperation with the ATO).

- What should the minimum PPF size be in dollar terms?

Response: CAF would propose a minimum size of \$250,000.

- Should a fund have to distribute all its capital when its total value falls below this minimum amount?

Response: No. It should be given the following suggested (or other yet to be determined) options:

- Two (2) years within which to restore its capital base (while simultaneously being required to annually distribute 5% of the value of its fund) failing which it must then distribute all of its capital; or
- Provide satisfactory evidence to the ATO that the PPF should be maintained to capture a substantial bequest (The issue here is “timing”! – a delicate issue to raise with the intended Testator/Founder/Trustee); or
- Rollover the capital fund into a donor advised sub-fund administered by, for example, the CAF Community Fund, ANZ Trustees, JBWere or Perpetual. This is currently not permitted – and is a concept that will be addressed later.

## 1d Increased public accountability

23. As PPFs receive significant tax concessions akin to public funds, the public should be able to identify the PPFs and be satisfied that PPFs are operating in an acceptable and transparent manner. While the requirement to operate in an acceptable and transparent manner is addressed in other parts of this paper, the Government proposes that all PPFs will be required to have an ABN, and that all PPFs be recorded on the Australian Business Register along with an indication that they are a PPF. Existing Business Register privacy rules will continue to apply. The Government is also considering whether the contact details of PPFs should be provided publicly. This would allow charities seeking funding to make representations to PPFs.

### Consultation questions

- Are there any relevant issues that need to be considered in improving and standardising the public accountability of PPFs?

Response: The current arrangements are sound.

- Are there any concerns with the proposal to require that the contact details of PPFs be provided to the public? What information should be provided publicly?

Response: This is a difficult issue. CAF believes that PPFs are already accountable to the public via the ATO. The concern about providing PPF contact details relates to the costs that PPFs would incur in dealing with the influx of unsolicited enquiries and funding applications. Most PPFs have a set of preferred charities/charitable causes they wish to fund. Where extra information is required, they carry out their own research and/or approach selected organisations directly.

Similarly, we would see many charitable organisations dedicating valuable resources to making funding applications that are destined to fail.

In summary, the consensus of the PPFs CAF has consulted is that contact details should not be supplied.

## **Principle 2 — PPFs are trusts that: (1) abide by all relevant laws and obligations, and (2) are open, transparent and accountable**

24. The changes proposed under this principle relate to: giving the ATO greater regulatory powers; introducing a 'fit and proper person test' for trustees; and moving relevant provisions from the Model Trust Deed into the Guidelines.

### **2a Give the ATO greater regulatory powers**

25. PPFs are regulated throughout their lifecycle at both the state and Commonwealth level.

- An initial assessment occurs before a PPF is prescribed by the Government in the Income Tax Assessment Regulations 1997 (ITAR 1997)<sup>7</sup>.
- PPFs must also to comply with state trust law and other important rules and legislation<sup>8</sup>.
- In addition the ATO monitors PPFs on an ongoing basis to ensure they continue to meet the Guidelines. PPFs are required by the Guidelines to provide an annual return to the ATO, and this requirement is proposed to continue<sup>9</sup>.
- PPFs must also have their financial statements audited by a person registered under Part 9.2 of the *Corporations Act 2001* (clause 11.3 of the Model Trust Deed), and these reports are submitted as part of the return.

26. There are limited remedial responses available to the ATO if a trustee of a PPF fails to meet the ongoing requirements for the fund to be a PPF. Currently, a PPF found to be in breach of the Guidelines may be de-listed as a DGR<sup>10</sup>. Current practice is for the

---

7 The process to list a PPF in the Regulations is different to the way that general category DGRs (including PAFs) obtain their DGR status — which is by way of ATO endorsement. PPFs are listed in a three-stage process: (1) an initial assessment of prospective PPFs is undertaken by the ATO to determine whether a prospective PPF meets the requirements set out in the Guidelines; (2) the prospective PPF's application is then referred to the Government (via Treasury) for a decision to be made by the Minister responsible for tax law administration matters; and (3) PPFs that have been approved by the Minister are then prescribed as DGRs by being added to a list in the ITAR 1997, which is subject to disallowance by either House of Parliament.

8 The state Trustee Acts are broadly similar, but do have some variation: *Trustee Act 1898* (Tas); *Trustee Act 1907* (NT); *Trustee Act 1925* (NSW); *Trustee Act 1925* (ACT); *Trustee Act 1936* (SA); *Trustee Act 1958* (Vic); *Trustees Act 1962* (WA); and *Trusts Act 1973* (Qld). Other important rules and legislation include: The PPF Guidelines and Model Trust Deed; the *Income Tax Assessment Act 1997* and *Income Tax Assessment Act 1936*; the common law concept of fiduciary responsibility; and the law of equity concept of charitable purpose. Other legislation may also impact on PPFs depending on the structure and range of activities, including: registration under state Fundraising Acts (which in NSW, for instance, imposes additional reporting and audit requirements) for trusts that seek or receive gifts from the public; and the *Privacy Act 1988* (Cth).

9 The return requires PPFs to provide information such as: donations received; income and distributions of the fund; expenses of the fund (for example, management fees); book value and closing value; and change of details information.

10 The definition of PPF in the ITAA 1997 indicates that the Treasurer may declare (in writing) a fund not to be a PPF. As the current PPF guidelines are not legislated, decisions made by the Treasurer in exercising this power are subject to federal administrative law.

ATO to draw the Treasurer's attention to cases of flagrant or repeated breaches of the PPF Guidelines, as opposed to genuine mistakes or oversights. The ATO may also revoke a PPF's endorsement as an income tax exempt charity if: (1) the ATO considers that the PPF is no longer charitable; or (2) the PPF has not provided information or a relevant document within a time specified by the ATO.

27. A number of PPFs have been found to have breached the Guidelines. These breaches include: PPFs carrying on a business; PPFs making loans offshore and/or to associates of the founder or major donor (these loans are of particular concern when they are provided at a reduced or zero rate of interest or are not repaid); and PPF funds being used to purchase property for use by the founder or their associates (examples of property have included both residential and commercial real estate and motor vehicles).
28. The ATO is limited in the actions it can take against trustees or funds breaching the Guidelines, their Trust Deed, or other relevant laws. The current 'all or nothing' approach means the ATO is unable to always apply appropriately scaled penalties that suit the nature of the breach of the Guidelines or Trust Deed. In some cases this may mean the ATO does not take action against a PPF because the remedy would be considered too harsh. Further, the ATO is unable to take any action against trustees who inappropriately manage PPFs. Importantly, in the case of trustees mismanaging a PPF's funds, the ATO is unable to remedy the loss of funds.
29. In its Budget announcement, the Government stated its intention to give the ATO greater regulatory power. Such powers are necessary for the ATO given the significance of the tax concessions involved. There may be Constitutional limitations on giving the ATO power to further regulate PPFs. However, these limitations could be overcome by requiring PPFs to have a corporate trustee.
30. It is considered that the extra costs incurred for shifting to a system requiring corporate trustees would be far outweighed by the ATO's enhanced ability to take action against PPFs that mismanage their funds, thereby satisfying the public that the PPF concession does not pose a problem to the integrity of the tax system. Corporate trustees are relatively popular in the self-managed superannuation fund sector, and the average assets of self managed super funds are lower than for PPFs.
31. It is proposed that a number of transitional rules be used to bring existing PPFs under the new Guidelines; for example, providing a transitional period of two years whereby existing PPFs can use the current Guidelines until they are brought under the new Guidelines.
32. A sample of 129 existing PPFs revealed that 84 per cent already had corporate trustees.

### Consultation questions

Response: CAF does not support a mandatory requirement for a corporate trustee - particularly in family based PPFs where there is an appropriate succession plan in place.

- Will two years be a long enough transitional period for existing PPFs to comply fully with the new Guidelines?

Response: If this proposal can be legally supported, then Yes, two (2) years is adequate.

- Are there any cost or other concerns relating to the corporate trustee proposal?

Response: Yes.

Firstly, higher ASIC fees apply to a corporate trustee of a PPF than to a corporate trustee of a self managed superannuation fund.

Secondly, there may be a number of different "trustee groups" that may wish to be represented separately - either individually or by a corporate entity.

33. As the responsibilities of PPFs are split between their tax obligations and their other trust obligations, the ATO may also be provided with powers (through new secrecy disclosure provisions and information gathering provisions) to make enquiries of relevant state or territory bodies and to disclose relevant information to state or territory attorneys-general. For example, these powers may be necessary where the ATO is concerned that a trustee of a PPF has misused PPF funds, or may otherwise be in breach of the relevant state or territory legislation governing trusts.

### Consultation question

- Are there any privacy concerns that the Government needs to consider?

Response: The ATO should legislate these powers in its favour.

34. The Government intends to allow the ATO to respond proportionately to misuse of PPFs by providing it with access to a wider range of penalties. It is considered that scaled penalties that suit a breach will enable the ATO to appropriately address the behaviour of the relevant party. For example, in the case of inappropriate behaviour of trustees, the penalty could include either leaving the assets of the fund intact, or requiring restitution.

35. The range of penalties could include: enforceable undertakings; fines; restitution; removal/disqualification of the trustee; winding up; and criminal, civil or administrative penalties.

### Consultation question

- Are there any concerns over particular penalty types?

Response: No - the only rider being that "the penalty should fit the crime".

## 2b Introduce fit and proper person test for trustees

36. The ATO has found that not for profit organisations generally 'show a strong desire to get it right, but often have a low level of knowledge about how the tax and superannuation systems work. Where compliance issues arise, they are mainly due to mistakes or a lack of knowledge.'<sup>11</sup>
37. The qualifications and skills of a PPF's trustees affect not only whether a PPF meets its legal obligations, but also the essential philanthropic character of a PPF. The Government is of the view that those trusted with running PPFs should be qualified for the position, and thus proposes considering qualifications for PPF trustees.
38. The Government also recognises that not all trustees of PPFs are professional trustees, and that imposing training or other qualification standards may restrict the number of people eligible and/or willing to take on the role of trustee<sup>12</sup>.
39. Certain trustees are already required to meet stricter requirements, such as trustees covered by the Superannuation Industry (Supervision) Act 1993. In addition, tax agents must meet certain criteria to be considered a fit and proper person. The respective criteria for these fit and proper person tests are outlined in *Appendix C*.

---

11 ATO Compliance Program 2008-09 page 63,  
[http://www.ato.gov.au/content/downloads/COR\\_0015516\\_CP0809.pdf](http://www.ato.gov.au/content/downloads/COR_0015516_CP0809.pdf).

12 The word 'trustee' in this context also extends to the directors of a corporate trustee.

## Consultation question re introduction of a Fit and Proper Person Test for Trustees

CAF agrees with the content of Paragraph 36.

CAF also believes that not all of the trustees of a PPF should be required to meet the “Fit and Proper Person Test” contained in Appendix C. The reasons are as follows:

(1) While many Founders/Trustees of a PPF would meet all of the criteria, there are those who have achieved financial success and have all of the personal attributes BUT NOT the technical qualifications etc mentioned in Clause (4)(b).

(2) Some Trustees may be friends, relatives – or more commonly – children of the Founder/Trustees who have not yet had an opportunity to acquire the required qualifications but who still have the wherewithal to make valuable contributions to the operations of the PPF.

HOWEVER, CAF recommends that the requirement for a Responsible Person on the governing body of the PPF should remain. CAF believes that the Responsible Person should be required to meet ALL of the criteria set out in Appendix C. Further, the Responsible Person should be the individual made primarily accountable for the oversight and proper administration of the PPF. There should be a positive obligation on the Responsible Person to ensure that the PPF meets all of its obligations. In addition to the annual audit, CAF suggests that the Annual Information Return include a provision for a Certificate by the Responsible Person to the effect that the operations of the PPF have been conducted in compliance with ATO regulations/guidelines.

Ideally the ATO – or a suitably qualified ATO auspiced organisation – should provide an obligatory Certificate Course that must be passed by all Responsible Persons before assuming the role. Attendance at Update Courses – in a similar format to the CLE courses run by the State Law Societies – should also be obligatory.

- If a fit and proper person test were introduced, what criteria should be imposed on trustees?

Response: Please see above

### 2c Move relevant provisions from Model Trust Deed into the Guidelines

40. It is intended that certain requirements of the existing Model Trust Deed be moved into the updated Guidelines. Doing so will give the rules the force of law. It is intended that there then would be no binding model deed, however the ATO may provide a model deed to assist new PPFs.

41. Notable clauses currently found in the Model Trust Deed include:

- prohibition of benefit to the trustee (including any of its members or directors), the donor/founder or any associate, including uncommercial transactions (clause 5 in the Model Trust Deed); and
- auditing requirements (clause 11.3 in the Model Trust Deed).



### Consultation questions

- Are there any other provisions presently in the Model Trust Deed that should be covered in the updated Guidelines?
- Are there any provisions not in the Deed that should be in the updated Guidelines?

Response: Beyond the inclusion of the “Fit and Proper Person” criteria, the existing Deed works well. Also, uniformity in the structure and content of the Deed provides benefits to all concerned.

### Principle 3 — PPFs are private

42. The change proposed under this principle relates to limiting the number of PPF donors.

#### 3a Limit the number of PPF donors

43. PPFs have been established as a vehicle to encourage private philanthropy. This characteristic implies that there is a *close relationship* between those who establish and those who donate to the fund, and is reflected in the Guidelines, which do not require a public fund to be maintained by a PPF.
44. It is intended to keep the current requirement that public donations cannot be the primary source of PPF donations. Those wishing to seek donations from a larger group (for example, large companies) should use another fund structure, such as a PAF, as soliciting tax deductible public donations requires a different level of regulation which is not provided by the PPF framework.
45. If a PPF's circumstances change (for examples, donor numbers exceed the limit), it is proposed that the rules provide a mechanism for conversion of a PPF to a PAF.

## Consultation questions

- Would there be any disadvantages if a cap were introduced on the number of donors to a PPF (for example, a maximum of 20 donors over the life of the fund)?

Response: Yes. Some PPF Founders/Trustees have numerous family members, friends, business contacts and acquaintances (that can all be properly categorised as “private” in accordance with the PPF Guidelines) that may wish to share their philanthropic experience through donating to the PPF. Also, the majority of PPFs have been established to operate in perpetuity. Such a limitation would restrict the effective long term operation of PPFs.

- Is conversion from PPF to PAF an acceptable mechanism to deal with changing PPF circumstances?

Response: **ABSOLUTELY.** This is a sorely needed structural reform. CAF contends that it should be possible for a PPF to be rolled over into a donor advised sub-fund – and vice versa.

- What rules could be used to deal with the conversion from a PPF to a PAF?

Recommended rules:

- Modest costs – preferably no costs – should be payable by the PPF to the PAF on rollover.
- Post-rollover, the former PPF Founder’s/Trustee’s grant making policy and recommendation’s should be considered by the Trustees of the PAF.
- Otherwise, the regime is already very well defined and well regulated.

### EXTRA CONSIDERATION

CAF believes it would also be a progressive step to allow a donor advised sub-fund to be rolled over into a PPF where the circumstances properly support the changeover.

## Principle 4 — PPFs are ancillary funds

46. The change proposed under this principle relates to restricting PPF investment to only liquid assets.

### 4a Restrict PPF investment to only liquid assets

47. Notwithstanding the investment requirements imposed upon trustees by various state trust Acts, PPFs should have sufficient liquid assets to meet their philanthropic obligations. Illiquid assets donated to or held by a PPF should be converted to liquid form as soon as practicable if they are likely to affect a PPF’s ability to meet its philanthropic obligations. This change would have the advantage of ensuring that donations can be quickly distributed. Furthermore, the value of liquid assets is generally easier (and therefore cheaper) to determine and verify.

**Consultation question**

- Would there be any disadvantages from introducing this limitation to the existing PPF investment rules?

Response: From the perspective of ease of administration, CAF substantially agrees that the majority - preferably all - of a PPF's investments should be held in liquid assets. However, in light of the impact of the current global financial crisis, CAF recommends that we continue to rely on the prudent person principles that apply to the investment of assets held and managed by Trustees (which require adequate diversification).