

9 December 2011

Manager
Philanthropy and Exemptions Unit
The Treasury
Langton Crescent
PARKES ACT 2600

By email: nfpreform@treasury.gov.au

Dear Sir/Madam

A Definition of Charity: Submission from nine Victorian Public Health Services and Public Hospitals

I attach a submission from nine Victorian public health services and public hospitals in response to your Consultation Paper "*A Definition of Charity*".

The public health services and public hospitals in Victoria have suffered significant financial loss by the removal of their charitable status following the review by the Board of Taxation in 2003. This has resulted in millions of dollars in lost revenue from private charitable trusts and corporate donors. These entities would have continued to donate had the health services been able to retain their charitable status or some other legislative mechanism was put in place to enable them to continue to donate to public health services and public hospitals.

The Commonwealth and Victorian governments have had to shoulder a greater financial burden to fund the health services as a result of the loss of these private donations. We can only assume this was an unintended consequence of the review.

The health services would welcome the opportunity to give oral evidence in support of their submission.

Yours faithfully



**Bill O'Shea
General Counsel
Alfred Health**

for and on behalf of:

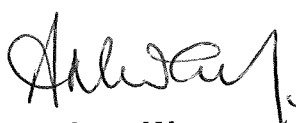
**Alfred Health
Melbourne Health
Austin Health
Eastern Health
The Royal Women's Hospital
Peninsula Health
Peter MacCallum Cancer Institute
Barwon Health
Western District Health Service**

Submission to Philanthropy and Exemptions Unit The Treasury

Consultation paper on the definition of charity

Submission from the following Victorian public health services
and public hospitals:

Alfred Health
Melbourne Health
Peninsula Health
Eastern Health
Austin Health
The Royal Women's Hospital
Peter MacCallum Cancer Institute
Barwon Health
Western District Health Service



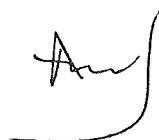
Andrew Way
Chief Executive
Alfred Health



A/Prof Alex Cockram
Acting Chief Executive
Melbourne Health



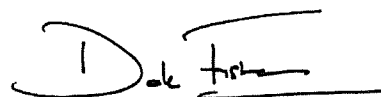
Dr Sherene Devanesen
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Peninsula Health



Alan Lilly
Chief Executive
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Dr Brendan Murphy
Chief Executive
Austin Health



Dale Fisher
Chief Executive
The Royal Women's
Hospital



Craig Bennett
Chief Executive
Peter MacCallum
Cancer Institute



Jim Fletcher
Chief Executive
Western District
Health Service



Paul Cohen
Acting Chief Executive
Barwon Health

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Introduction

Alfred Health, Melbourne Health, Peninsula Health, Eastern Health, Austin Health, The Royal Women's Hospital, Peter MacCallum Cancer Institute, Barwon Health and Western District Health Service ("**Health Services**") are either public health services or public hospitals established under the *Health Services Act 1988* (Vic).

They comprise the hospitals treating the majority of public patients in Victoria.

As a result of changes made to Australia's income tax legislation following a review of charities by the Board of Taxation in 2003 ("**Review**"), the Health Services (and in fact all public health services and public hospitals in Victoria) have lost their charitable status.

The Health Services are regarded by the Australian Taxation Office ("**ATO**") as a "government body" and therefore ineligible to fit the ATO's definition of a charity. This is despite the fact that they had enjoyed charitable status for many years prior to this decision being taken. It also ignores the fact that the Health Services as statutory bodies are separate legal persons in Victoria, unlike their counterparts interstate.

This change of charitable status has resulted in the Health Services being ineligible for donations from private organisations that are restricted to donating only to entities regarded as charitable by the ATO.

In particular, private testamentary trusts are affected and can no longer make donations to the Health Services. This change comes after these and other private charitable trusts have for many years provided millions of dollars in donations to the Health Services.

The decision to remove the charitable status of the Health Services has resulted in the unfortunate and unintended situation whereby the Commonwealth and the State of Victoria are forced to either make up the shortfall in private sector donations from public funds or see the Health Services deprived of this vital source of funding - surely neither outcome was intended by the review.

The Health Services welcome this opportunity to make a submission to the Treasury on a definition of charity. They see this as an opportunity to correct in the new legislation what appears to be the unintended consequences of the decision to abolish their charitable status.

Legislative history

In 2007, most public health services and public hospitals in Victoria received a letter from the ATO stating that because of the fact that they were "governmental" in nature, they were no longer entitled to an ATO endorsement that they were "an income tax exempt charitable entity" under Subdivision 50-B of the *Income Tax Assessment Act 1997* (Cth) ("**Tax Act**").

This ruling has caused problems for a number of private trusts which, under their terms, can only make donations to a "charity".

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This does not mean that public health services lost their deductible gift recipient (DGR) status. All donations to a public health service still remain tax deductible. However it means that a public health service can no longer produce a certificate from the ATO stating that it is a tax exempt charitable entity.

Some public health services in Victoria, including some of the Health Services, have established a foundation as a separate legal entity. These foundations have been given DGR status but they are regarded as category 2 charities and will not satisfy the requirement for a donation from a private charitable trust. A category 2 charity provides funds to a category 1 charity (the public health service) which actually carries out 'charitable works'. So establishing a separate legal entity does not solve the problem because category 2 charities are not regarded as 'charitable' under the Tax Act. Accordingly, many charitable trusts are not permitted by their trust deeds to make donations to them.

The result of this ruling by the ATO is that private charitable trusts put their own tax exempt charitable status at risk if they donate funds to a non-charitable entity. As well, the trustees could be personally liable for breach of trust if a donation were ever to be challenged and especially if the donated funds could not be returned. Thus private charitable trusts are refusing to continue making donations to public health services, fearing that as public health services do not have ATO charitable status, they could be putting their own tax exempt status (and the personal assets of trustees) at risk.

As well as charitable trusts, corporate donors with a policy of "donating to charity" are requiring the potential recipient to produce a certificate from the ATO stating that the entity is regarded by the ATO as a charity. Public health services in Victoria, including the Health Services, can no longer provide this certificate.

The apparent unintended consequence of the decision by the ATO to regularise the charitable status of public health services is that funds that were previously being donated to public health services by charitable trusts and the corporate sector are being diverted away from public health and given to entities with charitable status. The Commonwealth and the States are now faced with the problem of either making up the shortfall from this loss of donations from the private sector or seeing public health services deprived of these funds with no replacement. This was presumably not the intended outcome sought by the ATO when it decided to review the status of charitable entities in Australia.

The Victorian Government sought legal advice on how charitable trusts could continue donating to public health services in Victoria. It was advised to amend the *Charities Act 1978* (Vic) ("**Charities Act**") to allow private charitable trusts to opt into a scheme whereby if they give donations to a DGR entity which would be charitable but for being connected to government, this will not affect the status of the trust as a charitable trust. This has occurred with the enactment of s.7K.

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A number of charitable trusts have received legal advice that, despite the amendment to the Charities Act, opting in is in breach of their trust deeds. The reasons are that the trusts would be donating funds to an entity without an ATO certificate confirming its charitable status and that in any case, Commonwealth law (the Tax Act) overrides State law (the Charities Act).

Currently, the only trusts that can opt in to this new arrangement in Victoria are ancillary funds (category 2 charities) or prescribed private funds. Thus, whilst the amendment to the Charities Act has been a laudable initiative, it has limitations:

- it only applies to private charitable trusts based in Victoria;
- not all private charitable trusts will opt in: they cannot be forced to do so and some trustees remain nervous that if this was somehow struck down in the future, their trusts' charitable status could be jeopardised as well as the personal assets of trustees;
- it does not allow private charitable trusts to donate to a category 2 charity (such as a separately incorporated public health service foundation) because private charitable trusts are category 2 (i.e. 'funders' not 'doers') and they are restricted to donating to category 1 charities (the 'doers');
- it does not assist with the perception problem that public health services cannot produce an ATO certificate stating they are income tax exempt charitable entities;
- it is of no use to corporations who still ask for the ATO charity certification as proof that an entity is a charity.

Is a public health service a 'government body'?

Questions 14 and 15 in the Consultation Paper ask:

- whether further clarification is required in the definition of the types of legal entity which can be used to operate a charity; and
- whether the existing definition of 'government body' in the *Charities Bill 2003* ("**Charities Bill**") is adequate.

The Health Services in Victoria are separate legal entities established as bodies corporate by the *Health Services Act 1988 (Vic)*. Unlike their counterpart health services in other states, they are not part of a government department. However, the Victorian Minister for Health does retain the power to appoint and dismiss the Board of every Victorian public health service. On one view it could be argued that this power means that in effect, public health services in Victoria are 'government bodies'.

The Health Services submit that the Commonwealth should reconsider the definition of 'government body' in the case of public health services in

Australia. In particular, public health services in Victoria established by statute should be exempt from the definition of 'government bodies' at least for the purposes of being entitled to an ATO endorsement as an income tax exempt charitable entity. Despite the power afforded to the Victorian Minister for Health to appoint and dismiss the board, each public health service is a separate legal entity with the right to hold and dispose of property, enter contracts and sue and be sued in its own name. In fact, it is legally possible for public health services in Victoria to sue the Victorian government given their separate legal status. This seems inconsistent with a public health service being a 'government body'.

It is open to the Commonwealth to exempt all Australian public health services from the definition of 'government body' in the Charities Bill. It is also open to the Commonwealth to deem them to be charities for the purpose of receiving donations and other benefits from donors, including private charitable trusts.

A proposed solution

The Health Services submit that the best solution is an appropriate legislative amendment. This could be done in at least two ways:

1. the Tax Act could be amended such that public hospitals in Australia are deemed to be charities for the sole purpose of receiving donations and other benefits from donors; or
2. the proposed new statutory definition of 'charity' in the Charities Bill include a provision that public hospitals in Australia are charities for the sole purpose of receiving donations and other benefits from donors.

Either approach would put the charitable status of public health services in Australia beyond doubt. As a safeguard, if the 'charity' definition is limited to the receipt of donations, it would not open any 'floodgates' for the ATO. This solution would reasonably be expected to result in substantial private source funding being once again available to public health services. It would also result in Commonwealth and state governments not having to make up the shortfall in lost funding.