

SouthEast
Housing Co-operative

Housing Futures

Progressive Concessions

**Response to Re:Think Tax Discussion Paper
(March 2015)**

29 May 2015

PO Box 7141
Dandenong VIC
Australia 3175
T (03) 9706 8005
F (03) 9706 8558
www.sehc.org.au
Housing futures
ABN 51 286 919 868



Co-operative
enterprises build
a better world



SouthEast
Housing Co-operative
Housing Futures

The role of progressive taxes is to reduce the taxes of people with a lower ability-to-pay and shift the incidence increasingly to those with a higher ability-to-pay. The opposite of a progressive tax is a regressive tax - the relative tax rate or burden decreases as an individual's ability to pay increases.

Progressive taxes also apply to adjustments of the tax base by using tax exemptions, tax credits, or selective taxation that creates progressive distribution effects e.g. tax concessions available in Australia to the not-for-profit sector.

SouthEast Co-operative Housing Ltd benefits from tax concessions because our role is to create progressive distribution effects through providing affordable, secure, financially and environmentally sustainable housing for people on low incomes in the south east of Melbourne who want to be part of housing co-operative. We manage 160 properties for 440 people with future growth options under consideration. With tax concessions, SouthEast is financially viable total assets as at end of 30 June 2014 - \$4,458,879 an annual turnover for year ended 30 June 2014: \$1,757,270 and an operational surplus at 30 June 2014 of \$412,374

The removal of these tax concessions would be regressive and have a consequential impact on our ability to increase and improve housing services to people on low incomes.

The future focus on taxes, therefore, should be to improve and extend progressive taxes and not, instead, extend regressive taxation.

Chapter 7 Not-for-profit sector of **Re: Think Tax Discussion Paper** (March 2015) provides an overview of the not-for-profit (NFP) sector in Australia and the tax concessions available to different types of NFP organisations

There is recognising of the wider benefits of NFP activity (particularly where an NFP provides services that for-profit private sector organisations do not), these tax concessions arguably help to both improve societal outcomes and ensure that the overall level of activity in the NFP sector is closer to optimal. Notwithstanding this, it is important to assess their

PO Box 7141
Dandenong VIC
Australia 3175
T (03) 9706 8005
F (03) 9706 8558
www.sehc.org.au
Housing futures
ABN 51 286 919 868



Co-operative
enterprises build
a better world



SouthEast Housing Co-operative

Housing Futures

effectiveness to ensure that the concessions continue to meet their intended policy objectives, do not result in unintended consequences (such as high compliance costs or an uncompetitive advantage) and deliver the greatest possible community benefit. This is particularly important considering the revenue forgone as a result of these tax concessions. (p 124)

But, there is concern that NFP tax concessions result in significant revenue forgone. The two largest groups of tax concessions involve exemptions from paying fringe benefits tax (FBT) for public benevolent institutions (PBIs), health promotion charities (HPCs), public hospitals, non-profit hospitals, and public ambulance services; and income tax deductions for making gifts to DGRs. The (p 124) amount of revenue forgone from these concessions has been increasing, particularly the FBT exemptions. By 2017-18, the PBI concession is estimated to result in revenue forgone of nearly \$1.6 billion, from almost \$1 billion in 2010-11 (Chart 7.3). In comparison, the deduction for gifts to DGRs has remained relatively stable, increasing from nearly \$900 million in 2010-11 to almost \$1.2 billion in 2017-18. However, the actual revenue forgone from NFP concessions cannot be quantified because many organisations are not required to submit tax returns. This means that the actual revenue forgone is likely to be higher than is currently reported. (pp 124-125)

There is also the following concern: Given the size and reach of the NFP sector, some tax concessions may result in distortions that affect the broader allocation of resources in the economy, particularly where they operate in competition with for-profit providers. These distortions arise when the prices that NFPs pay for their inputs (such as labour) are altered by the presence of concessions in the tax legislation. (p 125)

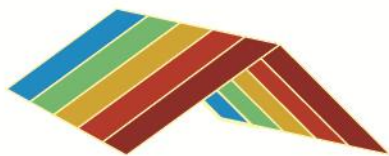
PO Box 7141
Dandenong VIC
Australia 3175
T (03) 9706 8005
F (03) 9706 8558
www.sehc.org.au

Housing futures

ABN 51 286 919 868



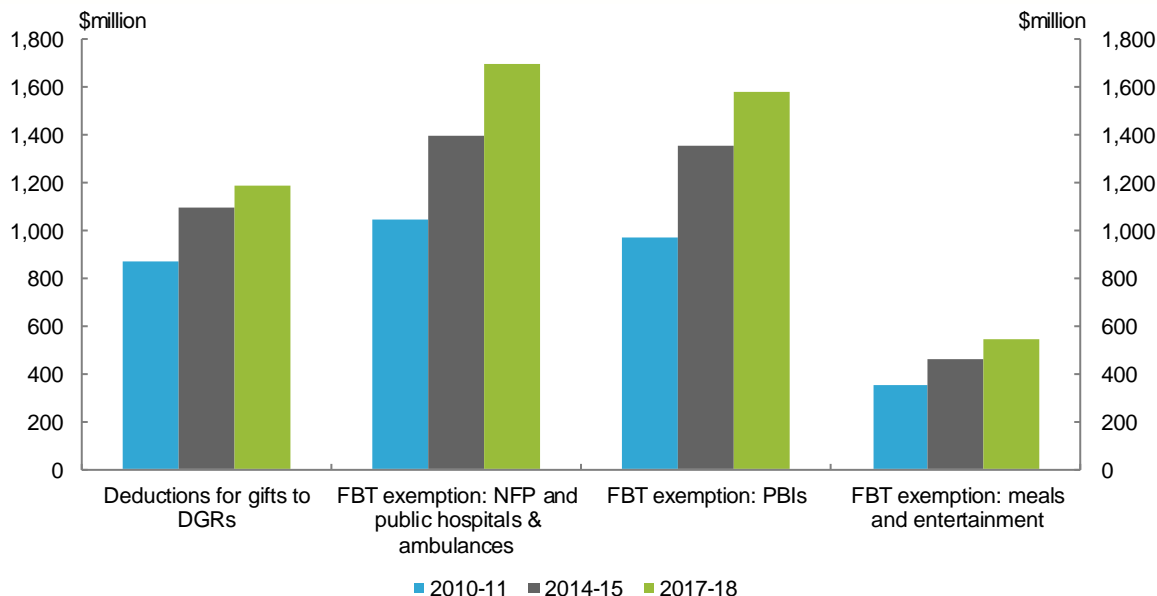
Co-operative
enterprises build
a better world



SouthEast Housing Co-operative

Housing Futures

Chart Error! No text of specified style in document..1 Estimated revenue forgone for selected Commonwealth tax concessions



Source: Australian Government 2015, *Tax Expenditures Statement 2014*, Australian Government, Canberra. (p 125)

Discussion questions:

Are the current tax arrangements for the NFP sector appropriate? Why or why not?

To what extent do the tax arrangements for the NFP sector raise particular concerns about competitive advantage compared to the tax arrangements for for-profit organisations?

What, if any, administrative arrangements could be simplified that would result in similar outcomes, but with reduced compliance costs?

What, if any, changes could be made to the current tax arrangements for the NFP sector that would enable the sector to deliver benefits to the Australian community more efficiently or effectively? (p 127)

It is puzzling that the tax discussion paper does not recognise the previous work undertaken by the Not-for-profit Sector Tax Concession Group Final Report (May 2013) and Australia's Future Tax System report to the Treasurer (December 2009). Why? Brief extracts follow:

PO Box 7141
Dandenong VIC
Australia 3175
T (03) 9706 8005
F (03) 9706 8558
www.sehc.org.au

Housing futures

ABN 51 286 919 868



Co-operative
enterprises build
a better world



SouthEast Housing Co-operative

Housing Futures

Not-for-profit Sector Tax Concession Working Group Final Report (May 2013)

The Not-for-profit (NFP) Sector Tax Concession Working Group (the Working Group) was established in February 2012 by the then Assistant Treasurer, Senator the Hon Mark Arbib. The Terms of Reference asked the Working Group to consider whether there are fairer, simpler and more effective ways of delivering the current envelope of support provided through tax concessions to the NFP sector.

Introduction

The Government provides an exemption from income tax for various NFP entities (p 6). In the absence of an exemption, charities and other NFPs would be subject to tax on their incomes. This would include income from businesses, income from investments (for example, rent, interest and dividends) and capital gains, but usually not gifts.

The income tax exemption is typically provided to charities and other entities that undertake purposes that are broadly beneficial to the community. Charities are NFPs that have a sole purpose that is charitable, for example:

- the relief of poverty or sickness or the needs of the aged;
- the advancement of religion;
- the advancement of education;

the provision of child care services; or other purposes beneficial to the community (p 7).

The provision of DGR status under Division 30 of the ITAA 1997 is the primary tax concession that promotes philanthropic giving to eligible entities. That status generally enables taxpayers to claim an income tax deduction for cash gifts made to such entities of \$2 or more, or property gifts valued by the ATO at more than \$5,000 (p 22). The tax deductibility of gifts in Australia at the Commonwealth level was introduced in the *Income Tax Assessment Act 1915*.

In 2010-11 around 4.8 million taxpayers claimed a deduction for gifts to DGRs, and donated around \$2.1 billion (p 26). The gift deduction concession was estimated to cost government around \$1 billion in the 2011-12 financial year and is estimated to cost approximately \$1.1 billion in the 2012-13 financial year, with the deduction for gifts to private ancillary funds (PAFs) and public ancillary funds (PuAFs) costing another \$135 million (p 27).

PO Box 7141
Dandenong VIC
Australia 3175
T (03) 9706 8005
F (03) 9706 8558
www.sehc.org.au

Housing futures

ABN 51 286 919 868



Co-operative
enterprises build
a better world



SouthEast

Housing Co-operative

Housing Futures

Eligibility for DGR status

It is clear that participants in the NFP sector, and the broader public, see the DGR framework as a crucial support for philanthropic giving in Australia. DGR status is highly valued and the gift deduction is seen as a significant concession which provides an incentive for donors to give. The submissions on the DGR framework in the Discussion Paper were numerous and often detailed, demonstrating the level of interest in the community in the way the tax system encourages and supports philanthropic activity in our society. The Working Group supports the continuation of the DGR framework as the primary way to encourage philanthropy.

Australia's future tax system Report to the Treasurer December 2009

The Australian Government has released the [final report](#) of the Australia's Future Tax System Review. Since being established in 2008, the Panel provided many opportunities for people to make a submission and engaged with the community through public meetings and focus groups, meetings with representative business and community groups, discussions with other government departments and agencies, and through its tax and transfer policy conference held in June 2009.

Not-for-profit (NFP) organisations make a highly valued contribution to community wellbeing in the areas of community and welfare service, religion, education, sport and recreation, environmental protection and animal welfare. The defining feature of NFP organisations is that they are constituted to distribute surpluses in accordance with their objectives, and are precluded from returning profits or surplus assets to members. (p 205)

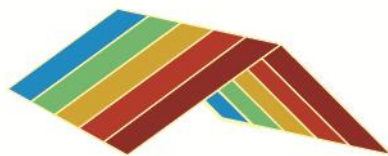
NFP organisations receive government and community support for their activities, in recognition that:

- NFP organisations supply goods and services with broad public benefits that may not otherwise be provided by private businesses. These benefits may be direct (such as providing legal advice to the homeless) or indirect (such as organising community sporting activities).
- NFP organisations are often more effective service providers than government or for-profit organisations, given their unique relationship with the community. An increasing number of traditionally government activities are being outsourced to NFP organisations.
- The activities of NFP organisations often supplement, or complement, existing government programs.

PO Box 7141
Dandenong VIC
Australia 3175
T (03) 9706 8005
F (03) 9706 8558
www.sehc.org.au
Housing futures
ABN 51 286 919 868



Co-operative
enterprises build
a better world



SouthEast
Housing Co-operative
Housing Futures

Much of the support provided to the NFP sector is delivered through tax concessions. These concessions are an important and longstanding source of financial support for the NFP sector, and assist NFP organisations to further their philanthropic activities and objectives. (p 206)
The tax concessions available to NFP organisations include income tax exemptions, a higher GST registration threshold, the ability to make supplies GST-free in certain circumstances,

GST input credits, capped exemptions from (or rebates of) fringe benefits tax (FBT), and the ability to receive tax deductible gifts (see Table B3–1). Not all NFP organisations receive all concessions — generally the concessions depend on the particular public benefit purposes of the organisation. (p 206)

Some submissions have expressed concern that income tax concessions may undermine the efficient allocation of economic resources. Economic theory provides a conceptual framework for assessing these concerns through Samuelson’s invariant valuations theorem (see Box B3–1). The application of the theorem relies on a range of assumptions, including that NFP organisations seek to maximise profits. Although this may not be true of all NFP organisations, it is a reasonable assumption given their purposes. In practice, the provision of tax concessions to NFP organisations is likely to result in an over-allocation of resources to the NFP sector. However, this bias is offset to some extent by the fact that the philanthropic activities undertaken by NFP organisations provide public benefits. (p 208)

Samuelson’s invariant valuations theorem (1964) provides a conceptual framework for assessing the impact of the income tax exemption for NFP organisations on resource allocation. The application of the theorem to NFP organisations assumes that these organisations seek to maximise profits in the same way as other businesses; however, this may not be true of all NFP organisations. The theorem states that where taxable income is the same as economic income, the discounted present value of a stream of cash flows is independent of the tax rate.

In other words, the maximum amount that an individual is prepared to pay for an asset is independent of the tax rate. Consequently, a tax on economic income will not create arbitrage opportunities between taxpayers on different rates and will not affect either relative or absolute asset values. Accordingly, it will not distort the composition or level of investment in the economy.

PO Box 7141
Dandenong VIC
Australia 3175
T (03) 9706 8005
F (03) 9706 8558
www.sehc.org.au
Housing futures
ABN 51 286 919 868



Co-operative
enterprises build
a better world



SouthEast Housing Co-operative

Housing Futures

Thus, providing that economic income is taxed, the existence of concessional tax NFP organisations should not distort asset allocation (or the level of investment) in the economy. However, as the current income tax base differs considerably from economic income, and as the tax concessions for NFP organisations are linked to particular activities regarded as providing a public benefit, the concessions are likely to distort investment decisions. However, to the extent that the concessions address a market failure (that is, the under-provision of social services), they may still increase wellbeing.

In relation to pricing, NFP organisations, like for-profit organisations, will seek to maximise their profits in support of their philanthropic activities. Accordingly, it appears that the income tax exemption does not provide an incentive for NFP organisations to undercut the prices of their for-profit competitors; rather, NFP organisations follow the same pricing policies as their competitors to maximise their profits.

Finding

The NFP income tax concessions do not generally violate the principle of competitive neutrality where NFP organisations operate in commercial markets. (p 209)

PO Box 7141
Dandenong VIC
Australia 3175
T (03) 9706 8005
F (03) 9706 8558
www.sehc.org.au
Housing futures
ABN 51 286 919 868



Co-operative
enterprises build
a better world