

Post implementation Review

Statutory Definition of Charity

What problem was the regulation meant to solve?

Prior to the introduction of the legal definition of a charity in 2014, no definition existed in Australian legislation. The meaning of charity and charitable purpose was largely administered on the basis of principles derived from common law, going as far back to the Statute of Elizabeth of 1601. This resulted in considerable confusion around the definition of charity for legal professionals, regulators and prospective charitable organisations. Rather than being able to refer to clearly defined legislation these stakeholders were forced to rely on common law interpretations and complex tax rulings from the Australian Taxation Office (ATO).

This lack of clarity caused a number of related problems including:

- Uncertainty for charitable organisations;
- Difficulty registering charitable status;
- Lack of clarity for a regulator;
- Increased likelihood of legal challenges; and
- Lack of platform for harmonisation across jurisdictions.

The introduction of the statutory definition was intended to preserve the existing common law definition with some minor modifications to provide greater clarity and certainty about the organisations which could be classified as charities. This would support charities and the community by making the definition easily understandable rather than stakeholders needing to rely on an understanding of the common law or complex tax rulings from the ATO.

Uncertainty

Without a legislative definition of charity, both charitable organisations themselves and those that support charitable organisations, were operating in an uncertain environment.

This uncertainty existed in part because new case law could change the definition of charity without direction from legislators. The statutory definition was intended to reduce uncertainty and to give Parliament the ability to more easily alter the definition over time to ensure that it remains appropriate, rather than having the common law interpreted by the courts as a result of legal challenges.

Difficulty registering charitable status

Charitable status is important for the Australian not-for-profit sector as it serves as the gateway to a range of tax concessions. To set up a charity prior to the introduction of the definition, organisations were required to prove to the ATO that they met the definition of a charity. Around 2,500 organisations register as charities each year.

The lack of clarity prior to the definition made it difficult for some organisations to register their charitable status without the need to seek professional legal advice. One stakeholder has estimated that legal costs to register a charity would be in the range of \$2,000 to \$5,000

on average. The complexity of the common law and ATO tax rulings made it difficult for a lay person to find and interpret the information they needed to prove charitable status. The introduction of a statutory definition was intended to make this information clearer and easily accessible to reduce the costs associated with registration.

Lack of clarity for a regulator

Prior to the introduction of the Australian Charities and Not-for-profits Commission (ACNC) and the suite of legislation to support the ACNC, including the Statutory Definition of Charity (Definition of Charity), there was a regulatory failure in the market. There was no body that was responsible for regulation of the charity and NFP sector. In effect the ATO acted as a de facto 'regulator' in determining which NFPs qualified for charitable status but did not proactively regulate charities once registered. This was detrimental to the sector as it opened up the opportunity for organisations to exist and operate under a charity or not-for-profit (NFP) umbrella but not be subject to regulation or compliance.

The statutory definition was intended to provide the ACNC with clear legislation which it could use to carry out its regulatory activities and provide interpretations to further clarify the definition. While the definition itself was not directly intended to address regulatory failure it was seen as an important tool for the regulator.

Increased likelihood of legal challenges

In instances where organisations were denied charitable status by the ATO and wished to challenge the ruling, the courts were needed to resolve the disputes imposing costs on charitable organisations and government. For example a High Court decision in the *Aid/Watch* case was needed to clarify the amount of political advocacy a charity can engage in. The introduction of the statutory definition was intended to help avoid these disputes by increasing clarity around the definition.

Lack of platform for harmonisation across jurisdictions

There was also dissatisfaction with the processes (and costs) associated with organisations needing to navigate different sets of regulatory requirements to register as charities across Australia's various jurisdictions. It was envisioned that a statutory definition at the Commonwealth level could act as a framework which could be adopted by Australia's states and territories over time.

Magnitude of the problem

When the statutory definition was introduced there were around 54,000 charities registered with the ACNC. In addition, there were several thousand NFP entities that were in operation but did not meet the definition of a charity. From 2013-14 to 2014-15 about 5,500 new charities have been registered by the ACNC. This presents a population significant enough that the lack of a clear definition of charity needed to be addressed.

Why was government action needed?

As outlined above, the meaning of charity and charitable purpose had not been comprehensively defined for the purposes of Commonwealth law; rather the meaning had largely been determined from the common law.

The common law meaning has developed over 400 years, largely based on the Preamble to the Statute of Charitable Uses (known as the Statute of Elizabeth), enacted by the English Parliament in 1601. Charitable purposes are commonly categorised (following the terminology of the *Commissioners for Special Purposes of Income Tax v Pemsel* [1891-1894] All ER Rep 28 (Pemsel case)) as the four 'heads of charity':

- the relief of poverty;
- the advancement of education;
- the advancement of religion; and
- other purposes beneficial to the community.

For a purpose to be charitable within the technical legal meaning of charitable under the common law (which overlaps but does not fully coincide with the popular or dictionary meaning), the purpose must be 'within the spirit and intendment' of the Statute of Elizabeth, and for the public benefit.

The development of the definition of charity and charitable purpose through case law based on the spirit and intendment of the Statute of Elizabeth has resulted in charity law that is in some areas unclear, inconsistent, or does not adequately address matters relevant to the contemporary Australian charity sector.

Clear definitions were needed in the sector to bring a shared understanding and provide legislative certainty for charities to operate in.

In addition to the above issues, a number of reviews recommended the introduction of a statutory definition of charity.

2001 Inquiry into the Definition of Charities and Related Organisations

The Inquiry into the Definition of Charities and Related Organisations was a response to legal disputes arising from the common law definition of charity and dissatisfaction with the process of determining charitable status.

The inquiry considered ways to improve the clarity and consistency of Australian Government definitions of charities and related organisations, and recommended the adoption of a statutory definition codifying, clarifying and correcting the common law meaning of charity. It also recommended the establishment of either an independent administrative body to administer the definition of charity, or a permanent advisory body for the ATO.

2003 Board of Taxation report into the Definition of Charity

In 2003, the then Treasurer requested that the Board of Taxation conduct a public consultation on draft legislation which included a legislative definition of a charity.

The Board received a total of 267 written submissions as well as input via meetings with key charitable bodies and representative groups, and group discussions in all State and Territory capitals.

The Board's report, *Consultation on the Definition of a Charity: A report to the Treasurer*, was provided to the then Treasurer on 19 December 2003. The report made a number of technical recommendations for changes to the draft legislation, which was based on feedback received from stakeholders. The report was released publicly on 11 May 2004 when the then Government announced its response, in Treasurer's Press Release No. 31 of 2004.

The Treasurer's Press Release outlined that the Government had taken advice from the Board of Taxation that the draft legislation did not achieve the level of clarity and certainty that was intended, and they would not be proceeding with the draft legislation.

The Government decided instead to pass more limited legislation, the *Extension of Charitable Purposes Act 2004 (Cth)*, which clarified the definition of charity in the cases of NFP child care, self-help groups and closed or contemplative religious orders.

2010 Productivity Commission report - Contribution of the Not-for-profit Sector

Several years later, the 2010 Productivity Commission (PC) report, *Contribution of the Not-for-Profit Sector*, was released.

Submissions to the Productivity Commission indicated that there was "considerable confusion and inconsistency around the definition of charitable purposes" and "dissatisfaction with the processes (and costs) associated with NFPs gaining tax concession status at various jurisdictional levels."

The final report reaffirmed the conclusions of the 2001 Inquiry into the Definition of Charities and Related Organisations and recommended the introduction of a statutory definition of charity to reduce uncertainty for NFPs applying for charitable status.

What policy options were considered?

Making no change – the non-regulatory option

For some time the Government made no change to the definition of Charity, despite several reviews calling for change.

It was clear from the numerous reviews conducted on this issue and from consultation with stakeholders on the draft legalisation for the *Charities Act 2013* that without change the lack of definition would continue to result in confusion and potentially costly litigation.

The Government essentially tested a no change option for many years (while the common law definition was utilised) and it was found to be ineffective.

Introducing a statutory definition

Due to the nature of the change the options were to introduce a definition or continue with the status quo; there were no other policy options to explore. The no definition option was considered to be unsustainable by stakeholders, meaning the only other option was to define the terms charity and charitable purpose.

Definition options

As can be noted from the previous sections, there is a long history of the Government considering change to the NFP legislation, including defining the term ‘charity’. The various reviews and reports included significant stakeholder consultation and advice from prominent policy experts, which were used to draft the eventual legislation.

Treasury consulted on the definition in 2011, looking particularly at the 2003 draft definition and also considered recommendations made by the Board of Taxation in its review of the ED of the Charities Bill 2003. Key issues in drafting the definition included whether there should be an explicit public benefit test; the level of political advocacy a charity can engage in; clarification around the types of entities that can be a charity; and the list of charitable purposes beyond the common law.

Introduction of the statutory definition

In 2011, the then Minister for Financial Services and Superannuation, announced that the Government would be establishing the ACNC from 1 July 2012, and in conjunction, introduce legislation for the Statutory Definition of Charity from 1 July 2013, among other relevant charity and NFP legislation.

At the time, the Minister stated "The adoption of a consistent definition of charity and single determination of charitable status will greatly assist the sector" and "the current definition of charity is based on over 400 years of common law and is complex, inconsistent between Australian jurisdictions, outdated and creates considerable uncertainty for the sector".

The purpose of the statutory definition was to clarify the common law, not to broaden or narrow the types of entities that would be defined as charities. As such, existing charities under the common law remained so under the statutory definition.

The ACNC was created in 2012, and the Charities Act 2013, where the definition of a charity is found, received Royal Assent on 28 June 2013. The definition was introduced at or around the same time as several other pieces of legislation supporting the charity and not-for-profit sector (the NFP sector). The ACNC was considered necessary as the NFP sector was largely unregulated and unguided by either a central body or by legislation.

The introduction of the above legislation provided a legal framework for charities and NFPs to follow, and a holistic approach for the monitoring of the NFP sector through the ACNC.

Objectives of the Charities Act 2013

Prior to introduction of the *Charities Act 2013*, the Government conducted public consultation on the draft legislation and extensive consultation with the NFP sector on the development of the definition.

The explanatory memorandum outlines the following points:

- The statutory definition is intended to provide greater clarity and certainty for charities, the public and regulators in determining whether an entity is charitable and consequently reduce the need for costly litigation.
- The statutory definition provides a framework for considering charity and charitable purposes. However, the definition retains the flexibility inherent in the common law that enables the courts, as well as Parliament, to continue to develop and extend the definition to other charitable purposes beneficial and relevant to contemporary Australia within the statutory framework. This will ensure that the definition remains appropriate and reflects modern society and community needs as they evolve.

- The statutory definition applies to all Commonwealth legislation. It may provide a common framework which States and Territories may adopt over time, thereby further reducing complexity and compliance costs for Australian charities.

The ACNC Commissioner has predominant responsibility for administering this definition through the *Australian Charities and Not-for-profits Commission Act 2012*.

Summary of the Charities Act 2013

The Charities Act affirmed that a charity must have charitable purposes that are for the public benefit. Any other purposes must be incidental or ancillary to, and in furtherance or in aid of, the charitable purposes. The Charities Act also requires a charity to:

- be not-for-profit
- not have a disqualifying purpose
- not be an individual, a political party or a government entity.

The Charities Act also affirms that a charity may advance public debate about a charitable purpose as an independent charitable purpose.

The introduction of the Charities Act increased the number of charity subtypes from seven to fourteen.

The statutory definition also extends the common law definition to include as charitable:

- rebuilding community assets following a natural disaster;
- entities which have native title property and payments and direct benefits to indigenous persons who are related as these entities may fail a public benefit test under the common law;
- funds that contribute to a charity-like government entity, and trusts that are subject to cy pres schemes.

What were the impacts of the regulation?

The *Charities Act 2013* was passed on 27 June 2013 and came into effect from 1 January 2014. As stated above, the intention of this legislation was to clarify the definition of charity but still maintain the flexibility of the existing common law definition. This section will examine the impact of the regulation against the previous status quo, which was no definition and a reliance on the common law.

Unanimously stakeholders have indicated that the introduction of a legislative definition has made a positive impact on the sector. While no negative impacts were identified, there are some additional areas of the law which stakeholders felt could be further clarified in the Act. Another common theme was that the impact of the definition itself is difficult to disentangle from the ACNC's administration of the Act and its role in helping charities to understand obligations through information, guidance, advice and other support.

Providing Clarity and Certainty

One of the stated goals of the *Charities Act 2013* is to increase clarity and certainty for charities, the public and regulators in determining whether an entity is charitable.

In particular the *Charities Act 2013* sought to more clearly define recognised charitable purposes.

Prior to the introduction of the statutory definition, charitable purposes were commonly categorised under the four heads of charity:

- the relief of poverty;
- the advancement of education;
- the advancement of religion; and
- other purposes beneficial to the community.

Over time the modern understanding of charity changed to cover activities outside of the traditional charitable activities such as arts and culture, environment, animal welfare and human rights. As the NFP sector in Australia has become more diverse a large number of charities fell into the 'other purposes beneficial to the community'. Due to the vagary of this definition, it was difficult to easily understand what might, and might not, be classified as a charitable purpose.

The *Charities Act 2013* provided more clarity in this area by defining twelve recognised charitable purposes.

These are:

- purpose of advancing Health;
- purpose of advancing Education;

- purpose of advancing social or public welfare;
- purpose of advancing religion;
- purpose of advancing culture;
- purpose of promoting reconciliation, mutual respect and tolerance between groups of individuals that are in Australia;
- purpose of promoting or protecting human rights;
- purpose of advancing the security or safety of Australia or the Australian public;
- purpose of preventing or relieving the suffering of animals;
- purpose of advancing the natural environment;
- any other purpose beneficial to the general public that may reasonably be regarded as analogous to, or within the spirit of, any of the purposes mentioned in the subtypes above; and
- the purpose of promoting or opposing a change to any matter established by law, policy or practice in the Commonwealth, a State, a Territory or another country, if in the case of promoting a change – the change is in furtherance or in aid of one or more of the purposes mentioned above; or, if in the case of opposing a change – the change is in opposition to, or in hindrance of, one or more of the purposes mentioned in those paragraphs.

Making it easier to register charitable status

Stakeholder feedback indicates that the addition of new charitable purposes has fulfilled its intended purpose of providing additional clarity. This has made it easier for charitable organisations to easily identify their charitable purpose and register with the ACNC. Prior to the introduction of the *Charities Act 2013* and the ACNC, organisations were forced to rely on sources of information that were difficult to interpret and in some cases needed to seek professional legal advice. Stakeholders indicated that the *Charities Act 2013*, together with the creation of the ACNC, have been valuable tools in improving access to reliable information. The definitions role in improving access to information has made it easier for organisations to understand the sector and make informed decisions about whether to seek registration as a charity, without the need to procure legal advice.

This change has also assisted the ACNC to register new charities. In its 2013-14 annual report the ACNC states that “the introduction of the Charities Act provided further impetus for enhancing the online registration form, allowing charities to register their sub-type in a more accurate, user friendly and streamlined way”.

Providing clarity for the regulator

The ACNC was intended to enhance the clarity of the statutory definition of charity by acting as a body which would provide further guidance on interpretive issues. The legislation has been successful in providing a base from which the ACNC can make interpretation statements to further clarify the definition. The ACNC has indicated that the clarity provided by the *Charities Act 2013* has made these decision making processes easier and is preferable to relying entirely on the common law.

Thus far the ACNC has provided six interpretation statements to clarify areas such as the meaning of government entity, health promotion charities and the provision of housing by charities.

Effect on existing registered charities

The intent of the *Charities Act 2013* was largely to clarify the existing common law. That is, it was intended to clarify rather than redefine the existing law. For this reason, the statutory definition was not expected to cause issues during the transition to the new Act.

As a result of the introduction of the Charities Act, 34,570 charities had subtypes that required updating. The ACNC worked with registered charities to transfer them to the new subtypes created by the *Charities Act 2013*, where applicable, over an 18 month period. Stakeholder feedback has been that the impact of transitioning to the new legislation was minimal.

Maintaining the flexibility of the common law approach

A potential danger when attempting to define charity in legislation is that the definition would be too narrow or prescriptive, which would exclude what society might consider a worthy charitable organisation from obtaining charitable status.

However stakeholders have not identified any problems with charities being excluded under the new definition. The *Charities Act 2013* includes a 'catch all' provision which covers "any other purpose beneficial to the general public that may reasonably be regarded as analogous to, or within the spirit of, any of the purposes mentioned in the subtypes above". Stakeholders have found that so far this 'catch all' provision has been sufficient in maintaining flexibility while still allowing the *Charities Act 2013* to more clearly define some areas of charitable purpose.

The ACNC has demonstrated the flexibility to use a combination of the *Charities Act 2013* and the common law in making its determinations. For example, because providing community housing is not specifically identified as a charitable purpose in the *Charities Act 2013*, the ACNC used common law principles to determine if such activities could be considered charitable purposes. The ACNC released a Commissioner's Interpretation Statement: Provision of housing by charities on 11 December 2014, which found that the provision of housing may come within one or more of the purposes set out in the *Charities Act 2013* including the purpose of advancing health, the purpose of advancing social or

public welfare and the 'catch all' provision which refers to any other purpose beneficial to the general public. The ACNC used the common law approach to determine that an organisation that was considered charitable in providing housing prior to the commencement of the *Charities Act 2013* remains charitable under the statutory definition.

Omissions from the definition

As noted in the previous section, the definition of charitable purpose has not added any additional uncertainty to areas of charity law or excluded worthwhile charities which were registered using the application of the common law. However, some stakeholders expressed the view that the *Charities Act 2013* could have gone further by clarifying other areas of the law and adding additional categories of charitable purposes.

Some stakeholders expressed the view that amateur sporting clubs should be added as a charitable purpose in the *Charities Act 2013*. Currently sporting and recreational organisations cannot be registered as charities unless their main purpose is charitable, such as providing sporting activities for the people with disabilities or the elderly. The provision of housing was also raised as an area that could have been specifically included in the definition of charitable purpose to provide further clarity on circumstances under which the activity can be considered to be charitable.

The *Charities Act 2013* could also have taken the opportunity to more clearly define what is meant by public benevolent institutions. These institutions receive the most generous tax concessions but are not mentioned in the Act.

Stakeholders also expressed the view that the definition of a government entity remains a difficult area of the law and would benefit from simplification. The *Charities Act 2013* states that a 'charity' cannot be a 'government entity' and attempted to give greater certainty about what is a government entity by stating the term has the same meaning as 'government entity' within the meaning of the *A New Tax System (Australian Business Number) Act 1999 (ABN Act)*. However, the question of what constitutes a government entity remains complicated and was clarified by a lengthy ACNC interpretation statement. In the ACNC's words, the interpretation statement "is highly technical, as the law is very complex in this area. It is likely to be primarily read by legal and other professionals, including professional advisers."

Harmonisation of state and federal laws

One of the intended benefits of the statutory definition was that it could provide a common framework which States and Territories could adopt over time, thereby further reducing complexity and compliance costs for Australian charities. Ideally, an entity could be assessed as being charitable for all purposes by a single agency such as the ACNC to avoid duplication.

Thus far, there has been no substantial progress towards harmonisation between state and federal laws. State rules remain different from the Commonwealth framework which means that charities need to meet both sets of requirements. Stakeholders indicated that the

increased clarity at the Commonwealth level was still beneficial even without harmonisation.

Stakeholders indicated that there is still potential for state rules to become more harmonised over time and that the *Charities Act 2013* provides a good framework for this process to occur. They noted that the definition of charity at the Commonwealth level does not preclude States and Territories from modifying the statutory definition to include carve outs according to their specific needs. The ACNC is working with the States and Territories to progress the matter.

The Regulation is still in its early stages

While stakeholders have indicated that the impact of the statutory definition has been positive, they have also cautioned that it is too early to fully evaluate the changes. New legislation needs time to be interpreted, and those interpretations tested in court, before the full effect of the legislation becomes clear. At this stage, there have been no judicial decisions since the introduction of the *Charities Act 2013* that can be used to clarify its impact.

The *Charities Act 2013* is still in the process of being interpreted by the ACNC, which is continuing to develop its approach to the statutory definition of charity as it makes registration decisions. The ACNC will continue to produce Commissioner's interpretation statements which cover how it understands the law. The ACNC also plans to review the charity register and produce a paper for public discussion on its findings. Reviewing segments of the register and making decisions on the status of registered charities could be a catalyst for legal action that would test and clarify the legislation. Until this process occurs, it is difficult to be certain about the impact of the *Charities Act 2013*.

A common view from stakeholders is that since the statutory definition appears to be working well thus far, there should be no rush to change it. Instead it would be more beneficial to allow the sector to settle and fully evaluate the changes at a later date.

Estimate of change in regulatory burden

Treasury estimates that the introduction of the statutory definition of charity has delivered a reduction in regulatory burden of around \$500,000 per annum.

Average annual regulatory burden (from business as usual)				
Change in costs (\$million)	Business	Community organisations	Individuals	Total change in costs
Total, by sector	-	-0.5	-	-0.5

In assessing the change in regulatory burden Treasury considered the following:

- Transition costs;
- The reduction in regulatory burden associated with improved clarity for organisations seeking to register as charities;
- Increased clarity for legal practitioners;
- The definition's role assisting the regulator; and
- The reduction in regulatory burden from shorter registration times.

Transition costs

As a result of the introduction of the Charities Act, 34,570 charities had subtypes that required updating, which was done over an 18 month period with assistance from the ACNC. Stakeholder feedback has been that the transition's effect on charities was minimal however it still involved some minor administrative costs. Transition costs were estimated at \$0.7 million of the annual regulatory burden.

Clarity for charities pursuing registration

Stakeholders have indicated that prospective charities now find it easier to access the information they need to register. This means they spend less time on the registration process and are less likely to need to seek legal advice. One stakeholder estimated that legal costs to register a charity would be in the range of \$2,000 to \$5,000 on average. Given about 5,000 new charities have been registered by the ACNC since the introduction of the definition a number of charities are likely to have been able to forego legal advice, avoiding the associated costs. Regulatory benefits from increased clarity have been estimated at \$1.2 million per annum.

Increased clarity for legal practitioners

Legal practitioners have indicated that the introduction of a statutory definition has clarified their understanding of the definition and assisted them in providing advice to clients. No data is available to estimate the quantum of this change. Treasury assesses this as a small unquantifiable reduction in regulatory burden.

Role in assisting the regulator

The ACNC has indicated that the ability to use the statutory definition as the basis for their decisions is preferable to relying on the common law alone. Having a clearer definition has made it easier for the ACNC to make decisions and fulfil its educative role by providing information to the public. Treasury assesses this as a small unquantifiable reduction in regulatory burden.

Shorter registration times

The introduction of the statutory definition of charity was part of a suite of changes including the transition of responsibility for evaluating and registering charities from the ATO to the ACNC. In the transition the ACNC also took on additional regulatory responsibilities, making it difficult to directly compare the two processes. Anecdotally the process has become significantly faster (in the order of 10-15 days), reducing the regulatory burden imposed on charities during the registration process. However, it is difficult to determine how much of this benefit to ascribe to the statutory definition versus the creation of the ACNC. For this reason Treasury assesses this as a small unquantifiable reduction in regulatory burden.

How was the regulation implemented and evaluated?

The statutory definition was introduced at or around the same time as several other pieces of legislation supporting the charity and not-for-profit sector, including the creation of the ACNC. The ACNC worked with registered charities to transfer them to the new charitable purpose subtypes created by the *Charities Act 2013*, where applicable, over an 18 month period.

As there is limited relevant data available on the NFP sector in Australia, this regulatory change was evaluated using targeted consultation with key stakeholders designed to reflect views from the various areas of the NFP sector.

Which stakeholders have been consulted?

Consultation with key stakeholders in the not-for-profit sector including from academia, law firms, community organisations and the ACNC, was undertaken between 26 February and 21 April 2016. The consultation involved holding meetings to discuss the impact of the statutory definition as well as follow up requests for further information on specific issues.

Has the regulation delivered a net benefit?

Based on the regulatory burden estimate and additional unquantifiable benefits identified during consultation with stakeholders, Treasury considers that the regulation has delivered a net benefit.

Stakeholders unanimously felt that the introduction of the statutory definition has been a positive change for the sector. No negative impacts of the change were identified, although some stakeholders felt that additional categories could have been included into the definition and that other areas relevant to the regulation of charities could be further clarified in legislation.

Stakeholders also agreed that a full evaluation of the changes would require more time because the sector is still in the process of adjusting to the changes. The full impact of the legislation will only be felt as the ACNC continues to interpret and apply the legislation. As this process takes place there are likely to be legal decisions which will further clarify any points of ambiguity.