
SPEECH NOTES

DATE: 31 OCTOBER 2014

SUBJECT: E SHALDERS SPEECH - UQ PRESENTATION

1. Introduction

Society can be divided into four sectors: business, government, civil society and the family.¹

Economists have developed theories to explain the role of civil society by reference to the first two sectors – business and government.² They are known as the three failures theory.

The three failures theory goes like this:

Business or the market is a sector comprised of people who act for private gain or i profit. It fails to provide public benefits.

Government meets this failure by providing public benefit, but association is compulsory (via taxation) and, therefore, subject to the will of the majority. Thus, some demands for public benefit remain unmet: usually the needs of minorities.

It may be that there are 'new' public goods. It may be that the public goods are very controversial. Or it may be that the size or quality of the public goods to be provided by government is in dispute.

The most common examples of these include private health care services, private education, and religion.

The third sector, also known as civil society or the not-for-profit sector, meets the failure of business and government to provide those public benefits.

It permits different and inconsistent social values to be pursued, and allows shared values to be pursued to a greater degree.³ It is through third sector organisations that minority or sectional interests can be pursued further without the rest of society being burdened with the cost of providing those public goods.⁴

My focus today is on this sector.

Churches and other faith-based or religious organisations form part of it, and the laws governing this sector have undergone a period of unprecedented change in recent years.

One of the changes is the introduction of a new government regulator that is tasked with maintaining public trust and confidence in the Sector.

The regulator is the Australian Charities and Not-for-profits Commission – known as the ACNC.

¹ Helmut Anheier, *Civil Society: Measurement, Evaluation, Policy* (2004).

² For an explanation of the three failures theory, see Richard Steinberg, 'Economic Theories of Nonprofit Organizations' in Walter W. Powell and Richard Steinberg (eds), *The Nonprofit Sector: A Research Handbook* (2nd ed, 2006).

³ James Douglas, *Why Charity?* (1983), 146.

⁴ James Douglas, *Why Charity?* (1983), 111-114.

To carry out its task effectively, the ACNC has been given considerable powers. These include the power to give directions to churches and other faith-based organisations registered with it, instigate investigations, and remove and replace the leadership.

The extent to which these powers are justified is a matter of debate. Today I am going to set out for you two competing arguments as to whether they are justified.

In short – one argument says, churches and organisations in the sector receive valuable tax concessions, and regulation is the price they pay for those concessions.

The alternative argument says that the concessions can be justified by the public benefit which the sector provides, and that the enforcement powers are an unwarranted restriction on freedom of religion and freedom of association.

I provide these arguments for your consideration at a time where there is a national debate about whether the ACNC should be retained in its present form, or abolished, or modified.

The present Government has pledged to abolish the ACNC, but Labor and the Greens are opposing those moves.

In that context I should be clear that this presentation will not provide you with an overview of that debate. That debate encompasses numerous issues which are beyond the scope of interest of this conference.

If you would like a balanced guide to that debate, I would direct you to the Moores submission to the Senate.⁵

I would also like to note at the outset that my comments about the ACNC are directed to the legislation establishing the ACNC, and not the way in which it is implemented by the present personnel employed by the ACNC. I know many of the ACNC personnel personally, and know they are committed to supporting the sector.

In so far as my comments extend to policy and theory behind the ACNC, they are my personal views, and only my personal views.

There are, on the table at the back, copies of my powerpoint presentation today with notes. In those notes are the references to the works of other academics that I have drawn from in today's presentation.

2. Overview

By way of overview:

I'll start by explaining the tax concessions available to the sector at the ACNC. And the ACNC, registration which is a prerequisite to obtaining those concessions.

I'll explain how the ACNC powers can be said to restrain freedom of association and freedom of religion, and then set out the two arguments as to whether they are justified.

3. Tax concessions

So, turning now to everyone's favourite topic at 2pm on a Friday – taxation law. Don't worry, my slides have lots of pictures.

⁵ See [Moores website](#).

There are a range of taxation concessions available to the third sector. Today I will focus on income tax exemption. That is, exemption from tax on the income that a Not for Profit receives, irrespective of whether it is from donations, government grants or investment activities.

Some tax concessions are only available to certain categories or types of organisations in the sector. But income tax exemption is available to a large proportion of the sector. For instance, sporting clubs and tourism associations along with others on the screen.

There are some preconditions which must be met for the organisations I have listed to qualify for income tax exemption.

However these preconditions vary between different types of organisations. They are not all treated the same. Some of them have to be registered with the ACNC.

ACNC

The ACNC is a Commonwealth government regulator of charities. Any organisation that would qualify for Commonwealth tax concessions as a charity must be registered with it as a precondition to eligibility.

Now – the word “charity” has a special meaning in this context.

In *Incorporated Council of Law Reporting for Qld v Federal Commissioner of Taxation*⁶, Justice Windeyer said that “charity is for law a concept of purpose, and a charitable institution is an instrument designed for carrying a charitable purpose into effect.”

Those purposes which are recognised as charitable have been developed by the common law over time. In 2013, the then Federal Labor Government set them out in legislation – the *Charities Act 2013*.

I’ve listed them on the screen. They are quite broad and include the advancement of religion, education, culture, and preventing or relieving the suffering of animals.

And there is an overarching requirement that the purpose be for the public benefit.⁷

So charity at law is much broader than the ordinary meaning, and includes any organisation established for the promotion of a particular religion.

That means any faith-based organisation that would qualify for Commonwealth tax concessions as a charity must be registered with the ACNC as a precondition to eligibility for those concessions.

Consequences of registration with the ACNC

The consequence of registering with the ACNC is that an organisation must be accountable to the government, and the broader public.

One of the ACNC objectives is to maintain, protect and enhance public trust and confidence in the Australian not-for-profit sector.⁸

⁶ *Incorporated Council of Law Reporting (Qld) v Federal Commissioner of Taxation* (1971) 125 CLR 659

⁷ s 5 *Charities Act 2013* (Cth).

⁸ s 15-5 of the *Australian Charities and Not-for-profits Commission Act* (Cth).

The ACNC facilitates this by requiring charities to provide information about their activities, operations and purpose, and then the ACNC publishes the information on its website.

The sort of information published includes:⁹

- who is responsible for governing the organisation;
- the rules by which the organisation operates
- what its activities are
- its income, sources of income, debts and other financial information;
- who it benefits
- how many employees and volunteers it has.

The ACNC also requires that organisations registered with it comply with the ACNC governance standards.

The ACNC governance standards are said to be minimum requirements for good governance¹⁰, and for the most part largely reflect other obligations at law. For example – one of the governance standards requires charities to use their assets for their purposes and prohibits them from distributing assets among their members.¹¹

However the ACNC governance standards also go further than some of the ordinary governance requirements you might expect. There is a requirement to disclose a *perceived* conflict of interest.

Now what is, or what is not, a perceived conflict of interest is highly subjective.

It is common for organisations to operate through different branches or arms or departments. For instance – some national bodies have separate entities to operate in Victoria. Some faith-based organisations separately incorporate their welfare or educational ministries. In my experience as a practitioner, it is in these sorts of contexts that a dispute over a perceived conflict of interest can arise.

ACNC powers

The relevance of the governance standards and the ACNC reporting obligations is that the ACNC has been considerable regulatory powers to ensure compliance.

The ACNC's enforcement powers include:

1. The power to give directions;¹² and
2. The power to suspend or remove and replace those in leadership.¹³

The power to give directions includes the power to require an organisation to do an act, or refrain from doing an act.¹⁴ The power also extends to giving directions to individuals in

⁹ See for example the 2014 Annual Information Statement questions on the [ACNC website](#).

¹⁰ See for example the "[Meet the governance standards](#)" page of the ACNC website..

¹¹ [ACNC governance standard # 1](#).

¹² Division 85 of the *Australian Charities and Not-for-profits Commission Act 2012*.

¹³ Division 100 of the *Australian Charities and Not-for-profits Commission Act 2012*.

¹⁴ s 85-10 of the *Australian Charities and Not-for-profits Commission Act 2012*.

leadership, requiring them to not participate in making decisions that affect the a substantial part of the business of the organisation.¹⁵

These powers mean that a situation could arise where the ACNC, as a government body, has power to remove the eldership or senior pastor or other leader of a Church, and appoint another person in their place. It could prevent those in leadership from engaging in activities that influence the behaviour of others in the organisation. It could issue directions requiring the religious body to do, or refrain from doing, anything.¹⁶

These powers can be triggered if there has been a contravention of the Act or governance standards, or if the Commissioner believes that there is likely to be such a contravention.¹⁷

In deciding whether to use the powers, the Commissioner must have regard to a range of factors, including the nature of the contravention, whether other means are available to address the issue, and the possibility of the organisation harming or jeopardising the public trust and confidence in the third sector.¹⁸

It should also be noted that some organisations registered with the ACNC are exempt from these powers – either because the powers are expressed only to apply to “Federally Regulated Entities” and they don’t meet that criteria,¹⁹ or because they fall into a category referred to as a “basic religious charity”.²⁰

These are technical terms that I won’t dwell on, but you can find some further explanation in your notes. In practical terms it means that whether the powers apply to an organisation depends on the organisation’s location, their legal structure and the type of activities they carry out.

But certainly, it is true to say that a fair number of religious organisations in this country are subject to all those powers.

These are powers that can be exercised by the ACNC as a statutory body and it is not necessary for it to obtain prior Court approval.

This represents a significant break from the past where an Attorney-General was given power to bring concerns before Court.²¹

So how does these powers impact freedom of association?.

¹⁵ s 85-10 of the *Australian Charities and Not-for-profits Commission Act 2012*.

¹⁶ Check whether limited by ref to ACNC objects?

¹⁷ s 85-5 of the *Australian Charities and Not-for-profits Commission Act 2012*.

¹⁸ s 35-10(2) and s 85-5(2) of the *Australian Charities and Not-for-profits Commission Act 2012*.

¹⁹ By way of summary, a Federally Regulated Entity is a constitutional corporation (that term is defined to include a corporation referred to in s 51(xx) of the Constitution – being a trading corporation or financial corporation formed within the limits of the Commonwealth, or a foreign corporation) or an organisation established in the Australian Capital Territory or Northern Territory. For a more exact definition see s 205-15 of the *Australian Charities and Not-for-profits Commission Act 2012*.

²⁰ By way of summary, a Basic Religious Charity is an unincorporated body formed for religious purposes, that does not have deductible gift recipient status in its own right, and it does not receive grants or tax deductible gifts above a certain threshold. For a more exact definition, see s 205-35 of the *Australian Charities and Not-for-profits Commission Act 2012*. Basic Religious Charities are exempted from the Commissioner’s power to suspend, remove and replace persons in leadership. They are not exempted from the power to give directions (so the same outcome can effectively be achieved).

²¹ See for example the *Charities Act 1978* (Vic).

Freedom of Association

Freedom of association is recognised as a fundamental human right in the UN Declaration of Human Rights. Article 20 states that everyone has the right to freedom of peaceful assembly and association.²²

Freedom of association is also recognised in the International Covenant on Civil and Political Rights – the ICCPR.²³ Article 20 states “everyone shall have the right to freedom of association with others”.

And independently of these conventions, freedom of association was recognised and protected by the common law.²⁴ It has been said to be “a fundamental aspect of our legal system” although it does not have the status of a free standing constitutional right that limits legislative power.²⁵

An historical review of the freedom to associate at common law shows that it is most clearly recognisable in context of religious associations.²⁶

This is not surprising because freedom of religion itself has an associational aspect. Article 18 of the UN Declaration of Human Rights recognises that everyone has (emphasis added) “freedom, either alone or *in community with others and in public or private, to manifest his religion or belief* in teaching, practice, worship and observance.”

Article 9 of the European Convention on Human rights is in similar terms and it is in that context that Christopher McCrudden, a distinguished British professor and barrister elaborates on the associational aspect of religion in his article entitled “Multiculturalism, freedom of religion, equality, and the British constitution: The JFS case considered”.

I’d like to quote from his article, referenced in your handouts, because he puts the position quite succinctly, but in doing so I will omit the case references for ease of comprehension.

He states:²⁷

The right to freedom of religion in Article 9 has, according to the European Court, two complementary aspects: an individual aspect and a collective/community aspect.

...

The ECtHR regularly emphasizes that states should not underestimate the importance of the community dimension of the right... ..”.

Article 9 ECHR must be interpreted and applied, “to allow a religious community “to associate freely, without arbitrary State intervention.” By way of example, it is

²² [UN Declaration of Human Rights](#)

²³ [ICCPR](#)

²⁴ See for example LexisNexis, *Halsbury’s Laws of Australia* (at 7 October 2011) 80 Civil and Political Rights, ‘Freedom of Association, Assembly and Procession’ 80-2135.

²⁵ *Tajjour v New South Wales; Hawthorne v New South Wales; Forster v New South Wales* [2014] HCA 35 (8 October 2014) at 224 per Gageler J referring to Dixon J in *Australian Communist Party v The Commonwealth* [1951] HCA 5; (1951) 83 CLR 1 at 200; [1951] HCA 5.

²⁶ Matthew Turnour, *Beyond Charity: Outlines of a Jurisprudence for Civil Society* (Phd Thesis, Queensland University of Technology, 2009).

²⁷ Christopher McCrudden, ‘Multiculturalism, freedom of religion, equality, and the British constitution: The JFS case considered’, (2011) 9 (1) *International Journal of Constitutional Law*, 217

uncontroversial that religious bodies and political parties can generally regulate their membership to include only those who share their beliefs and ideals. Moreover, the ECtHR has refused to permit states to interfere in the choice of leaders of particular churches. In a series of cases, the Court has held that the state must ensure that religious organizations retain their autonomy in relation to the selection of their own leaders.

So with that in mind, the question becomes: if the ACNC legislation restrains freedom of religion and freedom of association in – at the very least, the extent to which it can give directions and take control of governing body – then, is that restraint justified?

Is the ACNC regulatory scheme justified?

By way of context, the ICCPR provides only very limited grounds on which freedom of association should be limited. It states.

“No restrictions may be placed on the exercise of this right other than those which are prescribed by law and which are necessary in a democratic society in the interests of national security or public safety, public order ..., the protection of public health or morals or the protection of the rights and freedoms of others....

Clearly, the ACNC powers enable restraint of freedom of religion and association in circumstances beyond those identified in the ICCPR.

However, it is important to recognise that registration with the ACNC is only necessary for organisations that desire tax concessions, and in my experience as a practitioner, it is clear that those concessions are very desirable and a strong motivator for charities to register.

It also appears that heavy reliance has been placed on the Commonwealth legislative power with respect to taxation in s 51(ii) of the Constitution to support the constitutional validity of the legislation establishing the ACNC.²⁸

So it is in the context of tax concessions that the justifications for the granting of the ACNC powers will be considered in my presentation today.

I am aware that the debate over the ACNC and its merits is much broader than tax, and if you would like to read more broadly I would refer you again to the Moores submission referenced in your notes.

Tax as justification for the ACNC

Income tax exemptions for charities have existed in Commonwealth income tax legislation²⁹ in Australia since the early 1900s.³⁰

However the nature of the obligations now attached to those concessions in the form of the ACNC are new.

I would suggest that this is because the tax concessions are now thought of in terms of government expenditure.

²⁸ For a detailed discussion on this, see Melbourne University submission to the exposure draft of the ACNC legislation - [Submission to Treasury, 'Exposure Draft: the Australian Charities and Not-for-Profits Commission'](#).

²⁹ At least since 1915?

³⁰ perhaps qualify to say late 19th century – ref Pemsel? But then that's a trust not an institution – consider wording.

The Preamble to the *Australian Charities and Not-for-profits Act 2012*, which I will refer to as the ACNC Act, states that “the not for profit sector receives a range of funding” including “tax concessions”.

The Explanatory Material attempts to quantify the value of tax concessions in tax expenditure terms.

“Tax expenditure” connotes a concept of government expenditure, in the form of tax concessions. The expenditure is the difference in tax paid by taxpayers who receive a particular concession, relative to taxpayers who do not receive the concession.³¹ It is a way of expressing tax concessions as a form of government subsidy.

Although the amount of tax expenditure incurred by the government in the form of income tax exemptions cannot be properly estimated, the Explanatory Memorandum to the ACNC Act estimates it to be in the billions.³²

So, in a context where there are tight budgetary constraints, the spotlight has been turned on charities to justify their entitlement to those concessions.

In the words of Ann O’Connell, a tax lawyer, consultant and academic: “in one sense, some regulation is the price these organisations pay for access to the tax concessions.”³³

Alternative

However, there is an alternative view.

That view challenges the idea that tax concessions are government expenditure, and builds a rationale for exemption on the basis of a broader concept of public benefit. If it is accepted, the government regulation of charities – through the ACNC powers – could be said to be lacking in persuasive value.

In order for the concept of tax expenditure to work, there needs to be a clear benchmark or point at which income becomes subject to taxation, so any subsidy can be identified and measured.³⁴

However the benchmark is contested. This is acknowledged in the Australia’s Future Tax System: Report to the Treasurer – otherwise known as the Henry Review - which states:

Not all concessional elements of the tax system are classified as tax expenditures. This is because some concessions are considered to be structural elements of the tax system and are incorporated in the benchmark. For example, the personal income tax system includes a progressive marginal tax rate scale, which results in individuals on lower incomes paying a lower marginal rate of income tax than those on higher incomes. This arrangement is a structural design feature of the Australian tax system and is therefore not identified as a tax expenditure. There may be

³¹ [Productivity Commission, Contribution of the Not-for-Profit Sector: Research Report \(2010\), 162.](#)

³² [Explanatory Memorandum, Australian Charities and Not-for-profits Commission Bill 2012, 16.3.](#)

³³ Ann O’Connell, *Watching over the helpers: why regulation of charity matters* (27 December 2013) The Conversation< <http://theconversation.com/watching-over-the-helpers-why-regulation-of-charities-matters-19971>>.

³⁴ See Myles McGregor-Lowndes, Matthew Turnour and Elizabeth Turnour, ‘Not for Profit Income Tax Exemption: Is There a Hole in the Bucket, Dear Henry?’ (2011) 26 *Australian Tax Forum* 601.

*different views on which structural elements to include in the benchmark. These benchmarks can vary over time and can sometimes be perceived as arbitrary.*³⁵

In the 1990s, an argument was developed by Richard Krever, a professor in tax law, to say that little or no revenue is forgone by exempting charities from tax.

This argument has been neatly summarised in a paper entitled “Not for profit income tax exemption: is there a hole in the bucket, dear Henry?” authored by Myles McGregor-Lowndes, Matthew Turnour and me and reference in your handouts.

We explain the argument as follows:

Individuals are the accepted and appropriate unit upon which to impose income taxes. By definition, charities have no owners, only purposes, and are legally prohibited from distributing surpluses to individuals, so the income would have to be traced through to the individuals who benefited from the achievement of their stated purposes. Tracing individual beneficiaries would be difficult and expensive. Many beneficiaries of charities would be unlikely to pay tax because they are financially disadvantaged; or when public goods are involved they are so broadly spread and numerous that tracing them would be administratively unworkable.

...This misfit arises when applying tax expenditure theory to NFPs because personal gain, at the heart of income tax, is not the primary purpose of the not for profit undertaking.

In our paper we also outline a similar argument made by Ole Gjems-Onstad, a Norwegian tax professor. He argues that when the legislature makes exceptions for NFP organisations because they do not fit the personal gain model on which the taxation provision is based, the exemption ought not be viewed as a subsidy or a tax expenditure.³⁶

The logic in this argument can be demonstrated by way of example. Take for instance the taxation of trusts.

Ordinarily in a trust structure, income tax is paid by the beneficiaries of the trust. The trustee allocates a distribution and the beneficiary pays the tax on the distribution.

In the case of a charitable trust, there are no “beneficiaries” in the true sense as owners. Charitable trusts are distinguished from ordinary trusts because they are not trusts for individuals, they are trusts for purposes. So it does not fit the model of taxation which traces the wealth through to the individual which owns it.

In the case of charities, the purpose for which an organisation or trust is established must be a purpose of benefitting the public. The concept of what is or is not for the public benefit is contested, but you will recall from the discussion of the three failures theory at the outset, that part of the role of the third sector is to allow the pursuit of different conceptions of the public benefit. It is to allow minorities to pursue their conception of the public benefit.

When public benefit is articulated this way, I would suggest that it can actually be seen as an expression of the public benefits of freedom of association. These benefits have been

³⁵ Australia's Future Tax System Review Panel, Australia's Future Tax System: Report to the Treasurer (The Treasury, 2009) 731 ('Henry Review'), cited in Myles McGregor-Lowndes, Matthew Turnour and Elizabeth Turnour, 'Not for Profit Income Tax Exemption: Is There a Hole in the Bucket, Dear Henry?' (2011) 26 *Australian Tax Forum* 601.

³⁶ See See Myles McGregor-Lowndes, Matthew Turnour and Elizabeth Turnour, 'Not for Profit Income Tax Exemption: Is There a Hole in the Bucket, Dear Henry?' (2011) 26 *Australian Tax Forum* 601.

articulated by the United Nations Special Rapporteur on the rights to freedom of peaceful assembly and of association as follows:³⁷

The rights to freedom of peaceful assembly and of association serve as a vehicle for the exercise of many other civil, cultural, economic, political and social rights. The rights are essential components of democracy as they empower men and women to “express their political opinions, engage in literary and artistic pursuits and other cultural, economic and social activities, engage in religious observances or other beliefs, form and join trade unions and cooperatives, and elect leaders to represent their interests and hold them accountable” ... Such interdependence and interrelatedness with other rights make them a valuable indicator of a State’s respect for the enjoyment of many other human rights.

So – the alternative argument would suggest that perhaps tax concessions should be seen as a recognition of the public benefit contributed by charities to society as a whole, and an expression of freedom of association, and not as a drain on government revenue for which restraints on freedom of association and religion must be accepted.

Summary

So if I could summarise the material before you today -

Religious organisations, and other charitable voluntary associations are required to be accountable to the broader public for their tax concessions through the ACNC. However the considerable enforcement powers associated with that accountability can be said to impinge on freedom of association and freedom of religion.

This restriction has occurred because of a belief that tax concessions are a form of government expenditure and must be justified. This is a concept which attracts mainstream public support and is reflected in the explanatory memorandum to the ACNC Act.

However, there is a contrary view, and that is to recognise that charities contribute to the public benefit, and in fact embody many of the benefits to society that exist when freedom of association is protected. Accordingly, the tax concession of charities can be said to already be justified without the need for further public regulation and restraint.

The significant powers of the ACNC are, I am sure, in safe hands with the incumbents at the ACNC. No doubt, there are many within the community who are pleased to know that those powers exist to enable the ACNC to deal with extreme circumstances where leaders of churches and other charities have turned rogue, and who also find comfort in light of the ACNCs sensible and clearly stated policy, only to utilise those powers where other less draconian measures have failed or are clearly inappropriate.

However, being blessed with highly capable and sensible people at the ACNC is a separate issue to whether the powers that have been given to the ACNC are justifiable on a theoretical or public policy level. In my personal view, the justification for the extensive powers is lacking.

³⁷ [Report of the Special Rapporteur on the rights to freedom of peaceful assembly and of association, Maina Kiai.](#)