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Private & Confidential

Submission in response to the Discussion Paper: “Fairer, simpler, and more effective tax concessions for the not for profit sector” on behalf of various State, Territory and Commonwealth Public Universities

This submission has been prepared by Ernst & Young on behalf of various State, Territory and Commonwealth Public Universities, each of which may be impacted, to varying degrees, by the reform options contained in the Discussion Paper released by the Not for Profit (NFP) Sector Working Group in November 2012.

The following State, Territory and Commonwealth universities (collectively referred to as “Public Universities”) have agreed to participate in this submission:

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This submission is divided into two parts:

► Appendix A summarises the unique objectives of the public university sector and outlines reasons as to why it is fundamentally critical that current tax concessions available to the sector be maintained. Appendix A also outlines reasons supporting the extension of Fringe Benefits Tax (FBT) concessions to the public university sector to assist the sector remain competitive in attracting world class

1 Australian Catholic University is a not for profit university and is treated like a public university for the purpose of this submission notwithstanding it is eligible for the FBT rebate.

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academic, executive and administrative staff and to ensure consistency with the income tax exemption provisions;

- Appendix B addresses a number of key questions raised in the Discussion Paper from the perspective of the public university sector.

As the responses in Appendices A & B indicate, the public university sector does not recommend any significant change to the existing NFP tax concession framework. Any significant structural change to the tax concessions available to the public university sector at this time would be particularly inappropriate given the various outstanding NFP tax reforms currently being considered by Government, including:

- the proposed “Better targeting of NFP tax concessions”;
- the restated “in Australia” special conditions for tax concessions including deductible gift recipients; and
- the proposed statutory definition of ‘charity’.

We are particularly concerned that parallel reform proposals would add unreasonable uncertainty and compliance burdens, particularly for those organisations that may be in the process of implementing some of the proposed changes, some of which have retrospective application.

Notwithstanding the above, this submission recommends a number of worthwhile enhancements which would both “fine-tune” the existing NFP tax concession rules to promote a more simple, fair and effective framework, and also assist the public university sector in achieving its objectives and purposes. Fostering these objectives and purposes is critical in ensuring Australia continues to develop as a well educated and skilled nation, which is essential to its future prosperity. In summary, the public university sector strongly urges the Working Group, in its report to Government, to reinforce and confirm the position that:

- Tax concessions should continue to be provided to those organisations that have charitable objectives and provide significant public benefit. The tax concessions currently provided to public universities are largely effective in supporting their educational, research, innovation and social benefit objectives and should be maintained;

- Tax concessions do not, in every instance, violate the principles of competitive neutrality. Given the unique objectives of public universities and in particular their focus on education, research and diverse community engagements, there is sound policy rationale justifying the availability of tax concessions to their activities in contrast to “for profit” education providers. Tax concessions are required by public universities to maintain competitiveness in a sector which is being increasingly challenged by a growing number of international competitors. It is within the Australian public interest to maintain a world class tertiary education system;

- Tax concessions provided to public universities do not equate to lost revenue for the Government. Given a significant portion of public university revenue is received through Federal Government funding, it would not make sense to then impose tax upon the income received. In addition, maintaining tax concessions which support giving to the public university sector would decrease the reliance on Government support. Philanthropic funds are increasingly relied upon by the public university sector and any changes recommended by the Working Group should enhance the propensity of Australians to support the activities of the public university sector; and

- The entitlement to the FBT exemption / rebate should be amended to be consistent with the income tax exemption provisions. The education industry is dominated by income tax exempt entities that are also entitled to the FBT rebate. The public universities are denied access to this concession and therefore are at a disadvantage when competing for the best academic, management and administrative staff in the education sector. Moreover, most of Australia’s research intensive public
universities are heavily involved in health and medical research, often in collaboration or competition with hospitals and medical research institutions, which are treated differently for FBT purposes.

We look forward to discussing this submission further with the Working Group and Treasury at your earliest convenience, and note that the Discussion Paper indicates that the Working Group will conduct targeted consultation with interested stakeholders. Representatives of the public universities, together with Ernst & Young, would welcome the opportunity to be included in the consultation process both prior to the finalisation of the Working Group’s report to Government in March 2013 and any subsequent consultation framework. In the meantime, if there is any aspect of this submission in relation to which the Working Group would like more information, please contact Jason Wrigley (02 9248 5303), Alf Capito (02 8295 6473) or Richard Czerwik (03 9288 8408).

Yours faithfully

Jason Wrigley
Tax Partner
Ernst & Young
Appendix A

1. Introduction

In order to assist the Working Group in its consideration of the application of tax concessions to the public university sector, this part of the submission is intended to provide an overview of the history, current status and future potential trends that should be taken into account in developing fairer, simpler and more effective tax concessions for the public university sector.

The public university sector acknowledges that the NFP sector is broad and diverse and that a number of organisations will have their own worthwhile objectives and claims for on-going or additional support by way of tax concessions. The purpose of this submission is not to rank nor position public universities in contrast to other NFP entities, but instead to reinforce the critical role played by public universities in Australian society and outline the importance of tax concessions in maximising the public benefits which flow there from and in reducing the reliance on Government funding.

2. Overview of Australia's higher education sector

Australia's public universities continue to be recognised as the focal point of the higher education sector as well as the overall education sector. The Tertiary Education Quality and Standards Agency (TEQSA) national register of Higher Education Providers identifies 173 registered entities, 39 of which are universities. NFP public universities represent the overwhelming majority of all universities. The Australian university sector is a $23 billion dollar industry employing more than 100,000 academic, professional and administrative staff and generating $15 billion dollars in export revenue through the provision of education services to international students both in Australia and offshore.

Notwithstanding the direct and significant role it plays in the Australian economy, the public university sector is, at its core, a not for profit organisation established by law and required to service the public interest. It achieves this objective by providing Australians with affordable opportunities to access world class education services and by creating a community which fosters social inclusion, diversity and innovation.

The importance of the education sector was recently reinforced by the Productivity and Prosperity Advisory Panel (the Panel) in its 2010 Report. The Panel recognised that:

“A well educated and skilled people are central to Australia’s future prosperity and the so called “second generation success story”, which sees the children of migrants attain relatively high levels of education, tending to lift the average level of education attainment in Australia, is an important element in this.

Indeed there are tremendous opportunities for Australia to benefit from further emphasis on investment in education and skills development.

Both Government and industry are working to improve education and training. Recent reforms to universities will leave them better able to respond to student demand, giving more Australians the opportunity of the benefits of a tertiary education. At the other end of the spectrum, reforms to schools aim to improve the foundation skills of the population.”

Importantly, the Australian higher education landscape is changing rapidly and the public university sector in particular requires support to ensure it continues to be a vibrant contributor to Australian society. In addition to Australia’s 39 public and private universities, there are approximately 140 other registered higher education providers and this number has grown significantly in recent years. International competition in the tertiary education market in particular has rapidly increased as has the number of “for profit” education providers. These developments pose the following risks to the future viability and quality of Australian tertiary education:

- With the increase in international and “for profit” education providers, there is a risk that profits of the higher education sector are being extracted for shareholder or private benefit rather than being reinvested into research and other community activities. NFP public universities reinvest funds to support their social good objectives and are not carried on for the private benefit of shareholders or individuals;

- The growth in international tertiary education providers puts at risk the continuing development of Australian skills, research and innovation. Moreover, the potential reduction in student fee revenue for Australian public universities places greater strain on the ability of these organisations to deliver their social objectives and places more reliance on Government funding; and

- The growth in the number of education providers and “for profit” organisations in particular has not been matched by similar increases in research activity or cultural programs which are often not economically viable for these organisations.

Given these concerning developments, it is vital that the position of Australian public universities is properly protected to ensure that the critical contribution they make to society, the economy and the innovation system through their education, research and diverse community engagement activities is not impeded, particularly in the current challenging economic climate.

3. Key features of modern Australian public universities

There are currently 37 public universities located in Australia. The dominant university model in Australia is a broad-based teaching and research institution, supported by a large asset base and a large, predominantly in-house back office. Most universities are large, complex organisations engaged in diverse activities directed towards the common goal of pursuing objectives which benefit the public and foster social inclusion. Indeed, most Australian universities:

- Serve a broad mix of student segments - school leavers, mature age students and international students;

- Offer a broad range of disciplines - health sciences, arts, science, technology, business, economics, education, law and more;

- Deliver teaching and learning programs primarily on campus in Australia, supplemented by various online offerings, franchise arrangements, twinning partnerships and international branch campuses;

- Deliver and manage the vast bulk of student services and back-office functions (HR, IT, payroll, finance, procurement and so on) in-house.3

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3 “University of the future, A thousand year old industry on the cusp of profound change” Ernst & Young, 2012, page 14
Whilst today's modern Australian public universities continue to grow with a view to providing an extensive, contemporary and diverse tertiary educational experience, they have maintained their fundamental teaching and research identity and objective of advancing tertiary education. Where the public university is established by an Act of Parliament, the Act confirms their “core” objects, functions and powers. Where a public university is not established by an Act of Parliament, its “core” objects, functions and powers are set out in its constitution. Ordinarily, a public university's “core” objects and functions include the following:

- The provision of facilities for education and research of a university standard;
- The encouragement of the dissemination, advancement, development and application of knowledge informed by free inquiry;
- The provision of courses of study or instruction across a range of fields, and the carrying out of research, to meet the needs of the community;
- The participation in public discourse;
- The conferring of degrees, including those of Bachelor, Master and Doctor, and the awarding of diplomas, certificates and other awards;
- The provision of teaching and learning that engage with advanced knowledge and inquiry;
- The development of governance, procedural rules, admission policies, financial arrangements and quality assurance processes that are underpinned by the values and goals of the university and that are sufficient to ensure the integrity of the university's academic programs; and
- Providing essential community services and facilities

As the above indicates, public universities have varied and wide-ranging core objects and functions. In many cases, particularly with public universities based in regional areas, the core objects and functions may extend to supporting the community in which the university operates.

A non-exhaustive list of common activities undertaken by a public university in pursuit of its core objects includes:

- Provision of education;
- Services primarily provided to students and university staff (i.e. food outlets, car parks, medical centres, training facilities, sporting clubs/gyms, library, unions, hotels etc);
- Student accommodation;
- Property (university infrastructure and student accommodation) development and maintenance;
- Research and professional services (including consultancy and testing);
- Investment portfolios;
- Administrative functions;
- Operation of commercial activities by students in furtherance of their tertiary studies; and
- Commercial exploitation of intellectual property

These broad objectives and activities give rise to substantial funding requirements. In order to meet these requirements, public universities need to raise revenue from a number of sources. Whilst, revenues from student fees, philanthropy and commercial ventures continue to grow, the ability of the public university to deliver on its social objectives is very much dependant on the direct and indirect funding received in the form of grants and tax concessions from the Commonwealth and State Governments.

4. Existing tax concessions available to the NFP public university sector

Summarised below are the various Federal tax concessions that are generally available to Australian public universities. The importance of each of those concessions is considered in more detail in Appendix B in response to the relevant Discussion Paper questions.
4.1. Income Tax

Public universities are generally exempt from income tax either pursuant to item 1.4 of section 50-5 of the Income Tax Assessment Act 1997 (ITAA 1997) (as a public educational institution), or item 1.1 of section 50-5 (as a charitable institution), which reflects the public educational activities of the universities and their intrinsic connection with the NFP sector.

However, there may also be various other NFP entities connected with a public university, such as sporting and other clubs which may be eligible for income tax exemption (e.g. exempt under s.50-45 of the ITAA 1997) or which may, alternatively, apply the principle of mutuality in relation to member activities.

Public universities are generally eligible (as an exempt institution within the scope of s.207-115 of the ITAA 1997) to claim a refund of franking credits on franked distributions from Australian companies under section 67-25 of the ITAA 1997.

4.2. Deductible gift recipient

Most public universities are endorsed as a deductible gift recipient (DGR) under table item 1 in section 30-15 of the ITAA 1997 (relying on the public university category in s.30-25(1)). The endorsement is provided on an 'entity' basis rather than a more restrictive fund basis. Donations received by public universities are predominantly directed towards benefiting the education experience of students including student scholarships, improving student resources and by supporting Australian based research.

4.3. Fringe Benefits Tax

Pursuant to the Fringe Benefits Tax Assessment Act, 1986 (the FBT Act), a variety of businesses are entitled to concessions based on their operations and/or the sectors in which they provide services. For example, the FBT Act indicates that certain benefits provided by a very specific list of employers are deemed to be exempt benefits. Additionally, many NFP employers are allowed a rebate on their FBT otherwise payable. It is under these rebate provisions that many educational institutions receive relief.

Under the FBT Act, specifically in relation to the education sector, private universities (such as Bond University and Australian Catholic University) and primary and secondary private schools are eligible for the FBT rebate. This rebate applies such that for a rebatable employer, their FBT liability may be almost halved, subject to a per employee cap, compared to normal FBT paying employers, such as public universities.

Critically, there is no consistency between the employers afforded income tax exemptions provided under the ITAA 1997 and employers eligible for the FBT rebate provided for under the FBT Act. Currently, assessment for exemption from income tax is completely independent of an employer's liability to FBT, causing additional administration for employing entities to determine which, if any, concessions apply to their business. In practice, an employer may be required to trawl through any number of different Acts to determine the correct amount of income tax and FBT for which they are liable.

To the extent the income tax rules and FBT rules are incongruent on concessions for different entities, particularly within the same sector, it provides for disharmony across companies and, in turn, across the workplace environment. As the Working Group identifies, this also raises competitive neutrality issues.

The education industry is dominated by income tax exempt entities that are also entitled to the FBT rebate. However, the public universities are denied the FBT rebate on the basis they are/were historically an institute of the Commonwealth, a State or a Territory.
However these institutions are directly competing with other education providers that are eligible for the FBT rebate for the best employees. As demand for suitable employees increases, so too does the cost. This is in direct contrast to the objective that the universities fill in the marketplace. As NFP entities, wherever costs are increased there is a direct reduction in funds available to provide services and facilities to the public.

Faculty staff, such as lecturers and other teaching staff can be enticed by rebatable employers in primary and secondary schools or private universities. However, university employees also extend beyond just faculty staff. In order to function, the universities require administration staff, including Directors and Executives that field offers from other education and NFP entities that are entitled to the FBT rebate. Medical schools within the universities also compete with medical research institutions and hospitals to employ researchers and academics. In practice, such university employees within the medical schools are often working alongside public hospital or research institution employees that are entitled to the FBT rebate, whilst missing out themselves. Without the FBT rebate that is available to other rebatable employers, as noted above, the universities are forced to offer higher salaries or absorb higher FBT costs to deliver the same benefits to their employees. Alternatively, they are required to seek talented employees who are driven by a social and community conscience rather than monetary reward. However, given the prevalence of NFP, socially conscious entities in the education and research fields that are entitled to the rebate, this argument is relatively weak for the universities, making it even more difficult for universities.

These increased costs are further exacerbated by the recent Living Away From Home Allowance (LAFHA) amendments that have directly impacted the ability of universities to offer attractive remuneration packages to prospective employees from outside Australia. Initially aimed at preventing high income individuals from exploiting FBT concessions, the changes to the legislation have impacts across the entire mobile workforce regardless of pay, industry or even purpose of travel. If the universities wish to continue to attract international staff they are now faced with significant tax liabilities where they provide assistance to these individuals, which is often crucial in securing the talented individuals as employees. Where the universities cannot meet these higher costs, they are now forced to recruit from their local market. As noted above, this requires them to directly compete with local education providers that are eligible for the FBT rebate who can offer higher package values, for lower employer costs by way of effective salary packaging. By expanding the FBT rebate provisions to include all NFP education institutions, the public universities will be able to compete equitably for talented employees.

As a result of their NFP structure and Charter, it has been legislated that these universities be exempt from paying income tax. It therefore appears counter intuitive that an entity deemed to be exempt from paying income tax should be liable for FBT, particularly given the sector they work in, as noted above.

With the above considerations in mind, fairness dictates that public universities should be provided with access to the FBT rebate as a direct result of their NFP activities and the sector in which they operate.

Ideally this would be achieved by extending the relevant FBT concessions to all NFP entities. A situation where all income tax exempt entities are eligible for the same FBT concessions would enable the public universities to compete on a more even playing field for talent in the workforce focused on the sector in which they operate.

Alternatively, if it is not possible to extend the FBT concessions to all NFP entities then the rebate should at least be extended to all NFP entities operating in the education sector.
4.4. Goods and Services Tax (GST)

The majority of education courses supplied by the university sector are currently treated as GST-free. We note however that the GST Distribution Review Report prepared by Treasury dated October 2012 includes comments (although recognised as a contentious issue) that the GST-base could be strengthened if the GST-free treatment of supplies made by entities within certain industries, such as the health, education and food sectors, was to be removed. Any changes to the GST-free treatment of education courses would have a wide-reaching and significant impact on the university sector.

Notwithstanding the above, our comments in this submission have been prepared on the basis that the GST-free treatment of education courses will continue to remain in place. We have not considered the impact of how any changes to the GST base would affect either the GST concessions currently available to NFP entities or the university sector more widely, as we understand this to be outside the ambit of the Discussion Paper.

Of the GST concessions currently available to NFP entities, there are a number that are used widely by entities across the public university sector. These include:

- The GST-free concession in section 38-250 of the GST Act for supplies of accommodation and other supplies for nominal consideration. This is an important concession and applies, for example, where public universities provide accommodation and other services to their students;
- Public universities benefit from the ability to opt for input taxed treatment under section 41-160 of the GST Act in respect of their fundraising activities; and
- Entities within the public university sector also benefit from the concession available under section 111-18 of the GST Act which allows universities to claim input tax credits where volunteers are reimbursed directly for expenses they incur in the course of their voluntary services for the universities.

4.5. Summary

As the Working Group’s review is limited to the consideration of Federal tax concessions, we have not considered the eligibility of any State or Territory based tax concessions in relation to public universities or their connected entities.

The above summary of tax concessions illustrates that whilst public universities do benefit from a number of important NFP tax concessions, they are disadvantaged by their inability to access certain concessions, particularly FBT.

5. Tax concessions should complement Government Objectives for Public Universities

As the Working Group acknowledges, tax concessions are a form of Government assistance and should be directed towards worthy causes. The Government has consistently acknowledged the importance of the public university sector in Australia and has in place a number of strategies to ensure the continuing viability of the sector. These strategies are outlined, in part, in the Department of Education's 2009 Report: Transforming Australia’s Higher Education System4 and also in the Government’s Innovation Policy Report, 2012. These reports indicate that the Government’s objectives for public universities include:

- Encouraging public universities to diversify their income streams; and
- Encourage public universities to continue to innovate.

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4 Transforming Australia's Higher Education System - Department of Education, Employment and Workplace Relations - Commonwealth Government 2009
Given the above, the public university sector strongly argues that the tax concession framework should continue to support these Government objectives. These are discussed below:

5.1. Diversification of Income Streams

The higher education sector has been subject to significant structural, funding and regulatory review over recent years. These reviews have led to a number of changes to the way the sector now operates. The Government's strategy for the higher education sector, as set out in Transforming Australia’s Higher Education System, includes recommendations for various additional changes, particularly in relation to future funding models. Put simply, the higher education sector, including public universities, is under increasing pressure to diversify their income streams to reduce the traditional heavy reliance on Government educational funding. Accordingly, diversification of income streams going forward will be particularly important given the likelihood that Australian Governments, regardless of political persuasion, will be increasingly fiscally constrained. As such, it can be anticipated that Government funding, as a share of university revenue, is likely to decline and public universities will need to continue to search for ways to move beyond the ‘fight for funds’ relationship with Government. In particular, and relevant for the purposes of the Working Group’s review, are recommendations for public universities to increase their sources of funding from philanthropy. To this end, the Higher Education Base Funding Review in 2011 observed that:

"Philanthropy plays a far smaller role in Australian universities than in many overseas institutions. While the older universities receive substantial support from alumni, businesses and donors, other institutions have far less focus in this area of endeavour. The Government has previously received a recommendation from the Bradley Review of Australian Higher Education to develop a pool of funds as an inducement to match gifts from new donors. The Panel suggests performance in this area could be improved if some universities had access to a small seed funding scheme to help build institutional capacity."

If increasing levels of giving by Australians to the higher education sector is a priority for the Australian Government, there is an urgent need for an integration of relevant fiscal and taxation policies to ensure they work coherently to provide an environment conducive to giving, particularly by high wealth individuals. Given the above, the public university sector would support any reforms to the treatment of deductible gifts that would complement these objectives.

5.2. Innovation

Public Universities contribute significantly towards the provision of higher education and the advancement of knowledge by way of research and other activities in Australia. Accordingly, any reduction to existing tax concessions to public universities would be inconsistent with the Government’s broader innovation policy which is focused on encouraging the sustainable growth of Australian industries by developing a national innovation system that drives knowledge creation, cutting-edge science and research, international competitiveness and greater productivity.

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5 Transforming Australia’s Higher Education System - Department of Education, Employment and Workplace Relations- Commonwealth Government 2009
6 “University of the future, A thousand year old industry on the cusp of profound change” Ernst & Young, 2012, page 25
7 Higher Education Base Funding Review, Final Report, October 2011
6. Regulation to ensure the public benefit is maximised

The Discussion Paper clearly articulates the view that the provision of tax concessions to particular entities should be met by an appropriate level of public benefit (social good). To this end, the Discussion Paper envisages both review of the eligibility criteria as well the ongoing oversight that should be directed to the relevant entity to ensure eligibility criteria continue to be satisfied. The public university sector supports the broad ranging review of the Working Group in its examination of the entire range of tax concessions across the diverse range of entities that make up the NFP sector and agrees that, in certain circumstances, a greater degree of transparency in relation to the results of Government support of the NFP sector may be desired: this is supported by the Government’s recent establishment of the Australian Charities and Not for Profit Commission (ACNC) as a national regulator of charities and the NFP sector generally.

The Public University sector strongly urges the Working Group, in its report to Government, to reinforce the position that the public university sector remains one of the most tightly regulated NFP sectors. The public university sector is very closely regulated by State and Territory governments as owners, and also as part of the various sources of education and research funding provided by the Commonwealth, State and Territory Governments. Public Universities are also subject to State and Federal scrutiny through the application of laws, regulations and by-laws. It is submitted that these laws and regulations provide more than adequate transparency of public university sector operations and ensure that all activities conducted by these organisations are directed towards maximising public benefit through education and research.

An issue that may potentially be outside the current scope of the Working Group is the need for relief from potential duplicate regulation of NFP private universities by both the ACNC, as the national regulator of charities, and by TEQSA, the national higher education provider regulator that was established in 2011 following the Bradley Review of the higher education sector. We would be happy to discuss these matters in more detail with the Working Group / Treasury at a later date.

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8 TEQSA was established on 29 July 2011 under Section 132 of the *Tertiary Education Quality and Standards Agency Act 2011*. 

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Appendix B

PUBLIC UNIVERSITY COMMENTS ON CONSULTATION QUESTIONS

This part of the submission addresses a number of key questions raised in the Discussion Paper from the perspective of the public university sector. We have responded to the key issues relevant to the university sector, building upon comments made in Appendix A and have not sought to respond to all the questions raised in the Discussion Paper.

CHAPTER 1 – INCOME TAX EXEMPTION AND REFUNDABLE FRANKING CREDITS

Q1-4 What criteria should be used to determine whether an entity is entitled to an income tax exemption? Should additional special conditions apply to income tax exemptions?

Australian public universities are generally income tax exempt either under item 1.4 of section 50-5 of the ITAA 1997 (as a public educational institution), or item 1.1 of section 50-5 (as a charitable institution), which reflects the public educational activities of universities and their intrinsic connection with the NFP sector. Income tax exemption as a charitable institution requires endorsement, whereas income tax exemption as a public educational institution does not require endorsement provided the relevant conditions can be satisfied on a self assessment basis (although a private ruling would usually be sought to confirm eligibility).

Whilst there may be a technical debate as to which of the alternative bases for income tax exemption should apply to a public university, exemption as a charitable institution is the most common basis for income tax exemption for public universities.

There is a long standing tax policy for tax exemptions being provided to support and foster charitable institutions. The rationales for providing tax concessions particularly to charitable institutions are sufficiently set out in the Discussion Paper9. The advancement of education in Australia, particularly at the tertiary level, should continue to be recognised and supported as a charitable purpose and public universities should continue to be separately recognised for income tax exemption, notwithstanding the many and various advancements in education over time.

Income tax exemption is of great importance to public universities and should be maintained given the public benefit which flows from their operations. Approximately 50-60% of public university income comes from Government - it would not make sense to then make this subject to income tax.

Notwithstanding the generally recognised success of Australia’s public university sector, future predictions of ongoing government funding constraints and also the challenges arising from global competition and digital technologies, mean that Australia’s public university sector will need support to survive these challenges10.

9 NFP Sector Tax Concession Working Group Discussion Paper: Fairer, simpler and more effective tax concessions for the NFP sector, November 2012, page 9 to 13
10 “University of the future, A thousand year old industry on the cusp of profound change” Ernst & Young, 2012, page 4
The public universities are strongly opposed to any proposed recommendations or amendments to the income tax eligibility rules that may duplicate or conflict with the Government's proposed "Better Targeting of Tax Concessions" reforms. These reforms seek to remove tax concessions connected with the unrelated commercial activities of NFP entities. Any review of income tax exemption eligibility criteria that considers factors such as unrelated commercial activities, or any equivalent type of concept, should only be done as a combined holistic exercise. We are particularly concerned that parallel reform proposals would add unreasonable uncertainty and compliance burdens, particularly for those organisations that may be in the process of implementing the proposed changes which are proposed to have retrospective application from 1 July 2012. Furthermore, it is submitted that the concerns arising from the application of tax concessions to unrelated commercial activities of NFPs should not be resolved through the loss of entity wide tax concessions.

Similarly, the public universities are opposed to any additional recommendations or proposals for additional "special conditions" for income tax (or DGR) eligibility. As the Working Party is aware, the proposed restated 'in Australia' special conditions, which are currently before parliament, will impose an arguably excessive Australian pseudo residency requirements and operational restrictions upon public universities for income tax exemption (and DGR) purposes. These special conditions have the potential to significantly impact the funding needs and operations of the public university sector. On this basis, no addition special conditions should be recommended until the concerns regarding these proposed amendments are resolved.

Public universities are one of the most tightly regulated sectors in the NFP sector. Accordingly, no additional transparency in the university sector would be gained from imposing any further regulatory or integrity measures in respect of tax concessions on the public university sector.

Q5&6 Who should be eligible for refunds of franking credits?

Australian public universities are generally eligible (as an exempt institution within the scope of s.207-115) to claim a refund of franking credits on franked distributions from Australian companies under section 67-25 of the ITAA 1997.

Public universities may qualify as an exempt institution on the basis of being an endorsed charitable institution, or alternatively, as a deductible gift recipient (endorsed under the 'entity' basis rather than the fund basis). However, a public university which is exempt from income tax on the basis of its classification as "public educational institution", will not be eligible for refunds of franking credits.

Although from a practical perspective there would be little benefit arising for public universities as a result of an amendment to extend the list of entities eligible for refunds of franking credits to formally cover public educational institutions, this amendment may be required if the proposed changes to the definition of "charity" put at risk a public university's charitable status.

Public universities should continue to be eligible for refunds of franking credits. Universities have significant investments in Australian companies which generate income to fund scholarships, education and research. Any change to the existing system would place additional reliance on Government funding and distort public university investment decisions away from Australian equities in favour of bonds and debt, the returns on which would remain income tax free. Whilst the existing system of dividend imputation remains, which allows individual resident taxpayers to benefit from refunds of excess franking credits, without any system of means testing, it would be inequitable to remove the concession from existing eligible entities within the NFP sector based on any vague notion of resource/capital asset adequacy for the NFP entity: the practical reality is that the current model for a world standard public university calls for organisations with a large asset base.
To exclude public universities from the concession would place them at a disadvantage (in respect of
dividend income taxation) with both individuals and other entities within the the “For Profit” sector in that
are generally able to claim the franking credits as an offset against taxable profit.

In relation to any perceived inappropriate access to franking credits, we are of the view that the various
existing dividend imputation integrity rules operate effectively to address any potential abuse.

Q9. Increasing the tax free threshold for taxable NFPs

The public universities would support increasing the tax free threshold for taxable NFP entities. This
measure is relevant for numerous clubs and societies associated with universities, which are a very
important part of the student experience.

The existing threshold of $416 is of little practical benefit. A threshold of $5,000 would better suit the
needs of small sized NFP clubs and societies that may generate small surpluses from non-member
activities.

CHAPTER 2 – DEDUCTIBLE GIFT RECIPIENTS

As indicated earlier in this submission, public university funding will increasingly rely on philanthropy as a
source of revenue. Accordingly, any reforms to the current tax concession arrangements for donations
and gifts should not reduce the propensity for Australians to give to worthy, public benefit causes and
should also recognise that donations and gifts to the public university sector is overwhelmingly dominated
by higher wealth individuals with greater discretionary income. Put simply, the public university sector
urges the Working Group to consider the introduction of favourable tax arrangements targeted at this
group so that the total value of donations to universities is likely to increase and the reliance on direct
Government funding is similarly decreased.

Q11 to 14. Should DGR eligibility be extended to other income tax exempt NFPs?

The public university sector is, in principle, tentatively supportive of extending DGR status to a broader
range of income tax exempt NFP entities in the interest of fairness, and to encourage a broader range of
philanthropy in the community to the broader benefit of the NFP sector.

The support is tentative in light of the potentially significant revenue cost, which under the terms of
reference for the Working Group, is required to be funded from existing NFP tax concessions and
therefore likely to disadvantage some segments of the NFP sector, including potentially public
universities.

We submit that such a change should be recognised as a major structural reform to the NFP sector and,
as such, the Government should consider removing this measure from the NFP sector funding
requirement and undertake a broader funding analysis for this measure.

We are somewhat concerned by some of the comments that appear in Option 2 (cost saving measure)
which includes primary and secondary education providers, amongst a list of other entities, which would
not be eligible for DGR endorsement on the basis that they are perceived to provide “significant private
benefits”. Whilst this does not directly affect the public university sector, we are surprised and concerned
that the provision of education by a NFP entity, whether at primary, secondary or tertiary level, is viewed
as principally providing a private benefit to the student or family thereof. This ignores the findings and
recommendations of various education reviews which consistently reinforce the need for advancement of
all levels of the education system for the broader benefit of the economy and the community.
Q15 to 18. Tax deductions or offsets for gifts to DGRs?

Most public universities are endorsed as DGRs. Public universities typically receive significant bequests and donations in recognition of the social good their activities deliver. Whilst the degree of success in securing donations varies between universities (typically favouring the older universities), and donations only constitute a small proportion of the annual funding needs for most public universities, the trend for the future is that all public universities will be under increasing pressure to significantly increase fundraising based on philanthropy.

Notwithstanding that they presently only constitute a small proportion of the annual funding needs, donations remain vital to public universities in that the contributions and the investment earnings thereon, typically support vital research, student scholarships and high profile academic appointments. Consequently, the public universities strongly argue against any reduction of incentives to encourage giving.

The public universities do not support the use of a fixed tax offset (or a two tier system) to replace the existing tax deduction that is provided at the marginal tax rate of the taxpayer. The public university sector recommends that donations should, as a minimum, be deductible at an individual’s marginal rate of tax.

The data provided in the Discussion Paper shows that the highest level of average deductions are from taxpayers with taxable incomes exceeding $100,000. The proposed tax offset models being considered by the Working Group are likely to disadvantage and potentially discourage taxpayers on higher marginal tax rates from making gifts. Whilst survey data would be required to better determine the propensity of those taxpayers to be discouraged from making gifts, and the quantum of those gifts, the public universities are concerned that any such change is likely to be detrimental to the encouragement of philanthropy.

Instead, the public university sector encourages the working Group to strongly consider whether enhanced tax incentives designed to encourage greater levels of giving (i.e. which involves a deduction rate set at a level higher than the individual’s marginal rate of tax) would be more effective and reduce the reliance on Government funding.

Q26 Should the threshold for deductible gifts be increased from $2 to $25 (or some other amount)?

Whilst the majority of public university philanthropic fundraising generally involves amounts exceeding the thresholds being considered by the Working Group, we would tend not to support a proposal that would increase the threshold for deductible gifts.

The Discussion Paper does raise a number of likely valid efficiency based arguments, but the public universities are concerned that there are no guarantees that donors, who may initially be discouraged by a higher threshold, will necessary change their behaviour and increase the level of deductions or pool deductions, with no reduction to the overall level of gift giving. Again, survey data would need to be obtained to ascertain the reliability of such assumptions.

Notwithstanding that the threshold change may be considered relatively minor, there is a general concern that such a change may tend to send an inappropriate message to donors that the Government now values philanthropy less. This could inadvertently discourage the future philanthropic practices of Australians.

Q19 - Would a clearing house linked to the ACN Register be beneficial for the sector and public?
It would be beneficial for the public and beneficial for smaller charities with no current on-line giving facilities. It would give universities another place to receive donations and it is also good for donors as it will be linked to their tax return thereby ensuring deductions in cases of lost receipts.

Q23 Are there additional barriers relevant to increasing charitable giving by corporations and corporate foundations?

The rules around deductions for charity events where the minor benefit cannot exceed $150 or 20%
of the value of the contribution do not appear fair. We submit that the better approach would be to
maintain a minimum threshold of $150 but allow a deduction equal to difference between the value of the
benefit and the amount contributed, where the benefit is less than, say, 40% of the contribution.

This would avoid the perceived unfairness which would result where, for example, a donor pays $1 million
for a painting worth $200 and receives no offsetting tax deduction.

CHAPTER 3 – FRINGE BENEFITS TAX CONCESSIONS

Q 29 & 37 – Entitlement to FBT rebate

In response to questions 29 and 37 of the Discussion Paper, we believe that ideally, the entitlement to the
FBT rebate should be amended to be consistent with the income tax exemption provisions. Alternatively,
at the very least, the FBT rebate criteria should be amended to include all not-for-profit entities operating
in the public education sector. Capped exemption from FBT is currently provided to private universities
and schools as well as medical research institutions. It would be consistent with the recognition of the
community service undertaken by public universities to extend this exemption to NFP universities. In
addition to the arguments in Appendix A, we make the following additional comments.

Under the income tax exemption provisions, universities are considered exempt by way of their purpose
in the community as public education institutions that have a physical presence in Australia and that incur
their expenses and pursue their objectives principally in Australia (s50-5 & 50-55 ITAA 1997). However,
there is currently no such similar basis that would entitle them to a rebate for FBT purposes. This is
notwithstanding the dominance of schools and research institutions entities in the education sector, as
well as other non public tertiary institutions, that are entitled to the FBT rebate. Other education
institutions operating in the same sector as the universities are able to effectively half their FBT costs.

This appears to be in direct contrast to the original intention when the FBT rebate legislation was
introduced to the FBT Act. When the FBT Act was amended to value benefits at their tax inclusive value,
amendments were also introduced to ensure that tax exempt entities were no worse off than if the tax
exclusive value of benefits was used for FBT purposes. However, when enacted into legislation, the
provisions were written such that only certain tax exempt employers were entitled to the FBT rebate.
Over the course of the following 20 years, numerous additions, revisions and alterations have been made
to the rebate provisions and they now bear little resemblance to the original arrangements. Accordingly,
we suggest any rewriting of the rebate provisions should revolve around simplification such that entities
entitled to income tax concessions are entitled to the FBT rebate, if not full FBT exemption. Where this is
not possible, in the alternative, we would at the very least suggest that all public education institutions be
entitled to the same FBT rebate.

Q 31 & 32 – meal entertainment and entertainment facility leasing expenses

Where the FBT rebate is extended more broadly to non-profit employers, or at least to those specifically
in the public education industry, we would accept the introduction of a cap on salary sacrificed meal
entertainment and entertainment facility leasing expenses (EFLE) benefits as a reasonable compromise to
maintain revenue neutrality.
Whether these benefits are included in the current cap, or subject to their own cap (e.g. $15,000), the universities do not have a preference. Ultimately, provided employees of all not-for-profit entities are entitled to the same caps, it will result in an equitable outcome for the industry. However, we note these benefits are currently excluded from the existing caps because of the practical difficulty and cost that would be involved in tracking items to individuals as is required to apply the caps. Accordingly, for simplicity, any change should be directed at amounts specified in a salary sacrificed arrangement rather than meal entertainment and EFLE benefits provided in the ordinary course of the employer's operations. Any other approach would impose a disproportionate cost on employers relative to the issue sought to be addressed.

Q 34 - FBT rebate caps

In order to recoup costs involved with expanding the eligibility to the FBT rebate, we accept that it may be reasonable to look at the feasibility of limiting employees to only one rebate cap per annum, regardless of the number of rebatable employers for which they work.

However, whilst there may be merit to the concept of limiting the FBT rebate cap on a per employee (rather than per employer) basis, we agree with the concerns in the Working Group’s Discussion Paper that this will create significant additional compliance burdens on employers. We suggest more work would be needed to identify an equitable system, and the approach should only be taken if it can be confirmed that this will not result in significant additional compliance for employers.

Q 36 - Minor Benefit Exemption

Under the FBT Act, generally, benefits that have a nominal value of less than $300 and that are provided on an infrequent and irregular basis are exempt from FBT where it would be considered unreasonable to treat them as fringe benefits. However, whilst this general provision applies to most categories of fringe benefits, it does not apply to tax exempt body entertainment (TEBE) fringe benefits. Therefore, when tax exempt employers provide their employees with what would otherwise be deemed to be entertainment (recreational or otherwise), they are unable to apply this exemption, except in the most rare of cases. Effectively a de minimis test for small benefits, the minor benefit exemption allows employers to exclude small items from their FBT return. However, tax exempt employers are required to scrutinise every line item of their journal entries to find potential fringe benefits.

Given the small dollar value of benefits involved and the fact that NFP entities do not generally engage in significant entertainment activities, we suggest it does not follow sensibly that the minor benefit exemption should be denied to tax exempt employers. There is a significant amount of additional administration required to monitor this rule for these employers, for relatively few dollars gained for the ATO. On a practical level denying this exemption effectively prevents many entities from having an annual social gathering (Christmas Party or End of Financial Year Party etc) that would otherwise be a minor benefit for taxing employers. That is, it is effectively a tax on NFP entity Christmas parties.

There is no equitable reason why the minor benefit exemption should not be applicable to TEBE.

CHAPTER 4 - GOODS AND SERVICES TAX CONCESSIONS

The existing GST concessions should be maintained in their current form.

In particular, the continued availability of the GST-free concession under section 38-250 of the GST Act, for supplies of accommodation and other supplies for nominal consideration, is widely recognised as a key concession for the university sector. The primary use of this concession by the Universities is to support the provision of various services to their students.
The removal of this concession would impact heavily on the ability of the Universities to provide a number of services but, in particular, affordable accommodation, impacting not only the Universities' finances generally but also their ability to attract international students and students from outside the regional area of the university.

The suggested reform at paragraph 197 of the Discussion Paper to change from a GST-free concession to an opt-in arrangement to treat supplies as either input taxed or taxable would adversely impact the Universities' ability to supply affordable accommodation by effectively removing the benefit they currently enjoy as a result of this concession. Currently, student accommodation would, in the absence of any section 38-250 concession, be generally treated as input taxed. The opt-in alternative would therefore effectively result in the removal of any concession. Such a suggested change could result in either an increase in the price of student accommodation or the Universities bearing significant additional costs as a result of the removal of the ability to claim GST input tax credits on costs they incur in respect of the provision of student accommodation.

Therefore, the Universities are seeking to maintain the current forms of concessions available under the GST Act.