

Victorian Parliamentary Internship Research Report

# On the taxation of religious charities and the public benefit of charitable exemptions

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## Executive summary

This report provides an examination of the grounds on which organisations can be eligible for tax concessions. The focus of the enquiry is specifically religious charities that attain fiscal privileges on the basis of ‘advancement of religion’ as their charitable purpose. The report proceeds from the historical and theoretical basis for charitable status and how it operates in Australia. It is imperative to ground discussion around the relationship of the state to religious organisations in philosophical conceptions of the state and its responsibilities towards its citizenry. Findings of the report are that charity law in Australia is consistent with common law counterparts, namely Canada and the UK and dissonant with the approaches adopted in civil law jurisdictions like Italy and Germany. Conclusions of the report establish the necessity to reform charity law to remove the unfounded deferential treatment towards religion at law. This must be done in such a way as to support beneficial activities that some religious organisations carry out but limiting scope for abuse of the preferential fiscal regime available to charitable organisations. Reforms suggested to enact these objectives are: removing the presumption of benefit that exists in Australian charity law; and the abolishment of the ‘advancement of religion’ as a distinct charitable head. The major limitation of this report is its brevity. The subject area is complex and requires detailed examination. Constraints in length mean that extensive theoretical grounding could not be provided nor detailed comparisons with foreign jurisdictions. As such, the report forms part of a growing body of work to inform discussion on policy reform that needs to be undertaken to bring the regulation of the charitable sector in line with contemporary society’s needs and expectations.

## Introduction

Religious organisations account for a large proportion of Not-For-Profit (NFP) organisations in Australia that are eligible for considerable legal and fiscal privileges if they qualify for charitable status. The importance of the Non-For-Profit sector should not be understated. It provides many important social services as well as contributing significantly to employment and the economy more broadly. The sector employs 6.8% of Australians in employment, contributes around 3.3% to GDP by 2008 figures<sup>1</sup>. For Australia, the sector is economically significant, provides important social services, and accrues indirect support from the tax payer by way of subsidies, tax exemptions and other legal privileges to be examined later. The law that regulates the charitable sector however is based on out-dated traditions imported from England at federation and has undergone little substantial change since, even as society has evolved dramatically. It is time to review the present state of the law in Australia and overseas as part of the public debate on how best to negotiate the relation of religion to society for greatest net benefit for Australia.

Any examination of the relationship between the state and religious must depart from a conception of the good that the state seeks to endorse. A Rawlsian framework of reasonable plurality of incompatible comprehensive doctrines appeals as the most appropriate for a country so multi-theistic as Australia. This framework accepts the equal validity of private convictions anywhere on the spectrum of religiosity to atheism and allows for ideologies like humanism and rationalism. This approach also demands that faith plays no role in public policy because its proper remit is exclusively in personal convictions on topics where reason is unavailable. It is indisputable that such matters are of concern to private citizens who are entitled to freedom of faith (secular or theistic), but political justice must necessarily be blind to arguments that do not proceed from empirically demonstrated truths so as to originate from uncontentious positions to best discharge the polity's duty of care before its citizens.

## Charitable status for religious organisations

The purpose of this report is to interrogate the relationship between the state and religious organisations in the granting of 'charitable' status and subsequent fiscal privileges to organisations for the 'advancement of religion'. Fiscal privileges afforded to charitable organisations are lost revenue for the Treasury and are commonly perceived as an indirect subsidy of these organisations by the state. Exact figures are unavailable but a commonly cited estimate from 2009 suggests that religious tax exemptions cost Australia \$31billion per annum<sup>2</sup>. Of all registered charities in Australia, 37.4% report advancement of religion as their charitable purpose which is the biggest category<sup>3</sup>. The granting of charitable status to religious organisations is a historical artefact that has been preserved throughout centuries and is increasingly coming under scrutiny in secular liberal societies as an unacceptable form of state funded support for religion in a vastly different socio-political landscape to the one contemporaneous to the origins of these exemptions.

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<sup>1</sup> O'Halloran, K., McGregor-Lowndes, M., & Simon, K. (2008) *Charity Law and Social Policy: national and international perspectives on the functions of the law relating to charities*, Springer Publications pp 230

<sup>2</sup> Gomes, F & Perkins, L (2009) 'Taxes and subsidies: the cost of "advancing religion"', *Australian Humanist*, no 93

<sup>3</sup> Cortis, N et al (2015), 'Australian Charities Report 2014', *Centre for Social Impact and Social Policy Research Centre*, UNSW: Australia, pp 31

Charitable purposes at law are those, considered by government to be performed for the public benefit, relieving the state of the obligation to provide the same and thus make the organisation eligible for tax exemptions to encourage the beneficial activities.

Common law tradition of activities for the 'advancement of religion' being considered charitable at law stems from the 19<sup>th</sup> century. Society of the 19<sup>th</sup> century was different to today in many ways, especially the role of religion in public life and provision of social services which was dominated by the church. Religion was considered to form the basis of the need to 'do good' out of fear of Hell<sup>4</sup> and thus charitable actions and religious faith were inseparable. Therefore religion was accepted as *a priori* charitable without further consideration. Today, when people can separate motivations for benevolent activities from fear of Hell, the default charitable status of religious organisations ought to be reconsidered. While religion can motivate persons to perform charitable activities, these activities must be considered charitable of themselves and not based on their religious motivation<sup>5</sup>. There is a lack of empirically demonstrable benefit of religious belief that does not manifest in socially beneficial activities like provision of education, and care for the sick or impoverished.

The reverence with which topics of religion have often been treated should be reconsidered. Positions stemming from piety must be re-evaluated and made adherent to public reason or else abandoned. Throughout the development of common law on the topic of charity law, courts have noted that "benefits alleged to arise from the performance of purely religious acts [are] non-measurable and therefore non-charitable"<sup>6</sup>. Yet purely religious trusts and organisations continued to have their charitable status affirmed by the courts while some judges explicitly express the importance of charity law being reflective of society of the day rather than being held back by values and notions of a former time and a different society<sup>7</sup>.

It has been noted that courts cannot simply accept the statements of the faithful that benefit from individuals' belief is accrued to the public at large; secular courts must themselves ascertain the presence of public benefit<sup>8</sup>. Private benefits of religious faith cannot be passed off as public benefit because they fall under the charitable head of 'advancement of religion'<sup>9</sup>. Advancing religion is most evidently for the public good when it lends itself to establishing programs for purposes such as relief of the poor, provision of healthcare, or education, but these are ancillary to religious belief. Singling out 'advancement of religion' as charitable in and of itself is problematic given that many of the public goods associated with it are also associated "with secular beliefs and practises that are functionally similar to religion"<sup>10</sup>, lending weight to arguments that 'advancement of religion' is a redundant charitable purpose.

The status of religious organisations as charitable is the product of a historical religious prominence rather than any empirical evidence as to the benefit of such activity. The operation of the charitable heads needs to be re-evaluated because the legal meaning of charity is that the benefits of the claimed

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<sup>4</sup> Waters, D (2011), 'The advancement of religion in a pluralist society (Part I): distinguishing religion from giving to 'charity', *Trusts & Trustees*, vol 17, no 7, pp 659

<sup>5</sup> Waters, D (2011a) pp 665

<sup>6</sup> *Gilmour v Coats* 1949 In Waters, D (2011b) pp 731

<sup>7</sup> *National Anti- Vivisection Society v IRC* 1948 AC 31, Lord Simmonds at 69/70

<sup>8</sup> Waters, D (2011b) pp 730

<sup>9</sup> Waters, D (2011b) pp 731

<sup>10</sup> Harding, M (2014), *Charity Law and the Liberal State*, Cambridge University Press, pp. 236

activity are considered important enough to be supported with public funds<sup>11</sup>. The State has valid interest in regulation of the charitable sector to ensure it secures a good deal in terms of the public service provision that it would otherwise be obliged to fund, and the provision is good value for the foregone tax revenue<sup>12</sup>. Tax exemption for the provision of public goods also removed the state's right to decide which areas of social need benefit from that tax allocation<sup>13</sup>. In a libertarian conception of government, this position is defensible but in present society, while health services are suffering from underfunding and other public goods like education and welfare are increasingly strained, the prospering pursuit of advancement of religion with its intangible and questionably 'public' benefits is problematic. The relationship between the state and the NFP sector in provision of public benefit is necessarily one of partnership where at present, the state in Australia is failing to exert its legitimate authority to secure efficiency and cost effectiveness for the public.

## On the necessity of pluralism of comprehensive doctrines and the limited scope for faith

In Australia it is evident that religious affiliation is still a majority phenomenon in our population. 2011 census data revealed 68% of respondents to the optional question self-reported religious affiliation. Yet religious affiliation is in decline.<sup>14</sup> Further, active participation in religious organisations stands at roughly 10% of the population and these are significant factors when evaluating the role of religion in the lives of citizens. Australia's religious diversity is presently extensive in scope, with 120 religions reported in 2011 with 250 or more followers. Religious adherents are overwhelmingly Christian, accounting for 61% of respondents with non-Christians accounting for 7% of respondents.

A purpose of society is to facilitate conditions for the pursuit of reasonable, divergent conceptions of the good. In a pluralist society like ours, this can be accomplished by permitting an overlapping consensus of "all the reasonable opposing religious, philosophical, and moral doctrines likely to persist over generations and to gain a sizeable body of adherents"<sup>15</sup>. Given the persistence of comprehensive moral doctrines (religious or secular), the political conception must be such that can it accepted by persons holding any of these reasonable comprehensive doctrines. Thus the political system must not be in conflict with the relative doctrines and therefore not derived from, or specifically endorsing, any individual doctrine. Accepting the premise that where reason is available, faith has no place, a viable political conception would then be consistent with evidence based methodologies, allowing for the *private* pursuit of any religious conviction consistent with reason and with the capacity to enhance well-being of its adherents.

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<sup>11</sup> Harding, M., O'Connell, A., & Stewart, M., (2014) *Not-For-Profit Law: Theoretical and Comparative Perspectives*, Cambridge University Press: Cambridge pp 111

<sup>12</sup> O'Halloran, K., McGregor-Lowndes, M., & Simon, K. (2008) pp 13

<sup>13</sup> O'Halloran, K., McGregor-Lowndes, M., & Simon, K. (2008) pp 16

<sup>14</sup> The number of people reporting no religion in Australia has increased substantially over the past hundred years, from one in 250 people to one in five. In 1911 there were 10,000 people (0.4%) who chose the option 'No religion' on their Census form; in 2011 there were just under 4.8 million (22% of Australians)

'Percentage of People (a) Reporting No Religion (b), 1911-2011' Australian Bureau of Statistics accessed at <<http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/4102.0Main+Features30Nov+2013>>

<sup>15</sup> Rawls, (1993) *Political Liberalism*, NY Columbia University Press

The proper place for religious faith for rational persons is all areas of life that are fundamentally mysterious<sup>16</sup> or unknowable where faith provides explanation in the absence of reason. With advancement of science, the areas that remain mysterious or unknowable are decreasing in number and scope and thus the breadth of religion's remit to the rational person is decreasing. Per Rawls, reasonable persons ought to accept reason above faith everywhere it is available. Yet to suggest that in the private convictions of persons the remit of religion is diminished, is not to accept that we can do away with religion all together. In the personal convictions of religious persons on matters where reason is unavailable, faith can promote well-being and encourage performance of socially beneficial activities which ought to be supported by the government equally whether their origin is religious or secular.

Ultimately, this report does not deal with the merits of religion or religious belief, nor whether freedom of religion is beneficial to society, those topics are beyond the scope of this paper. This report addresses the regulation of the charitable sector that enjoys considerable concessions in order to interrogate whether the present regime gives Australia the most benefit in exchange for the lost tax revenue of those concessions.

## Operation of 'advancement of religion' in Australia

Advancement of religion as a charitable head is adopted from common law<sup>17</sup>.

A challenge that 'advancement of religion' as a charitable purpose poses to effective regulation of the charitable sector is its scope for abuse by quasi-commercial entities under the guise of religion. Australian courts have ruled that charities are able to run commercial enterprises that create profit, enjoying charitable fiscal privileges, provided that income was destined to further the charitable purpose in question<sup>18</sup>. It is hard to deny charities the right to generate profit to fund socially necessary activities like forms of welfare provision to the homeless or impoverished. However, the landscape looks vastly different when charitable organisations whose purpose is to advance **[their]** religion run enterprises for profit, designed solely for the 'advancement of religion' which brings no benefits to society and yet enjoy the same tax concessions as publicly beneficial organisations. Such examples include the church of Scientology, the Hillsong Church and Paradise Community Church which have all been described as cultish, harmful to their members and yet they claim fiscal exemptions for activities like dissemination of their music CDs, hiring stadiums for evangelical events to extract donations from their loyal adherents<sup>19</sup>.

## The problem of the presumption of benefit

In order for a purpose to be charitable at common law, it must fit under the Pemsell heads<sup>20</sup> and be for the public benefit. The latter requirement is a two-part test, the benefit must accrue to the public or a sufficient part thereof (so the organisation cannot benefit only donors or those related to the directors);

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<sup>16</sup> Macklem, T (2000) 'Faith as a Secular Value', *McGill Law Journal* vol 45, pp 51

<sup>17</sup> Per Justice Donovan: "to advance religion means to promote it, to spread its message ever wider among mankind; to take some positive steps to sustain and increase religious belief; and these things are done in a variety of ways which may be comprehensively described as pastoral or missionary" In *United Grand Lodge of Ancient Free and Accepted Masons of England v Holborn Borough Council* (1957) 1 WLR 1080 in Picarda, H (1999) *The law and practice relating to charities*, 3rd ed, Butterworths: London pp 84

<sup>18</sup> *Commissioner of Taxation v Word Investments* in O'Halloran, K., McGregor-Lowndes, M., & Simon, K. (2008) pp 246

<sup>19</sup> Ferguson, A (2005) 'Charity cases' *BRW*, March 24-30

<sup>20</sup> The *Pemsell* case (1891) forms the authoritative iteration of religious organisations being considered de facto charitable as it was explicitly named one of the four charitable heads (referred to as the Pemsell heads): The relief of poverty; The advancement of education; The advancement of religion; Purposes beneficial to the community and not falling under any of the preceding heads



and the activities must be demonstrably beneficial. In relation to the first three Pemsel heads, historically a presumption of 'benefit' has operated and continues to operate in Australia to this day. When it comes to claims of spiritual benefit in certain "advancement of religion" cases, courts appear deferent to religious belief about the benefits claimed"<sup>21</sup>. The formulation of the presumption is inherited from common law with esteemed judges upholding its operation. "Some benefit accrues to the public from the attendance at places of worship of persons who live in this world and mix with their fellow citizens" J Cross in *Neville Estates Ltd v Madden*<sup>22</sup> suggesting that merely attending places of worship makes the actions of someone beneficial to society which is a tenuous logical link. At present, section 7 of the *2013 Charities Act (Cwth)* contains such a presumption explicitly stated:

### **7 Certain purposes presumed to be for the public benefit**

In the absence of evidence to the contrary, a purpose that an entity has is presumed to satisfy the requirements of paragraphs 6(1)(a) and (b) (purposes for the public benefit), if the purpose is any of the following purposes:

- (a) the purpose of preventing and relieving sickness, disease or human suffering;
- (b) the purpose of advancing education;
- (c) the purpose of relieving the poverty, distress or disadvantage of individuals or families;
- (d) the purpose of caring for and supporting:
  - (i) the aged; or
  - (ii) individuals with disabilities;
- (e) the purpose of advancing religion.

The presumption stands "in the absence of evidence to the contrary" meaning the presumption operates *a priori* unless evidence to the contrary is brought for advancement of religion along with several other recognised charitable purposes. It is possible to contend that departing from a robust freedom of faith argument, allowing state support of religious and other intangible conceptions of the good is reasonable so long as they do not promote hate or actively cause harm so as not to impinge on the freedoms of citizens to hold personal doctrines that are not materialistically founded. This is a reasonable ethical position and could be upheld at the federal level but it must be endorsed as such and not under the current approach of pious and deferential treatment of religion based on presumptions of its benefit to society that are unproven and largely unexamined.

<sup>21</sup> *Nelan v Downes* (1917) 23 CLR 546 HCA

<sup>22</sup> In Ridge, P (2011), 'Religious Charitable Status and Public Benefit in Australia', *Melbourne Uni Law Review*, vol 35, no 3, pp. 1071 pp 1075

While reform in this area of law is sensitive, it is imperative to keep perspective on the intentions of the law. The inclusion of religion as a charitable purpose dates back to a time when welfare was not provided by the state as we know it but rather the various Christian churches in the local areas<sup>23</sup>, society has undergone extensive transformation since then, making this defacto charitable category obsolete. In the 21<sup>st</sup> century, state concessions should be disbursed rationally and when benefit of activity cannot be quantified, organisations should not be entitled to regulation departing from an unfounded presumption that spares them from following the same regulations as other charities<sup>24</sup>; namely operating under a presumption of benefit that only applies to several charitable purposes<sup>25</sup>. It is neither rational nor justifiable that the advancement of religion should be considered, of itself, a public benefit.<sup>26</sup>

## Fiscal privileges at the Victorian State and Federal level

### State level

At the Victorian State level, concessions include:

- Land Tax exemption<sup>27</sup>
- Payroll Tax<sup>28,29</sup>
- Stamp duty exemption<sup>30</sup>

### Federal level

At the Commonwealth level, concessions include:

- Exemption from income tax for eligible entities<sup>31</sup>
- Capital Gains Tax exemption for registered religious charities and trusts
- GST concessions<sup>32</sup>
- Exemption or rebate under the Fringe Benefits Tax regime<sup>33</sup>

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<sup>23</sup> Perkins JL (2011) 'submission for the Inquiry into the Definition of Charity' <http://secularparty.wordpress.com/2011/12/06/submission-for-the-inquiry-into-the-definition-of-charity/>

<sup>24</sup> Perkins JL (2011)

<sup>25</sup> S7 Charities Act 2013

<sup>26</sup> Perkins, JL (2008) 'Re: review of Australia's future tax system', *Secular Party of Australia* letter to AFTS Secretariat (The Treasury)

<sup>27</sup> - for land that is exclusively for charitable purposes per State Revenue Office Victoria Ruling (2007) "land used exclusively for charitable purposes", *Land Tax act 2005, Revenue Ruling LTA 004*

<sup>28</sup> - 'religious or public benevolent institution' or a 'charitable body' is exempt from Payroll Tax obligation for wages paid to employees exclusively engaged in religious or public benevolent employment' Babie, P (ed) (2015) 'Chapter 365 -Religion', *Halsbury's Laws of Australia* ch 365- 460

<sup>29</sup> wages to employees of enterprises owned by religious charities but not themselves fulfilling the charitable purposes are not eligible for payroll tax exemption 'Exemption for wages paid by non-profit organisations and religious and public benevolent institutions' Payroll Tax Bulletin SRO Jun 2012 PTX2/12 <http://www.sro.vic.gov.au/node/230>; Payroll Tax Act 2007 (VIC)

<sup>30</sup> Duties Act 2000 (Vic): charitable organisations at law are eligible for exemption from duties listed in the Duties Act including on the transfer of property; declaration of trust over property; certain registration duties on particular vehicle

<sup>31</sup> *Word Investments* case entrenched the 'destination of income' test into charity law; once it is demonstrated that income earned is for charitable purposes, the means by which it is raised does not erase its charitable tax exemptions this means that charities can run for profit businesses that enjoy income tax exemption provided the profits are used for pursuit of the named charitable purposes per McGregor-Lowndes, M (2010), *Modernising Charity Law: Recent Developments and Future Directions*, Edward Edgar Publishing: Cheltenham pp 5

<sup>32</sup> over 80% of charities are registered for GST and are able to claim a refund for the GST component of the goods and services they buy Knight, P & Gilchrist, D (2015) 'Australia's Faith-based Charities 2013: A summary of data from the Australian Charities 2013 Report', *Curtin University* pp 26

<sup>33</sup> Benefits provided to employees of religious institutions are exempt where the employer is a registered religious institution; the employee is a religious practitioner; a benefit provided to an employee, their spouse, or child; the benefit is directly related to their pastoral or other duties Babie, P (ed) (2015) 'Chapter 365 -Religion', *Halsbury's Laws of Australia*, ch 365

- Deductible Gift Recipient (DGR) status eligibility\*\* - Not applicable to most organisations that only 'advance religion' and state no other purpose, less than 5% of charities have DGR status

## The goals of reform:

Reforms must address issues identified with the current regime in a manner that is cost-effective and would result in net gain for Australia, considering both costs and benefits of any measure suggested. Lack of accountability for indirectly publicly funded activities is commonly cited as an issue with the current state of charitable law. Any reform must attempt to “strike a balance between minimising ...burdens placed on registered entities, while ensuring appropriate accountability and transparency”,<sup>34</sup> to ensure the good works that the NFP sector undertakes are encouraged but in a way coherent to public views and sensibilities.

A further goal of reform is to restore confidence in the sector. One way this can be achieved is by erasing the socially aged purpose of advancing religion, so that the beneficial activities can be subsumed by other categories of charitable purposes. This would be an important step given the public's diminishing faith in the sector and growing perception of the harms of the sector outweighing its benefits. A growing concern is international findings that charities are susceptible to becoming vehicles for money laundering<sup>35</sup> given the relatively sparse regulation and excessive trust placed in the entities by regulators. For instance, best estimates of the Canada Revenue Agency suggest that for cases under current criminal investigation, such abuses represent a loss of \$200 million in tax revenue<sup>36</sup>. The public perception of religion is also suffering from a crisis of confidence: public appetite for transparency and accountability are met with reports of rampant and systematic abuses of religious organisations of their own congregations. Particularly troubling are the abuses against the most vulnerable of those such as children<sup>37</sup>. In such a climate, it appears irresponsible to allow organisations whose sole purpose is unaccountable 'advancement of religion' to receive tax payer support.

## Reform: the removal of the presumption of benefit<sup>38</sup>

The presumption of benefit gives organisations with the stated purpose of advancement of religion access to fiscal privileges on the basis of intangible and unquantifiable benefits to society. This application of the public benefit test to establish charitable status is incompatible with evidence-based policy and does not represent a defensible burden on the rest of society to shoulder the exemptions enjoyed by organisations not obliged to perform any demonstrably beneficial activities. The privileges enjoyed by charitable organisations are intended to encourage beneficial activities greater than the loss of foregone revenue and this standard cannot objectively be met by religious organisations that pursue no charitable purpose beyond the 'advancement of religion'. Charity law is a particularly dated area of the law where principles still deployed are centuries old so common law on the area must necessarily be

<sup>34</sup> Explanatory Memorandum to the ACNC Act 2012 (Cth) 69 [6.6]

<sup>35</sup> See eg. OECD (2009) “report on the abuse of charities for money laundering and tax evasion”

<sup>36</sup> OECD (2009) pp 15

<sup>37</sup> Betrayal of Trust Report, *Victorian Parliament*, tabled 13/11/13 accessed 10/05/16 at < <http://www.parliament.vic.gov.au/fcdc/article/1788>>

<sup>38</sup> Note: This reform was attempted in 2010 when Senator Xenophon of the Commonwealth Parliament introduced a bill to reform income tax law<sup>38</sup> to insert a positive public benefit test to apply to all charitable purposes. While this reform was unsuccessful then, it should be reconsidered as a way to bring Australian charity law in line with current social conditions, considering that religious affiliation is in decline and religious services are attended by a small minority of the public.

read in its historical context<sup>39</sup> and at present, the law is dissonant with realities of the role of religion in Australia.

Justice Kirby expressed this sentiment in dissenting judgement in *Federal Commissioner of Taxation v Word Investments Ltd*:

*“as a generally applicable principle, it is important to spare general tax payers from the obligation to pay income tax effectively to support or underwrite the activities of religious... organisations with which they disagree”*<sup>40</sup>

A robust Public Benefit test can be created. While in principle it ought to conform to a sound evidential scheme, in practice, this presents a challenge because such a test must not delve into the merits of beliefs but rather whether the practise of belief confers any public benefit. In a pluralist society like ours, a high level of abstraction as to the benefits of belief can be adopted but the benefits of worship to society at large would still need to be presented rather than presumed. An approach that requires affirmation of the benefit of faith and the lack of harm caused by the particular group to its members and the community will likely not affect most organisations presently considered charitable. The symbolic impact of removing the presumption of benefit for ‘advancement of religion’ is significant along with potential for the exclusion of presently presumed groups whose activities are cult-like or harmful to their own members and cannot be defended even at a high level of rational abstraction.

This reform has taken place in the UK, with statutory iteration of the abolishment of the presumption as follows:

*Charities Act 2011, Chapter 4(2): “In determining whether the public benefit requirement is satisfied... it is not to be presumed that a purpose of a particular description is for the public benefit”*

The abolishment of the presumption has had limited practical impact on the operation of charity law<sup>41</sup>. However, the implication of the reform is that it paves the way for increasingly progressive approaches to charitable status. The Charity Commission in the UK has indicated that benefit must ‘be capable of proof, through factuality and positive evidence’ and that ‘expression of opinions and beliefs are not enough’, and that ‘factual evidence produced must be sufficient so that the courts are capable of evaluating it’<sup>42</sup> which are standards worthy of imitation and increasingly robust deployment.

## Reform: abolish ‘advancement of religion’ as a separate charitable purpose

This reform would have greater impact than simply removing the presumption of benefit because:

- It allows measurable and tangible outcomes to form the basis of charitable status even if they happen to be religiously motivated

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<sup>39</sup> Ridge, P (2011) pp. 1078

<sup>40</sup> *Federal Commissioner of Taxation v Word Investments Ltd (2008) 236 CLR 204, 248 [110]*

<sup>41</sup> See eg Harding, M (2014) pp 28 , examples of a 2010 decision to register the Druid Network as a charity. The Charity Commission considered submissions on a variety of positions on the possible benefits of the practise of Druidry before conceding that the public benefit test was met despite the lack of demonstrated benefit to the public of the group’s worship practises.

<sup>42</sup> Charity Commission of England and Wales, *Analysis of the Law Underpinning Charities and Public Benefit*, rev. edn (2011), 2.4

- It would embrace the principle that private activities need not be supported by the state unless they provide meaningful social benefits given that the link between private worship and public benefit is too intangible for rational policy making
- Religious charities that perform socially beneficial activities beyond those that constitute only advancement of religion would still qualify for fiscal exemptions for those activities that are socially beneficial such as provision for the disadvantaged in the community

In practise, such a method is politically difficult and challenging to implement. One issue flagged in submission to the UK Charities Commission is that forcing religious charities to meet the demands of charitable status in the absence of 'advancement of religion' as a valid purpose would be injurious to those organisations that are overwhelmingly small community based groups<sup>43</sup>. The harm is that it would require those charities to undertake secular activities to qualify for benefits which places burdens on those organisations that detract from their primary activities of worship, evangelism, ritual and ceremonial practises which can only qualify presently under 'advancement of religion'<sup>44</sup>. Yet, the entity is supported by charitable fiscal privileges based on the activities undertaken and not their origins, given that the test is 'public benefit' not 'beneficial intent'. As such, encouraging organisations eligible for benefits to engage in socially beneficial activities can only result in net gain for society.

Of all charities reporting advancement of religion as one of their purposes, 62% did not nominate any other purpose, 24% also included advancement of education, 18% relief of poverty, sickness or the needs of the aged, 3% provision of childcare and 16% other purposes beneficial to the community<sup>45</sup>. This data indicated that a large proportion of charitable organizations could register under alternative charitable heads that that are of public benefit and the 62% that listed no other purposes would be obliged to perform socially beneficial activities to qualify for fiscal and legal privileges.

Sensitivity to diverse conceptions of the good is warranted in a pluralist society and it would indeed be harmful to the faithful to suggest that their beliefs have to be defended in terms of material benefits alone<sup>46</sup> but that is not the purpose of such reform. Indeed, the aim is not to attack freedom of worship and religion but rather withdraw tax funded subsidies from organisations that provide no proven benefits to broader society.

## International case studies – civil law jurisdictions

Europe operates a system of mutual interdependence of State and religion<sup>47</sup>. There are several forms of direct or indirect State financial support for religion: 'church tax'; tax concessions; subsidies for public services performed; compensation for historical confiscation and damage<sup>48</sup>. The regimes are vastly different to those in common law countries due to the different history of state relation to religion in formal arrangements for the provision of social services. For purposes of comparison with Australia,

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<sup>43</sup> Waters, D (2011b) pp 734

<sup>44</sup> Ridge, P (2011) pp 1074

<sup>45</sup> Knight, P & Gilchrist, D (2015) pp 3

<sup>46</sup> Waters, D (2011a) pp 666

<sup>47</sup> Doe, N (2011), 'The Property and Finances of Religion', *Law and Religion in Europe: A Comparative Introduction*, Oxford University Press pp 175

<sup>48</sup> Doe, N (2011) pp 175

these jurisdictions offer insight into a more integrated model of governance between the state and the charitable sector.

## Germany

In Germany, the law provides considerable incentive to encourage the financing of public-benefit. The means of doing so is quite different to the approach in Australia. While they also allow deduction of donations, they uniquely provide to certain religious groups dedicated funds from a tax on the religious population called the Kirchensteuer, and various other public subsidies for religious communities. Demographically, 30% of Germany's 80.8million population are registered Roman Catholics and 29% are registered Protestants<sup>49</sup>. The Kirchensteuer is collected as a proportion of income tax (8-9% of total income and capital gains tax liability) and then distributed by the state to the religious organisation, approximately 80% of the budget of the Protestant and Catholic Churches in Germany are funded by the church tax<sup>50</sup>. Tax authorities review whether organisations have met requirements for public-benefit status every three years based on tax returns submitted by the association<sup>51</sup>. The Roman Catholic Church as well as the Protestant/Lutheran Church in Germany has corporation status under public law meaning they have the right to levy a church tax on their members<sup>52</sup>. The only way to avoid paying this tax is to formally leave the church and rescind the right to participate in Church rites and ceremonies like marriages and burials<sup>53</sup>. This opt-out system means citizens that do not wish to support religious organisations through their tax contributions do not have to<sup>54</sup>. This system means that the congregations themselves pay for the continued operation of the religious organisations. The Churches that qualify for receipt of the religious tax revenue spend around 20% of their church tax income towards charitable purposes<sup>55</sup>. Public law status also means they are exempt from bankruptcy law, corporate income tax, inheritance and gift taxes<sup>56</sup>.

The German system is very different to Australia's partly owing to the levy of the tax on the religious but also because of the close symbiotic relationship between the registered religious organisations and the government in the area of public service provision. Germany's religious organisations have an established role, being the predominant local suppliers of public goods and local services which include kindergartens, recreation centres, schools, nursing homes and hospitals<sup>57</sup>. The German system has been described as a tripartite relationship between destitute persons, the state and the service providers; the state enters into contractual relationships with service providers on agreements incorporating service standards and cost reimbursements<sup>58</sup> resulting in targeted provision of social services according to local community needs.

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<sup>49</sup> Gummer, C (2014) 'Germany's Faithful Balk at Tweak to Church Tax', *Wall Street Journal Europe*, Sep 3 2014

<sup>50</sup> Doe, N (2011) pp 175

<sup>51</sup> OECD (2009) "Report on abuse of charities for money laundering and tax evasion" pp 7

<sup>52</sup> Robbers, G (2013) 'Recent legal developments in Germany: Infant circumcision and Church Tax', *ecclesiastic law journal*, vol 15 pp. 69-74 pp 6

<sup>53</sup> Bacareza, HE (2009), 'The Origin and Development of the Kirchensteuer of Germany and Other European Countries', *Philippine Canonical Forum*, vol 11, pp 5

<sup>54</sup> Hoffer, S R (2010), 'Caesar as God's Banker: Using Germany's Church Tax as an Example of Non-Geographically Bounded Taxing Jurisdiction', *Washington University Global Studies Law Review*, pp 629

<sup>55</sup> Becker, T (2008) 'Religious organisations as providers of social services in Germany', *American Institute for Contemporary Germany Studies John Hopkins Institute*, pp 28

<sup>56</sup> Hoffer, S R (2010) pp 602

<sup>57</sup> Hoffer, S R (2010) pp 630

<sup>58</sup> Becker, T (2008) pp 26

## Italy

Certain states like Italy provide for individuals to allocate a proportion of their income tax to a selected religious or secular object which the state then allocates to that organisation. Limited other concessions apply to religious organisations that don't participate in such agreements with the state. Organisations that have an agreement with the state are listed on the income tax return under a category to allocate 0.8% of their income tax to a religious organisation for support of the clergy, worship services or other similar purposes, or the Italian State for measures like relief for natural disasters, refugees and conservation of cultural monuments<sup>59</sup>. This type of tax is called *otto per mille* or 'eight per thousand', and by their decision on the tax return, citizens decide how the total 0.8% levied by the state will be distributed to members of this taxation program<sup>60</sup>. There is a second similar tax, called *cinque per mille* 'five per thousand', which is distributed to non-profit bodies, volunteer activities, social promotion associations, scientific research, universities and health research<sup>61</sup>. Neither of these taxes depend on the citizen's denomination but are rather an independent decision by each taxpayer. Religious organisations are exempt from value added tax, receive a rebate of 50% on corporation tax for income in relation to charitable and educational activities, and municipal property tax is only levied on buildings levied exclusively for worship and on many buildings belonging to the Catholic Church<sup>62</sup>.

An interesting reform recently carried out in Europe relates to real estate tax regime. The European Commission found the former Italian system of real estate tax exemptions granted to non-commercial entities is incompatible with EU state aid rules<sup>63</sup>. Italy subsequently amended the system and adopted an approach that does not involve state aid contrary to anti-competition law because tax exemptions will only apply to premises where non-economic activities are carried out by non-commercial entities. The reform was instigated in response to a finding that applying tax exemptions designed for non-economic activity by non-for-profit organisations to all activities performed by those organisations constitutes unfair state aid as these for-profit enterprises compete on the same private market as normal commercial players and therefore receive an "undue advantage"<sup>64</sup>.

## Conclusions

At present, significant fiscal privileges apply to charitable organisations, some of which are religious entities of various recognised denominations. As a vestige of a deeply religious history, organisations operating for the 'advancement of religion' have enjoyed the privileged status of being deemed charitable at law without significant consideration of the nature of their contribution to society. In charity law, the main test of becoming eligible for Charitable status and the associated special tax

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<sup>59</sup> Doe, N (2011) pp 175

<sup>60</sup> Durisotto, D (2010) 'Financing of Churches in Italy', *Law & Justice - The Christian Law Review*, vol. 165 pp 164

<sup>61</sup> Durisotto, D (2010) pp 169

<sup>62</sup> Durisotto, D (2010) pp 169

<sup>63</sup> 'State Aid: Commission finds Italian ICI real estate tax exemptions for non-commercial entities incompatible and clears amended exemptions under new IMU law', *European Commission on Competition*, Press release 19 December 2012

<sup>64</sup> 'State Aid...' Press release *European Commission on Competition*

regime is demonstrable public benefit of activities performed. In this report I sought to establish that the presumption of public benefit that has historically been applied to religious organisations needs to be abolished as inconsistent with modern sensibilities and the duty of government to base policy on reason and evidence. Once the presumption of benefit is abolished, the 'advancement of religion' fails to meet the public benefit test for Charitable status in the case of organisations that do not perform other activities of demonstrable public benefit like provision for the destitute and disadvantaged in the community. As such, it seems pertinent to abolish the head of 'advancement of religion' from charity law to ensure that the tax allocation of charitable exemptions is only applied to organisations that perform socially beneficial purposes. These steps to curb abuses of the Not-For-Profit tax concessions would result in net benefit for Australia in supporting legitimate social service provision by charities, regardless of their affiliation because the activities undertaken, and not the nature of the organisation deserves tax payer support.

The regulatory regime in Australia is functionally similar to those in other common law countries due to shared legal, cultural and social history. However, this cannot be taken as an excuse to avoid reform on such a sensitive issue given that it is widely recognised that the state of charity law across common law jurisdictions is out dated with contemporary societies to which it is applied. Civil law jurisdictions offer a contrast to the common law system of managing the relationship of the state to charitable organisations. Germany in particular presents a closely integrated model in charitable service provision mediated by the state with an additional tax on the religious population collected by the state to fund the operation of religious organisations which is appealing from a 'user pays' rationale. A different form of taxation for religion operates in Italy at several levels of affiliation between the state and various religious groups. Whether such methods are appropriate for Australia would require extensive consultation and financial modelling and such assessment was beyond the scope of this paper.

Ultimately, it is imperative to emphasise that the intention of reform to charitable tax exemptions is not to interrogate the merits of faith or religious belief systems. The free practise of faith and religion is not at issue. The intention of reform is to erase inappropriately deferential treatment towards religion from tax law to ensure that tax concessions for socially beneficial activities are disbursed rationally, where benefit can be established to standards acceptable at law.

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