THE INDUSTRY COMMISSION INQUIRY INTO

CHARITABLE ORGANIZATIONS IN AUSTRALIA:

A LEGAL WALKABOUT

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Presented at

AUSTRALIAN CHARITY AT THE CROSSROADS CONFERENCE

MELBOURNE, AUSTRALIA

November 10-11, 1994

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I N D E X

INTRODUCTION

The convenors of this conference have chosen to call it "Australian Charity at the Cross Roads". They have invited me to come down from Canada and comment on the problems in defining charity. I am immensely grateful that they have asked me merely to talk about the problems in the legal concept of charity rather than asking me to propose any workable solutions. As a lawyer who spends considerable time trying to understand the common law's understanding of charity, I can tell you that if Australia is at the crossroads in defining charity, it is considerably ahead of the rest of the world. Quite frankly, when it comes to defining charity, the common law world has lost its way. This is not a recent phenonemon. The law of charity has lost its moral compass with the evolution of our societies from homogeneous religious societies to modern secular pluralistic societies and has not yet found a legal compass which guides the sector on issues of values in the way which religion did in generations past. If by chance the law of charity is approaching crossroads of any kind, it is entirely by accident and has no idea that its wanderings are about to cease.

This conference was convened to look at the Draft Report of the Industry Commission "Charitable Organizations in Australia, An Inquiry into Community Social Welfare Organizations"[1]. In my opinion Australia would have done a far greater service to not only its own society, but to other countries which are watching the Inquiry, if the contents of the Terms of Reference given to the Industry Commission had been as broad as its title - "Charitable Organizations in Australia". Instead, it was limited to the narrow definition of the sector set out in Paragraph 2.[2] Presumably, this restriction was to maintain a consistency with a definitional problem which is uniquely Australian. Australia has a different definition of charity for purposes of tax exemption for institutions than it does for tax deductibility of donations from donors. I think it is very unsatisfactory to attempt to draw boundaries separating education and religion from social welfare and community benefit charities as Australia does. The Draft Report substantially maintains this distinction but makes the problem much worse from a lawyer's perspective, by trying to redefine this portion of the sector as Community Social Welfare Organizations.

It is very important to recognize and distinguish the problems which arise merely from the unique Australian problem of limiting tax deductibility to "direct"[3] eleemosynary charitable activity and global problems arising from the outdated and restrictive definition of what the law regards as charitable pursuant to Pemsel[4]. It seems to me that extending tax privileges to those who indirectly carry on charitable activity through counseling, education and other preventative measures should be reasonably simple to successfully attain. Instead, the Draft Report introduces a new term "Community Social Welfare Organizations (CSWOs) which does not take into account the legal definition of charity. I remain unclear as to whether the Draft Report intends to fundamentally restrict CSWO's to what the law regards as charitable or to radically broaden the legal concept of charity.

In my opinion the Terms of Reference of the Inquiry are so restrictive as to be fundamentally flawed. The Industry Commission relied on the restrictive Terms of Reference to refuse

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[1] October 1994, Canberra (hereinafter "Draft Report").

[2] Draft Report, supra, Terms of Reference, p. XV.

[3] Tax Determination, TD 93/11 cited in Draft Report at p. 229.

[4] The Commissioners for the Special Purposes of the Income Tax v. Pemsel, [1891] A.C. 531 (H.L.) [hereinafter Pemsel].

submissions from religious and educational charities. Unfortunately, two of its most sweeping Draft Recommendations to apply not only to CSWOs. Draft Recommendation 11.5 says the Commonwealth Government should remove the exemption from the Fringe Benefits Tax for Public Benefit Institutions.[5] Covering all Public Benefit Institutions ("PBI") goes beyond the Terms of Reference. The Draft Report ranges even farther afield in Draft Recommendation 9.2 when it says "[f]undraising legislation should apply equally to all organizations involved in fundraising activities, whether or not they are charities."(emphasis added)[6]

The Draft Report's solution of proposing a new category of social organization is problematic because it defies definition at law. The Draft Report has not addressed the legal problems and I doubt that the Commonwealth Government will want to legislate a new definition of charity which will substantially impact the financial obligations of State governments and the legal standing of institutions as charities in the courts of law.[7] Otherwise, the only way to give effect to any new definition of CSWOs is to create a new classification under Section 78 of the Income Tax Assessment Act 1936 ("ITAA") and implement Draft Recommendation 11.2 which states:

> The Australian Tax Office should introduce a process of review of Community Social Welfare Organizations receiving tax deductibility status and other tax benefits."[8]

This would enable the Australian Tax Office ("ATO") rather than the courts to determine what is a CSWO. It could do so without reference to the law of charity. As the proposed definition of a CSWO clearly includes existing PBIs this would open the door for their re-assessment based on the ATO's criteria rather than continuing the existing system of being given tax benefits as a matter of right once they qualify as PBIs at law. Being an equity lawyer, I have grave concerns about moving decisions relating to the definition of the charitable sector to fiscal authorities.

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[5] Draft Report, supra, Draft Recommendation 11.5 at p. 254.

[6] Draft Report, supra, Draft Recommendation 9.2 at p. 201.

[7] The introduction of CSWOs into law would likely require declaratory legislation such as the Recreational Charities Act, 1958, (6 & 7 Eliz. II, c. 17) which is the the only limited statutory definition given to charity in England's law.

[8] Draft Report, supra, Draft Recommendation 11.2 at p. 233.

LEGAL VERSUS POPULAR MEANING OF CHARITY

The problems in defining charity predate the Industry Commission by centuries. Historically there is a distinction between the average person's understanding of charity and the legal definition. If one goes back to medieval times one finds that charity was a religious concept and not a legal one. Tudor England, as a homogeneous Christian society, had a reasonably uniform common understanding of what charity meant. The legal definition of charity goes back to the Preamble to the Statute of Elizabeth[9] in 1601 which excluded religion and instead focused on social problems, education, employment and building public facilities ("Preamble").[10] These purposes did not reflect the activities and causes which the average responsible person had an innate visceral understanding and recognition of as being charitable. Thus the confusion between what I call "visceral" charity and legal charity has been there since the inception of the legal concept of charity.

Two hundred years passed after the Preamble before the courts attempted to classify the purposes which it regarded as charitable and it simply relied upon the "spirit and intendment of the Preamble". However, in 1805 in the case of Morice v. Bishop of Durham[11] Sir Samuel Romilly put forward the common law's first classification of charitable purposes under four heads:

> "There are four objects, within one of which all charity, to be administered in this Court, must fall: 1st, relief of the indigent; in various ways: money: provisions: education: medical assistance; etc.: 2dly, the advancement of learning: 3dly, the advancement of religion; and, 4thly, which is the most difficult, the advancement of objects of general public utility. A just application of this property within the meaning of this testatrix will not fall within any of these objects: for instance, **assisting individuals, not in a state of indigence, but possessing the comforts of life, is liberality; but not charity in any of those senses**."[12] (emphasis added)

Romilly argued for the return to visceral charity as it would be understood at the beginning of the nineteenth century by insisting that indigence was a prerequisite for charity. The Lord Chancellor agreed by deciding:

> "But the Question is, whether, according to the ordinary sense, not the sense of the Passages and Authors alluded to, treating upon the great and extensive sense of the word `Charity' in the Christian Religion, this Testatrix meant by these words to confine the Defendant to such Acts of Charity or Charitable Purposes as this Court

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[9] An Acte to Redress the Misemployment of Landes, Goodes and Stockes of Money heretofore Given to Charitable Uses, 1601 (43 Eliz. 1), c. 4.

[10] The purposes listed in the Preamble as charitable are:

> "The relief of aged, impotent, and poor people; the maintenance of sick and maimed soldiers and mariners, schools of learning, free schools and scholars of universities; the repair of bridges, havens, causeways, churches, sea banks and highways; the education and preferment of orphans; the relief, stock or maintenance of houses of correction; marriages of poor maids; supportation, aid and help of young tradesmen, handicraftsmen and persons decayed; the relief or redemption of prisoners or captives and the aid or ease of any poor inhabitants concerning payments of fifteens, setting out of soldiers and other taxes." ("Fifteens" is a tax of one fifteenth formerly imposed upon personal property.)

[11] Morice v. The Bishop of Durham (1805), 10 Ves. Jun. 522, 32 E.R. 947 (Ch.) [hereinafter Morice, cited to Ves. Jun.].

[12] Morice, supra, at 532.

would have enforced by Decree..."[13]

Morice v. Bishop of Durham stood as the law until 1891 when the courts in Pemsel liberated the law of charity from the requirement of indigence by relying on the technical legal meaning of charity rather the popular meaning. In Pemsel, Lord Macnaghten said that the law of charity must not be governed by the "popular or vulgar use of the word"[14] but that charity must be interpreted according to its technical meaning "peculiar to the law". The leading case on the law of charity is primarily a discussion on the differences between the popular meaning of the term charity and the technical legal meaning. Lord Macnaghten's famous classification of the four heads of charity in Pemsel was less than one paragraph in an eighteen page judgement. The classification was written in the following context:

> "...How far then, it may be asked, does the popular meaning of the word `charity' correspond with the legal meaning? `Charity' in its legal sense comprises four principal divisions: trusts for the relief of poverty; trusts for the advancement of education; trusts for the advancement of religion; and trusts for other purposes beneficial to the community, not falling under any of the preceding heads. **The trusts last referred to are not the less charitable in the eye of the law, because incidentally they benefit the rich as well as the poor, as indeed, every charity that deserves the name must do either directly or indirectly.**"[15] (emphasis added)

Lord Macnaghten moved the future evolution of the common law of charity to his articulation of the fourth head -- other purposes beneficial to the community. This led to what I refer to as Renaissance Philanthropy[16] or (in the words of Lord Goodman) "those whose objects are of a more hedonistic nature which contribute to the quality of life."[17] Lord Macnaghten was not just reacting to an evolution in society which had moved visceral charity into a more modern legal meaning but was trying to actively move the law forward. Immediately after the sentences quoted above he said:

> "It seems to me that a person of education, at any rate, if he were speaking with reference to endowed charities, would include in the category educational and religious charities, as well as charities for the relief of the poor. Roughly speaking, I think he would exclude the fourth division."[18]

The courts have not attempted another classification since Pemsel and its four heads are the basis of the legal definition of charity. However, determining what any particular society in any particular

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[13] Morice, supra, at 543.

[14] Pemsel, supra, at 582.

[15] Pemsel, supra, at 583.

[16] See the author's article "Religious, reformation, remedial and renaissance philanthropy" in P. 6 & I. Vidal, eds., Delivering Welfare - repositioning non-profit and co-operative action in western European welfare states, (Barcelona: Centre d'Iniciatives de l'Economia Social, 1994), also in (1993/94) 2 The Charity Law and Practice Review 53.

[17] Lord Goodman, National Council of Social Services Committee of Inquiry into the Effect of Charity Law and Practice on Voluntary Organizations (London: Bedford Square Press, 1976) [hereinafter Goodman] at i.

[18] Pemsel, supra, at 583.

age viscerally regards as charitable remains one of the greatest challenges facing the law of charity. As Lord Macnaghten suggested, the level of education of the person considering the question has relevance when considering the question.[19] In today's world you will get very different answers if you move the determination of the issue away from the individual and the courts and give it to the fiscal authorities.

In arguing for a comprehensive view of visceral charity let me not minimize the extent of the problem in coming to an acceptable common understanding of what purposes and activities should be included in the modern world. The law has not only lost its moral compass, it has lost any sense of where its boundaries are or should be. Ever since Pemsel the emphasis has been on the fourth head and the legal definition has been extended without discipline or consistent logic. When legal reasoning failed the courts resorted to "analogy" to the Preamble. In effect, the legal meaning has, as Australians would understand, been on a "walkabout" with no one even looking for a crossroad since Pemsel. There are no boundaries and no particular destination - only occasional annoyances, excesses or "bad hair days" when individual judges get cranky and cry "enough already". This is illustrated in the Australian case of The Royal National Agricultural and Industrial Association v. Chester[20] where a pigeon fancier left a bequest to improve the breeding and racing of Homer Pigeons. If you are on a walkabout, there is nothing more annoying than being passed by a racing pigeon flying straight to the destination inculcated in its homing instinct carrying an important communication. The High Court of Australia recognized that such carrier pigeons had a useful role in times of war as well as peace but could not find any "analogy"[21] to consider breeding them as beneficial to the community for purposes of the law of charity.

AUSTRALIAN ELEEMOSYNARY CHARITY FOR DONORS

While the rest of the common law world has accepted the four heads of charity in Pemsel, Australia rejected Lord Macnaghten's technical legal definition of charity and reverted to its popular meaning. In the High Court of Australia in Chesterman v. FCT Isaacs J. said:

> "...I am very distinctly of opinion that to prevent tautology and to give each word a sensible meaning the word `charitable' in sec. 8(5) of the Estate Duty Assessment Act has not the extensive Elizabethan meaning, but has what may be shortly, though perhaps incompletely, called its eleemosynary meaning...`Charitable' must therefore, in the sub-section referred to, be understood in its `popular' sense...I exclude the idea that is involved in the technical meaning of `charity' that except in trusts directly for the relief of `poverty' the distinction between rich and poor has no relevance."[22]

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[19] Given that the definitions of both a CSWO and eleemosynary charity exclude educational and religious charities, it would be impolite to speculate what Lord Macnaghten might have thought of the educational level of those who exclude education and religion from the sector.

[20] [1974] 48 A.L.J.R. 304.

[21] If, however, you have a purpose close enough to a judge's heart, such as the production of law reports, the court can find it "within the equity and the spirit and intendment of the preamble" "without seeking any analogy in cases which have gone before" (emphasis added) as Barwick C.J. did in the High Court of Australia in Incorporated Council of Law Reporting of the State of Queensland v. Commissioner of Taxation of the Commonwealth of Australia [1971] 125. C.L.R. 659 at p. 669.

[22] [1923] 32 C.L.R. 362 at 384-385 (hereinafter Chesterman (HCA)").

In coming to this decision as to a "sensible meaning" of charity, Australia followed Lord Herschell's minority judgement in Pemsel and re-introduced the indigence requirement which determined Morice v. Bishop of Durham. The High Court of Australia adopted Lord Herschell's minority opinion in Pemsel that:

> "the popular conception of charitable purposes covers the relief of any form of necessity, destitution, or helplessness which excites the compassion or sympathy of men, and so appeals to their benevolence for relief".[23]

The problem Australia had in 1923 was that its legal decisions could be appealed to the Privy Council in London. Consequently, in November 1925 the House of Lords overruled the High Court[24] and re-imposed the technical legal Elizabethan definition of charity used in Pemsel. Isaacs J. was not about to let London have the last word. In February 1926 he had the opportunity to rule on the same issue under a different Australian statute and circumvented the Privy Council decision. He did this in the classic legal way of splitting hairs on technical wording which any reasonable person would know to leave alone. Isaacs J. said that because the Income Tax Assessment Act used the term "public charitable institutions" rather than "charitable purposes" it should be given its popular meaning rather than its legal meaning.[25] It is an amusing irony to an equity lawyer that Lord Macnaghten relied upon the wording in the Income Tax Act of England to introduce the technical legal meaning of charity in Pemsel and Isaacs J. relied upon the technical words in the Income Tax Assessment Act of Australia to re-introduce the popular meaning of charity. Isaacs J. was not impressed that Lord Macnaghten's "person of education" would include educational and religious charities. He was disdainful of "quaint Chancery decisions" which affixed "purposes quite outside what **any ordinary person** would understand by charitable".[26] (emphasis added)

Australia therefore moved away from the rest of the common law world in restricting charity for purposes of tax deductibility to "eleemosynary charity". Eleemosynary charity is a major step forward in the jurisprudence of the legal meaning of charity because it accomplishes the important objective of replacing a term one can not define with a term one can not spell.[27] While Australians having a Fosters may engage in lively debates over the precise meaning of the popular term "eleemosynary", Canadians having a Molsons would be unable to move the debate beyond how to spell it. In Canada the popular meaning of charity is far broader than eleemosynary and I would be surprised if the restricted definition reflects visceral charity in Australia in the 1990's. If I had been an Australian with the knowledge that the Industry Commission had an inquiry into "Charitable Organizations in Australia", I would have ignored the restrictive Terms of Reference and made submissions demanding that the charitable sector be recognized to include far more than eleemosynary community social welfare organizations.

The Australian courts have shown some sensitivity to the subjective and moral definition of charity

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[23] Chesterman (HCA), supra, at p. 384.

[24] Chesterman v. FCT [1926], A.C. 128 (hereinafter "Chesterman (PC)").

[25] Young Men's Christian Association of Melbourne v. FCT [1926], 37 C.L.R. 351 (hereinafter "YMCA Melbourne [1926]").

[26] YMCA Melbourne [1926], supra, at p. 359.

[27] Equity lawyers are very skilled at this as evidenced by their substitution of the term "fiduciary" for "trust".

but would not recognize my concept of visceral charity. Fullagar J. in the High Court of Australia in Salvation Army (Victoria) Property Trust v. Fern Tree Gully Corporation said:

> "There is a subjective element in the term (charitable) as used non-technically, which is absent when it is used technically. The characteristic of a charitable act or purpose in this sense is that it possesses a certain moral quality...On the other hand, when we ask whether the act or purpose is charitable in the technical sense, the test to be applied is wholly objective..."[28]

PEMSEL DEFINITION FOR INSTITUTIONS

Australia does apply the broad legal meaning of charity when determining tax exemptions. The more modern High Court of Australia embraced the Privy Council decision in Chesterman (PC) and applied the Pemsel test to the definition of "charitable institution".[29] In that case an institution which the High Court of Australia had previously denied status of a "public educational institution"[30] was determined to be a "charitable institution" because its educational objects were "clearly beneficial to the whole community"[31] and "of public utility"[32]. Australia therefore applies the technical legal Elizabethan definition of charity when determining questions of law and when determining exemption from tax under various statutes.

The average person wanting to understand the meaning of charity is most inclined to form his view of the law based upon the tax privileges extended to the donor making a charitable donation rather than the tax privileges extended to charitable institutions. Australia applies something approximating the eleemosynary definition of charity when determining tax deductibility for donations. The average person trying to decide whether tax privileges in any way reflect his or her personal notion of visceral charity is going to consider personal tax deductibility rather than institutional exemption from wholesale sales tax, fringe benefits tax, land tax or stamp duties and bank charges.

Apart from the practical fiscal implications to the donor's pocketbook by using a different definition for deductibility, the language used raises potential technical legal problems. Section 78 of the Income Tax Assessment Act 1936 ("ITAA") grants tax deductibility for donations to "Public Benevolent Institutions". The technical legal definition of charity in Pemsel is avoided by using the term "benevolent" instead of charitable. The problem is that the courts have determined that "benevolent" has a wider meaning than legal charity[33] and therefore is not charitable. Further, the High Court of Australia has made it clear that the "expression `public benevolent institution' is not a

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[28] (1952) 85 C.L.R. 159 at p. 184.

[29] Incorporated Council of Law Reporting of the State of Queensland v. Commissioner of Taxation of the Commonwealth of Australia [1971], 125 C.L.R. 659 (hereinafter "ICLR Queensland [1971]").

[30] Incorporated Council of Law Reporting for the State of Queensland v. Federal Commissioner of Taxation [1924], 34 C.L.R. 580.

[31] ICLR Queensland [1971], supra, p. 668 per Barwick C.J.

[32] ICLR Queensland [1971], supra, p. 672 per Windeyer J.

[33] Re Diplock [1941] Ch. 253 (C.A.); on appeal sub. nom. Chichester Diocesan Fund v. Simpson [1944], A.C. 341 (H.L.).

term of art"[34] so it can defy definition. Taylor J. wrote:

> "These decisions clearly show that the expression `public benevolent institution' is not a term of art and that it should be understood in the sense in which it is commonly used...According to this view a benevolent institution is an institution having as its object the relief of `poverty, sickness, destitution or helplessness' or `poverty, distress, suffering or misfortune'. These words of definition are not rigid and inflexible but they do convey the general notion of what constitutes the essential attributes of a benevolent institution."[35]

The result is that Australia now has a clear distinction between the technical legal Elizabethan charity and the popular eleemosynary meaning of charity. The problem is compounded by referring to or incorporating eleemosynary charities under the classification of "public benevolent institutions". As a legal writer I believe that this has dire negative consequences for their future legal rights. As a practising lawyer I have the suspicion that there are only a few ivory-tower equity lawyers who would know or care. If I was an Australian judge, however, I would be extremely concerned about the failure to consider legal principles in the Draft Report.

CSWOs ARE A TAX RATHER THAN A LEGAL CONCEPT

In my opinion the Draft Report has overlooked technical legal issues involved in the meaning of charity. The Draft Report says:

> "The term charitable organization is relevant to tax law but has little applicability outside this area and, as the organizations themselves point out, the term has outdated connotations".[36]

The Draft Report then conjures up out of thin air the term "Community Social Welfare Organization" and then never builds the propoer legal foundation to support it. The focus shifts to tax issues and the Draft Report recognizes that the sector is intensely interested in tax privileges[37]. The Industry Commission responds to this by recommending extending tax privileges to CSWOs stating:

> "The Commonwealth Government should retain the tax deductibility of donations and extend it to donations made to all Community Social Welfare Organizations."[38]

The Draft Report does not say exactly how this should be done but the implication is that CSWOs will be extended PBI status as the submissions and the Draft Report always compare or contrast their tax status to that of PBI's. It is also possible that CSWOs will simply become a new category under section 78. Either method would pose major problems from a jurisprudential perspective as CSWOs represent an incomprehensible blending of Pemsel's first and fourth heads. In my opinion,

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[34] Union Trustee Company of Australia v. FCT [1962], 108 C.L.R. 451 at 455 (hereinafter "Union Trustee").

[35] Union Trustee, supra, at p. 454.

[36] Draft Report, supra, Box 1.1, at p. 2.

[37] Draft Report, supra, Section 2.3.4. at pp. 33-34.

[38] Draft Report, surpa, Draft Recommendation 11.1, p. 239.

even conceding that the term charitable has outdated connotations, it is extremely reckless to jettison the linkage with the historical legal concept of charitable organizations to obtain tax privileges. Considerable effort must be made to secure the legal linkage to the concept of charity by modernizing it rather than by jettisoning it.

The fact is that history demonstrates that the law and courts of equity have consistently nurtured and protected the charitable sector. The Draft Report is prepared to sell the birthright given to the charitable sector by the courts for a mess of pottage offered by the taxman. In my global wanderings I have yet to find a tax legislator who understands the law of equity. It is a fool's bargain to grab for some enhanced tax deduction benefits without first guaranteeing that the sector's legal rights and privileges are protected.

IMPORTANCE OF CSWOs BEING CHARITABLE AT LAW

My prejudices about the extent to which tax issues are trampling legal issues in the evolution of the modern charitable sector are confirmed by the Draft Report's own words that the "term charitable organization is relevant to tax law". The Preamble did not result in a stampede down to Elizabeth I's tax office of organizations seeking a declaration of their tax status. Instead, the result was wealthy citizens going to their lawyers and drafting Wills which left their estates to charitable purposes. In his masterful historical study entitled Philanthropy in England 1480-1660[39] Professor W.K. Jordan examined these testamentary benefactions and said:

> "It is likewise clear that it was the mercantile aristocracy of London which came in the course of our period to exercise a dominant influence on the moulding of national aspirations and on shaping and endowing the institutions required to translate aspirations into enduring reality. These Londoners, who were very rich and almost incredibly generous, spread the pervasive pattern of their giving across the whole face of England. The focus of their attack was on the ancient evil of poverty. But they were prescient enough to sense that poverty could never be destroyed unless the ignorance in which it spawns was relieved. Such men scorned and discarded alms, the mechanism of medieval charity, since they were profoundly persuaded that casual, undisciplined charity was as ineffective as it was wasteful. The great and effective instrument which the mercantile aristocracy, whether of London, Bristol, or Norwich, developed to secure the translation of their aspirations into historical reality was the charitable trust, which was to be classically defined and most powerfully encouraged by the great Elizabethan statute of charitable uses."[40]

The results of the statutory protections and enabling provisions in the Statute of Elizabeth as documented by Jordan were spectacular:

> "...in the span of two generations Protestantism had in fact created in England a new social order and that in terms of effective charitable giving had outstripped by far the whole of the charitable accumulation of the medieval past."[41]

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[39] George Allen & Unwin, London, 1959 (hereafter cited as "Jordan")

[40] Jordan, supra, pp. 18-19.

[41] Jordan, supra, p. 230.

If CSWOs want to encourage people to fund them through large bequests in their wills or receive funds from charitable trusts, it would be fatal to break the legal link with charity even if it has outdated connotations. If Australia wants to enable CSWOs to benefit from the huge testamentary transfer of wealth anticipated in the next two decades it must not ignore charitable trusts as that term is understood by the courts rather than the taxman. The Draft Report makes a tremendously import recommendation in this regard when it says:

> "Assets bequeathed to Community Social Welfare Organizations that enjoy tax deductibility should be free from any capital gains tax liability."[42]

My concern is that ordinary people will write bequests in their Wills leaving property to CSWOs. If the courts do not recognize those organizations as being charitable at law, greedy relatives may succeed in over-turning those bequests and denying the money to the CSWO. A significant portion of the law of charity including cases such as Morice v. Bishop of Durham, Pemsel, Stratton v. Simpson[43], Hardey v. Tory[44] and Sir Moses Montefiore Jewish Home v. Howell[45] are courts deciding whether testamentary bequests are valid charitable gifts.

The world is debating whether the charitable sector should be primarily shaped and regulated by the courts - as modelled by the Charity Commissioners for England and Wales - or the tax authorities - as modeled by the Internal Revenue Service in the U.S. or Revenue Canada. The Industry Commission, without a word of conscious deliberation in 341 pages of its Draft Report and almost as many pages of appendices, has implicitly but unquestionably opted for a future governed by the tax authorities.[46] Worse, it has delegated domestic charity to the Australian Tax Office but assigned overseas charity to the Australian International Development Assistance Bureau.[47] The potential for accelerating this branch of law into becoming entirely dysfunctional is greatly enhanced by having a body whose primary focus is administrative usurp the role of the courts in determining what is meant by charity.

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[42] Draft Report, supra, Draft Recommendation 11.7 at p. 266.

[43] [1970] 125 C.L.R. 138 at p. 158. (hereinafter "Stratton")

[44] [1923] 32 C.L.R. 592.

[45] [1984] 2 NSWLR 406 (NSW Supreme Court Equity Division).

[46] While the Draft Report does not say exactly how tax deductibility status should be extended to CSWOs, it does explicitly recommend that the Australian Tax Office should introduce a process of review of CSWOs receiving tax deductibility status and other tax benefits. (Draft Recommendation 11.2) This clearly moves the review to the ATO and introduces the concept that tax status no longer continues automatically once granted.

[47] Draft Report, supra, Draft Recommendation 6.1, at p. 137.

PROMOTION OF ADVOCACY

The Draft Report promotes the increased use of advocacy by CSWOs to achieve social justice.[48] It acknowledges the potential of tension between the sector and government but ignores the problems imposed for and by the law of charity. The legal proposition that charities are prohibited from having political purposes is rooted in Lord Parker's statement (the "Bowman Principle") in Bowman v. Secular Society Limited[49] in the House of Lords in 1917:

> "A trust for the attainment of political objects has always been held invalid, not because it is illegal, for everyone is at liberty to advocate or promote by any lawful means a change in the law, but because the court has no means of judging whether a proposed change in the law will or will not be for the public benefit, and therefore cannot say that a gift to secure the change is a charitable gift."

The House of Lords went even farther in 1948 when it adopted Lord Simonds' reasoning (the "Anti-Vivisection Principle") that:

> "The law could not stultify itself by holding that it was for the public benefit that the law itself should be changed. Each court in deciding on the validity of a gift must decide on the principle that the law is right as it stands."[50]

The English courts have continued to apply this reasoning as evidenced by McGovern and others v. A.G. in which Slade J. held that the Amnesty International Trust was not charitable saying:

> "From the passages from the speeches of Lord Parker, Lord Wright and Lord Simonds which I have read, I extract the principle that the court will not regard as charitable a trust of which a main object is to procure an alteration of the law of the United Kingdom for one or both of two reasons. First, the court will ordinarily have no sufficient means of judging, as a matter of evidence, whether the proposed change will or will not be for the public benefit. Second, even if the evidence suffices to enable it to form a prima face opinion that a change in the law is desirable, it must still decide the case on the principle that the law is right as it stands, since to do otherwise would be to usurp the function of the legislature."[51]

However much one may disagree with both the reasoning and the result of these decisions on political activities, they are the law in Australia and must not be ignored. Ironically, the law of charity is possibly more liberal than the Draft Report. The law does not allow a charity to have political "purposes"; but does allow a charity to carry on incidental and ancillary political "activities". The Draft Report, however, slams the door much tighter than the existing law in refusing to allow a CSWO to "receive any other money or property" other than gifts for its charitable purposes[52] so it does not allow expenditures for incidental and ancillary non-charitable

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[48] Draft Report, supra, Section 3.5.3. at pp. 65-66.

[49] [1917] A.C. 406 at 442 (H.L.).

[50] National Anti-Vivisection Society v. I.R.C. [1948] A.C. 31 at 50 (H.L.).

[51] [1981] 3 All E.R. 493 at 506 (Ch.D.).

[52] Draft Report, supra, Section 11.5.3. at p. 241 - characteristic (c)(i) & (iv).

activities.

PROBLEMS STEMMING FROM MISCELLANEOUS TERMS

Let me outline some of the legal concerns which I think need to be addressed before the final report. These issues are raised primarily by way of looking for potential problems without alleging that they must necessarily block the implementation of the existing recommendations.

- The Term - COMMUNITY SOCIAL WELFARE ORGANIZATIONS (CSWO)

The Draft Report introduces a brand new term (CSWOs) and must give consideration to how the courts will interpret this term. There is considerable confusion in the Draft Report's understanding of how the existing first and fourth heads of Pemsel are interpreted both in relation to law and tax.

- The Term - "COMMUNITY"

The addition of the term community to social welfare organizations could have unintended negative and restrictive ramifications when subjected to a legal analysis. One of the most problematic issues in the great walkabout on the meaning of charity is determining how broad and unrestricted a section of the public is required for it to qualify as "community". The Industry Commission should not import this debate without giving it careful consideration.

The term community in Lord Macnaghten's fourth head "beneficial to the community" is possibly anti-pluralistic.[53] This has implications for the inclusion of service providers which restrict their services to specific ethnic communities.[54] Careful consideration needs to be given to the definition of "section of the public" adopted in the High Court of Australia in Thompson v. FCT[55] which held that a school for children of the Masonic Order was not a valid charitable purpose.

The legal definition of community is much easier to meet if the CSWOs are going to be considered charities in the relief of poverty. If the broad understanding is that they are eleemosynary is acceptable to the sector, the problem is diminished. CSWOs, however, need to be extremely careful that such important services as teaching English as a second language to immigrants is not excluded by the Draft Report's definition of CSWOs which excludes "organizations that advance education".[56] If such services are included as beneficial to the community rather than relief of poverty, one is then caught by the House of Lords decision as to "community" in Oppenheim v. Tobacco Securities Trust Co. Ltd.[57] which held that an educational trust for a company's employees was not charitable even though there were more than 110,000 employees.

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[53] The House of Lords in Williams' Trustees v. I.R.C., [1947] A.C. 447, held that every object of public utility is not necessarily a charity and ruled that a trust established to promote Welsh language, culture and social intercourse in London did not qualify as meeting the requirement of being beneficial to the community.

[54] Draft Report, supra, Section 2.5.1. at p. 41.

[55] (1959) 102 C.L.R. 315 at 323.

[56] Draft Report, supra, Figure 11.1, at p. 220.

[57] [1951] A.C. 297.

Another problem with the term community is that it might import the requirement that the activity must be local or at least domestic. The Draft Report definition suggests that CSWOs are necessarily domestic. It may be easy to separate domestic and foreign activities from a service provision perspective. If the Industry Commission wants to encourage more financial donations, it is less clear that a donor will always distinguish between the domestic and foreign activities of the Red Cross or Salvation Army.

Australia does import into its law greater domestic restrictions than other countries and I am not supportive of that. After the Chesterman (PC) decision in the Privy Council the Estate Duty Assessment Act[58] was amended[59] to introduce exemption for gifts "to a fund established or maintained for the purpose of providing money for use for such institutions, or for the relief of persons in necessitous circumstances in Australia". If your mind can get beyond trying to figure out how the courts would interpret "necessitous circumstances", you realize that the recipients must be in Australia.

The law is not as restrictive on the domestic issue as the Draft Report or the tax legislation. According to The Law of Trusts in Australia:

> "If the objects of a trust are necessarily valid as a charity in New South Wales, it is immaterial that the capital or income is to be expended wholly outside New South Wales, provided that the objects are also valid where the funds are to be spent."[60]

- Inclusion of - SELF-HELP GROUPS

The Draft Report accepts and commends the inclusion of many self-help groups in CSWOs.[61] One can read the Draft Report and come to the conclusion that it does not intend to change the law of charity but simply fails to recognize that the law of charity excludes the majority of such groups. On the other hand the Draft Report contains statements such as:

> "For example, organizations involved in self-help and mutual support, advocacy, community participation and self-management, and action based research, are not considered `benevolent' under the present definition."[62]

While a tax legislator can extend such groups' tax privileges by a stroke of the pen, it is not enough to simply list them as an example of a CSWO in Figure 11.1. to grant them charitable purpose status at law. The Draft Report's own listed characteristics of a CSWO requires that its public fund "is used only to support the organization's charitable purpose".[63] What the taxman giveth, the law immediately takes away if the necessary work is not done to declare self-help as a charitable purpose.

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[58] 1914-1957 (Cth).

[59] Act No. 47 of 1928, s. 5(b).

[60] Meagher & Gummow, Fifth Edition, Butterworths, 1986 p. 216.

[61] Draft Report, supra, Section 3.1.1. at pp. 50-51.

[62] Draft Report, supra, at p. 215.

[63] Draft Report, supra, Section 11.5.3. at p. 241.

The Term - BENEVOLENT

The Draft Report wants CSWOs to receive all of the tax deductibility privileges extended to Public Benevolent Institutions ("PBI") pursuant to section 78 of the ITAA.[64] It cites Tax Determination 93/11[65] as an example of the ATO's distinction between "benevolent" and "charitable". Demonstrating a level of terminological dyslexia which only a taxman can hope to attain, black becomes white and white becomes black. How is a layperson to remember that the ATO wants a CSWO to be benevolent whereas the courts will deny tax exemptions to an organization which "is not a charitable organization but merely a benevolent body"[66]?

The Term - INSTITUTIONS

It is not clear what the word "institutions" means in the term PBI.[67] Isaacs J. thought "institutions" was important enough to distinguish the decision of the Privy Council in Chesterman (PC) when he decided YWCA Melbourne [1926][68] in the High Court of Australia. Gibbs J. (also in the High Court) said an institution "would not ordinarily connote a mere trust".[69] By the end of the same judgement, however, he cites Hardey v. Tory[70] as authority for the proposition that "a gift for charitable institutions is prima facie a gift for charitable purposes".[71] Also in the same judgement he cites the leading English case[72] which says "benevolent" is not charitable in deciding that "unless the purposes to which the income (of a trust) must be applied are exclusively charitable the trust fails because it `tends to a perpetuity'".[73] The concept of "exclusively"[74] charitable is very problematic to many of the concepts imported into the Draft Report.

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[64] Draft Report, supra, Draft Recommendation 11.1 at p. 239.

[65] Draft Report, supra, Section 11.5.3. at p. 237.

[66] City of South Melbourne v. YMCA of Melbourne, [1960] V.R. 709 at p. 710.

[67] For a discussion of the meaning of institution under state statutes see Priestley J.A.'s judgement in Glebe Administration Board v. Commissioner of Pay-roll Tax (N.S.W.) [1987], 87 ATC 4,825.

[68] YMCA Melbourne [1926], supra, at p. 358.

[69] Stratton, supra, at p. 158.

[70] [1923] 32 C.L.R. 592.

[71] Stratton, supra, at p. 163.

[72] Re Diplock [1941] Ch. 253 (C.A.); on appeal sub. nom. Chichester Diocesan Fund v. Simpson [1944], A.C. 341 (H.L.).

[73] Stratton, supra, at p. 157.

[74] In British Launderers' Research Association v. Borough of Hendon Rating Authority [1949] 1 K.B. 462 (C.A.) at pp. 467-8 Denning L.J. wrote:

> "There is one thing which is clear both on the wording of the statute and the cases. The word "exclusively" must be given its full effect. It is not sufficient that the society should be instituted "mainly" or "primarily" or "chiefly" for the purposes of science, literature or the fine arts. It must be instituted "exclusively" for those purposes. The only qualification -- which, indeed, is not really a qualification at all -- is that other purposes which are merely incidental to the purposes of science and literature or the fine arts, that is, merely a means to the fulfilment of those purposes, do not deprive a society of the exemption. Once however, the other purposes cease to be merely incidental but become

PROBLEMS RESULTING FROM TRUSTS NOT BEING EXCLUSIVELY CHARITABLE

The consequence of a trust failing for having purposes which are not exclusively charitable is that it is deemed never to have existed and the property reverts to the donor. There are a few instances (which are considered anomalies) when the courts have upheld a non-charitable purpose trust. The implications of benevolent and non-charitable purposes for the sector must not be ignored if the Industry Commission wants to encourage charitable gifting. The Australian courts have said "...The charitable nature of the gift derives from the fact that the purposes and objects of the institution are themselves charitable..."[75] If one works backwards through these legal propositions one would want to be very careful in determining it is prudent for CSWOs to move away from having purposes which the law regards as charitable.

The common law concept of a trust requires beneficiaries to be human beings or corporations who can and will ensure that the trustee properly discharges his duties as the courts will not take the initiative to enforce a trust.[76] If there are no persons to enforce the trust, it is void. The only exception is for purpose trusts which have exclusively charitable purposes.[77] Charitable purpose trusts are valid because the Crown (as parens patriae) on behalf of the public is prepared to enforce such a trust. The court, however, will only enforce purposes which are exclusively charitable. In Morice v. Bishop of Durham the Lord Chancellor would only consider a bequest to be charitable if "this Testatrix meant by these words to confine the Defendant to such Acts of Charity or Charitable Purposes as this Court would have enforced by Decree..."[78]. If the court would not enforce a trust, it must fail as being too indefinite or uncertain. This enforceability principle was reinforced by the Privy Council decision in Leahy v. A.G. N.S.W..[79]

The enforceability principle is a very important safeguard in the common law to protect the rights and interests of charitable trusts. This could be lost if the CSWOs are not considered to be charitable. Further, the courts would almost certainly lose their ability to exercise their cy pres function to modernize and amend charitable trusts.

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collateral; that is, become additional purposes of the society; then, whether they be main or subsidiary, whether they exist jointly with or separately from the purposes of science, literature or the fine arts, the society cannot claim the exemption."

[75] Re Godfree (deceased) [1952] VLR 353 at p. 356.

[76] D.W.M. Waters, The Law of Trusts in Canada, 2d ed. (Toronto: Carswell, 1984), p.503.

[77] In the Re Denley's [1969] 1Ch 373, [1968] 3 All ER 65 the rule was relaxed slightly to validate a non-charitable purpose trust where there were individuals with sufficiently direct interest in the trust that they had standing before the courts to enforce it.

[78] Morice, supra, at 543.

[79] [1959] A.C. 457, at p. 484; [1959] 2 All E.R. 300 (P.C.).

DRAFT REPORT'S CHARACTERISTICS OF A CSWO

It is ironic that the Draft Report introduces the concept of the CSWO in an attempt to move beyond the narrow outdated definition of charity which precludes self-help and advocacy and then proceeds to contradict all of that liberality in its characteristics of a CSWO. The very first characteristic is that its principal purpose is charitable.[80] This would broaden the current Australian definition by allowing indirect[81] charitable relief but would not embrace purposes which the law did not recognize as charitable. It would explicitly eliminate PBI's such as Amnesty International which are "listed"[82] in Section 78 of the ITAA but are considered not to be charitable by the courts (McGovern and others v. A.G.). This contradiction is not reflected in Figure 11.1.[83]

The second characteristic is that a CSWO does not pay any of its profits or give any of its property to its shareholders, controllers or members. This is a traditional restriction placed on charities. As the Draft Report explicitly states that some CSWOs are "co-operatives"[84], it seems to have ignored this characteristic. Also, the Draft Report opens the chute down a slippery slope with Draft Recommendation 6.2 for international social welfare providers by stating that the Australian International Development Assistance Bureau "should ensure that for-profit firms are not excluded".[85]

The greatest restrictions come from the third characteristic that a CSWO must have a "public fund" with five limitations. All gifts, interest and revenue must be given to this public fund and a CSWO must not receive any other money or property. This money can be "used only to support the organization's charitable purpose". Therefore, it can not use funds for self-help, advocacy or any other purpose which the law does not recognize as being charitable.

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[80] Draft Report, supra, at p. 241.

[81] This would accomplish the Draft Report's objective of extending benefits to indirect assistance such as counselling and preventative programs.

[82] The Australian practice of allowing a named organization to become a PBI by virtue of negotiating with the ATO its inclusion on a "list" rather than meeting categories or qualifications recognized by law is already a significant step away from having "charitable" status determined by fiscal rather than legal criteria.

[83] Draft Report, supra, at p. 220.

[84] Draft Report, supra, at p. 9.

[85] Draft Report, supra, at p. 140.

CONCLUSION

The Draft Report makes some useful recommendations from the point of view of the sector and its concerns. It fails, however, to give due consideration to the legal issues involved and could create considerable problems if these are not addressed before the final report. The legal problems in defining a CSWO so as to broaden its application for tax purposes while retaining the necessary characteristics to remain charitable at law are formidable. In my opinion the charitable sector would be better to devote its energies to achieving a modern comprehensive definition of charitable organizations which is broader than eleemosynary charity and includes Pemsel's education and religion heads. The Industry Commission's concept of a CSWO would then be unnecessary. The process of the Inquiry has been positive and brought many diverse elements of the charitable sector together. The Draft Report makes many useful and progressive recommendations based on its significant interaction with the sector and solid economic analysis. I, however, have been asked to analyze the "technical legal" aspects of the Draft Report rather than "popular" provisions. The momentum of the Inquiry should be built upon to achieve a genuine breakthrough in modernizing the law of charity rather than simply accepting the poorly constructed concept of a Community Social Welfare Organization.