

Private Funds (PPFs)

The New Rules

Vera Visevic from Makinson & d'Apice explains the new rulings in regard to Prescribed Private Funds (PPFs) and discusses how this will impact on fundraising for charities.



As at October 24, 2008 there were 769 Prescribed Private Funds¹ (PPFs) approved by the Federal Government. These PPFs have a corpus of some \$1.3 billion and have made grants of approximately \$301 million to deductible gift recipients (DGRs) across a variety of categories. Over \$120 million was distributed from PPFs to the community in the 2006/07 financial year alone. In other words, PPFs are a significant source of donations for DGRs and should be the subject of special focus by DGRs from a fundraising perspective.

Most people working in the not-for-profit sector would have heard in recent times about the proposed changes to the legislation surrounding PPFs. The changes have been the subject of discussion and consultation for some months, stemming back to late last year. The Federal Government has now made available the draft new legislation for comment. This article will discuss the more salient proposed changes and how they will impact on fundraising for charities.

Definition

1. A PPF is a private charitable fund established by a trust deed to which businesses, families and individuals can make tax-deductible donations. Under the recent proposed changes to the law, these funds will now be referred to as

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Private Ancillary Funds (PAFs).¹

2. The *Tax Laws Amendment (Measures No 4) Bill 2009* (Bill) brings the full administration of the PPF regime under the authority of the Commissioner of Taxation (i.e. ATO). Treasury has also released draft New Guidelines to apply to PPFs. The Bill and New Guidelines (when in final form) will take effect from 1 October 2009.

Requirements that currently apply to PPFs

3. The following are the main requirements:

i. the PPF must be established under a will or instrument of trust, solely for the purpose of providing money, property or benefits to deductible gift recipients (DGRs) or towards establishing DGRs;

ii. the PPF must meet the public fund requirements (without the need to invite donations from the public or the requirement for certain public participation in its administration); and

iii. Currently, the PPF must meet the requirements of the integrity assurance measures mentioned in the guidelines.

iv. As from 1 October 2009, in order for a trust fund to become a PPF and endorsed as a DGR, the trustee will need to agree to be bound by the New Guidelines (in a form approved by the Commissioner).

The New Requirements that will apply to PPFs

Corporate Trustee

4. A significant change that the Bill introduces is the requirement that the trustee of a PPF must be a corporate

trustee (a PPF may have multiple corporate trustees). Currently, trustees of PPFs can be either individuals or corporations.

5. This new requirement ensures that directors meet a minimum standard of behaviour as the *Corporations Act 2001* (Cth) sets out circumstances under which an individual will be automatically disqualified from managing corporations.

6. From a charity's perspective, this should give it more confidence that PPFs are being operated and managed legally and in a manner which ensures that the sole purpose of the PPF is being accomplished, that is, supporting charities which are DGRs.

Penalties

7. Another significant change that the Bill introduces is that it gives the Commissioner the power to impose administrative penalties on trustees that fail to comply with the New Guidelines, as well as the power to remove trustees of non-complying funds (for matters of serious non compliance). This can be contrasted with the current guidelines which provide an 'all or nothing' penalty system.

Liability

8. The Bill sets out that the trustee and the directors are jointly and severally liable for any administrative penalty, and the penalty must not be reimbursed by the PPF. The rationale behind this is that corporate trustees of PPFs generally have very little capital and this liability on directors will ensure that PPFs comply with the New Guidelines.

Indemnity

9. The New Guidelines further set out that the governing rules of a

PPF must not indemnify the trustee (or any employee, officer or agent of the trustee) for a loss or liability attributable to dishonesty or negligence of the trustee, employee, officer or agent, or a deliberate act known to be a breach of trust.

Process for establishing a PPF

10. Currently, a person wishing to set up a PPF must first apply to the ATO. PPFs then go through a number of processes before they are submitted to the Minister. The ATO then forwards valid applications to the Government for consideration. The ATO cannot guarantee that a PPF application will be endorsed, as it is ultimately a decision for the Minister.

11. As at 1 October 2009, the Commissioner will be responsible for determining whether a trust fund is a PPF, and if that fund is entitled to be endorsed as a DGR. The Commissioner's decision is reviewable by the Administrative Appeals Tribunal and by the Courts.

12. Many charities recommend to their regular 'bigger' donors to consider establishing a PPF. This new process will make it easier for a PPF to be established and endorsed by such a donor.

Other requirements

13. Under the current regime, whilst a PPF may solicit and receive gifts from the public, gifts from the public cannot be the primary source of gifts to it. However, the New Guidelines prescribe that a PPF must not solicit donations from the public and in any financial year, the PPF must not accept donations totalling more than 10% (in total) of the market value of its assets from entities (other than a founder of

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the PPF, associates of the founder or employees of the founder).

Purpose of a PPF

14. The sole purpose of the PPF must be to provide money, property or benefits to funds, authorities or institutions, gifts to which are DGRs (e.g. public benevolent institutions, health promotion charities, overseas aid funds). A PPF cannot have other purposes.

15. A PPF cannot make a donation/grant to ancillary funds (which is a common structure for community foundations), other PPFs, political parties and Artbank.

Investments by PPFs

16. The New Guidelines set out that a PPF must prepare and maintain a current investment strategy for the fund. The strategy should have regard to risk, composition and liquidity of the PPF's investments. The trustee must then implement the strategy and ensure that all investments are made in accordance with it.

Minimum Distributions to DGRs

17. The guidelines issued by the ATO for PPFs outline the Government policy with regard to accumulation of gifts by PPFs. There are currently complex rules governing accumulation targets for PPFs. The New Guidelines replace these rules with a simpler minimum annual distribution rate for funds.

18. The New Guidelines set out that during each financial year a PPF must distribute at least 5% of the market value of the PPF's assets (as at the end of the previous financial year). The PPF must distribute at least \$11,000 (or the remainder of the PPF fund if that is worth less than

\$11,000) during that financial year if the 5% is less than \$11,000 and the expenses of the PPF for that financial year are paid from the PPF's assets or income. No distribution is required during the financial year during which the PPF is established.

19. From a DGR's perspective, which is attempting to obtain donations from PPFs, this is an important fact to understand. DGRs may face reluctance from PPFs to make donations once a PPF has reached its minimum threshold of 5%, especially during a 'tough' year.

Distribution Strategy

20. The New Guidelines set out that a trustee must prepare and maintain a current distribution strategy for the PPF. The strategy must set out the anticipated quantity of donations to be received, expected recipients of the distributions of those donations and size of the distribution the PPF estimates that it will make.

21. This new requirement has two consequences for DGRs which are hoping to elicit donations from PPFs:

22. (a) A trustee of a PPF has to plan in advance (one expects at least annually) as to which DGRs it is going to support and to what monetary extent. This may make it more difficult for DGRs approaching PPFs to elicit donations out of them, which do not conform to the distribution strategy once that strategy has been adopted by the trustee.


23. (b) It would be easier for DGRs if they could obtain copies of these distribution strategies so as to know which PPFs to target for donations. However, there is no indication at this

stage that these distribution strategies will be publicly available.

How do we find these PPFs?

24. Here is the challenge! There was a suggestion earlier in the consultations concerning PPFs that their contact details should be made publicly available to make it easier for charities to approach them with a view to soliciting donations from them. Many PPFs which made a submission to the Federal Government rejected this suggestion; their argument being that as they are in fact 'Private' Prescribed Funds, they should not be required to reveal their contact details. As a consequence, this suggestion was kiboshed.

25. One benefit however from the new laws concerning PPFs is the requirement that they have a corporate trustee. The effect of this is that charities will be able to carry out a company search of the trustee company and, in so doing, obtain the address of the registered office of the trustee company. Approaches can then be made to the trustee company for donations.

The more a charity understands about the mechanics of operating a PPF, the easier it will be for a charity to target PPFs for donations. PPFs are, and should continue to be, a significant source of funds for charities, which are endorsed as DGRs. Each DGR should have some strategy in place about soliciting donations from PPFs, as the sole purpose for PPFs existing is to funnel funds through to DGRs. PPFs are therefore well worth considering as a source of donations. 

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In this article, we will continue to refer to these funds as PPFs, for the sake of consistency.