



Charities Bill introduces new compliance regime

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The Select Committee is due to report back to Parliament by the end of September, with the view to having the Bill enacted before the end of the year. Initially only the parts of the Bill related to the establishment of the Commission will take effect, with other parts to take effect at a later date in one or more stages. The reason for this 'staggered start' is that it gives the fledgling Commission time to develop the necessary systems to operate effectively.

This newsletter outlines key issues based on the current form of the Bill. Submissions close on 3 June 2004. If you intend to make a submission and need further information and advice, please contact us – details are listed at the end of this newsletter.

The Charities Bill: headlines and impact

- Retains the current definition of charity.
- Establishes a Charities Commission to oversee charitable entities.
- Denies any tax relief unless charities are registered with the Commission.
- Makes information on all registered charitable entities accessible to the public.
- Requires every charitable entity to complete an annual return.
- Retains the link to the Income Tax Act to determine tax exempt and donee status.

- Gives the Commission the power to investigate and/or de-register a charitable entity.
- Gives the District Court jurisdiction to hear appeals against Commission decisions.

What is a "charity"?

Although the Bill contains a new definition of "charitable purpose", it does not alter the current understanding of what is a charitable purpose, which incorporates the traditional four heads of charity:

- The relief of poverty;
- The advancement of education;
- The advancement of religion; and
- Other purposes beneficial to society.

The Bill also restates the concessions enacted in 2003 that broadened the traditional public benefit test to include descendants from a common ancestor.

It is likely that any entity that currently satisfies the charity requirements will continue to do so under the Bill.

Entity

The Bill defines "entity" as "any society, institution, or trustees of a trust", covering all of the standard means of forming a charitable entity, particularly those of incorporated societies and charitable trusts.

Charitable entities and approved donees

The Bill continues current practice in distinguishing between entities that apply to be exempt from income tax



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– charitable entities – and those that only seek to be approved as donees so that donors can receive a rebate for tax purposes.

The vast majority of entities apply to be granted both charitable entity and approved donee status.

It is worth noting that donee organisations will be subject to almost identical regulations as charitable entities.

New requirements to register

Entities must comply with prescribed criteria in order to register as a charitable entity.

The entity must be established for charitable purposes, it must have an appropriate name and all officers of the entity must be “qualified” in accordance with the Bill. A “qualified” officer is defined as a person not disqualified for various reasons listed in the Bill.

Trustees of a trust must be treated as complying with these requirements if they have a binding ruling from Inland Revenue under section CB 4(1)(c) or (e) of the Income Tax Act 1994 (as opposed to the informal letter of compliance that most charitable entities receive from Inland Revenue at present) or if the income derived by the trustees is for charitable purposes under section 24B of the Maori Trust Boards Act 1955.

Registration compulsory to claim tax relief

An explanatory note to the Bill says that: “Registration with the Commission will be voluntary and will not alter a charity’s legal status.” However, unless an entity

is registered with the Commission no tax relief will be available.

The Bill does not exempt entities that have tax exempt status under the current regime. Therefore, if an existing charitable entity fails to register with the Commission, it will lose its tax exempt status.

Commentary to the Bill notes that entities with current charitable approval from Inland Revenue will be thoroughly reviewed before being approved by the Commission.

In practice, the Commission may accept all existing charities for registration and then review the position when annual returns are filed (see the ‘Must Report Annually’ section below).

New Charities Commission

The proposed Charities Commission is designed to provide an administrative centre for the activities of charities.

Its role and function will be similar to those of the Registrar of Companies and the Companies Office in relation to companies.

Powers of the Commission

The Commission has powers to investigate charitable entities, gather information and, ultimately, remove an entity from the register.

Inquiries

The Commission’s powers allow it to investigate the activities of a charitable entity. It will also be able to investigate matters of management, results and outcomes, and the “value, condition,

management, and application of the property and income belonging to the charitable entity”.

This clearly envisages some type of broad audit power, allowing the Commission to investigate an entity’s distributions or expenditures.

Warning notices

The Commission can issue a warning notice saying why it believes the entity is failing to meet its obligations as a charity and what actions it is expected to take to rectify the situation.

If the entity does not take corrective action, the Commission can publish the warning notice (with such a publication generally being immune from defamation actions).

Removal from the register

The Commission can remove a charitable entity from the register where:

- The entity is no longer qualified for registration;
- There has been significant or persistent failure by the entity to meet its obligations under the Act;
- There has been significant or persistent failure by any one or more of the officers of the entity to meet their obligations under the Act;
- A person has been engaged in a “serious wrongdoing” in connection with the entity; or
- The entity itself has requested that it be removed.

Deregistration can be backdated in certain circumstances, including when an entity “is affected by a tax avoidance arrangement”.

This could include entities that innocently invest in a seemingly legitimate scheme that itself invests in a broader tax avoidance arrangement.

Appeals against Commission decisions

An entity may appeal to the District Court against the Commission’s decision to decline registration or to remove it from the register. Currently all court proceedings relating to charitable entities are matters for the High Court.

Information now public

The Commission will be required to put registered entities on a public register of charitable entities and allocate identification numbers. This seems similar to the database of information currently compiled by the Companies Office.

Members of the public will be able to search charitable entities by name, registration number, the name of an officer or other prescribed criteria. A website or other electronic solution therefore seems the most likely option.

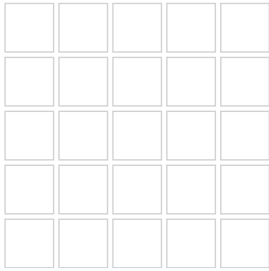
Must report annually

Charitable entities will be required to complete annual returns within four months of their balance date. These will need to be signed by two or more officers.

The structure and content of annual returns will be prescribed by the Governor General at a later date.

The Commission will use an annual return to consider whether the charitable entity continues to qualify for registration, so it is likely that some sort of financial information will be required.

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Must continue to meet tax requirements

Charitable entities will need to ensure that they continue to satisfy all the requirements under section CB 4(1) of the Income Tax Act – and only if these are met will they continue to qualify for tax exempt status.

So, while non-registration means no tax exemption or donee status, registration does not guarantee tax exemption or donee status.

Conclusion

The Bill imposes extra administrative costs on any charitable entity.

However, provided the entity complies with the registration requirements and keeps accurate financial information and

records, it is unlikely that these costs will be substantially different.

A key issue for some charitable entities will be the public availability of information.

Charitable entities will not be able to guard founding documents or the names and details of officers.

Advice and information

Please contact our tax team if you wish to make a submission on the Bill, or would like further advice on the potential impact of the Bill.

For further information, please contact your usual Bell Gully adviser or:

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