The Industry Commission inquiry into charitable organisations

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ABSTRACT

The Industry Commission has carried out Australia's largest inquiry into charities. It was, from the point of view of charities, an unsatisfactory operation, all the more so since it was not clear why the task had been given to the commission. This article examines the commission's work in three ways: the overall relationship between government and charities; the commission's proposed major reforms; and the minor reforms.

Introduction

The Industry Commission has conducted Australia's largest inquiry into charitable organisations. The inquiry has been one of the commission's most ambitious tasks. Given the size of the country's charitable sector, the commission examined what it called 'community social welfare organisations'.

The inquiry did not therefore explicitly deal with health. However, the report has several implications for charities throughout Australia, including those involved in health. This article begins with two general comments on the nature of the inquiry. It then analyses the commission's work at three levels: the relationship between the government and charities; the commission's proposed macro reforms; and the commission's proposed micro reforms.

The Industry Commission published a draft report in October 1994 for public comment. The final report was presented to the government in 1995. The government is currently examining what recommendations it will accept and how they are to be implemented.

The Industry Commission

The Industry Commission is the major independent review and advisory body on industry policy for the Australian Government. It was established in its current form in 1990. Its predecessors were the Tariff Board and the Industries Assistance Commission. The commission's roots are therefore in a body that was designed to protect Australian industry from foreign competition by the imposition of tariffs.

The commission's philosophy changed in the 1970s and 1980s; instead of deciding on tariff levels it recommended how tariffs ought to be removed. It became – like other parts of the government – more concerned with opening up Australian industry to the so-called 'level playing field' of international competition. To use contemporary jargon, the commission consists of 'rational economists' who place a high regard on the market, deregulation, a minimal government role in the economy, and the value of transparency and competition as aids to efficiency.

Charities were worried about the news that in December 1993 the Assistant Treasurer (Hon. George Gear MHR) had asked the commission to examine charities. First, charities do not see themselves as an 'industry'; they operate on a not-for-profit basis and so have a different motivation from that of the usual industries examined by the commission. For example, volunteers play a very important role within all charities and volunteers cannot be easily accommodated within the commission's economic paradigm, which is based on market principles of supply and demand; volunteers give their labour to a charity (rather than sell it).

Second, charities operate on the basis of need and not 'effective demand'. In other words, they go where people want help – they do not operate on the ability of people to pay. If anything, charities specialise in market failure – the people who have lost out in all the economic gain from which other parts of society have benefited. Charities operate on the basis on responsibility to one's neighbour – not the purchasing power of the neighbour.

Third, charities try to be good stewards of their money but they were never created to be profit-making businesses. They often sprawl across several sectors. The bottom line is to help a client – rather than produce a profit. Therefore, a charity like the NSW Spastic Centre, for example, has operations which include hotel services, therapy services, a bus line, and an achievement award for young women. All of these services are required to help the clients, but they are such a diverse collection that no

entrepreneur would combine them in the interests of making a profit. Consequently, the commission's usual method of economic analysis would not be applicable to charities.

Finally, many charities perceived the Industry Commission as one of the government bodies responsible for their increased workload during the 1980s and 1990s. The commission conducted various inquiries aimed at making Australian industries more efficient, usually by the shedding of labour. The increase in unemployment and family breakdown contributed to the extra workload of the charities.

The 1994 draft report had a number of recommendations which reinforced the fears of charities. After considerable consultation, the Industry Commission toned down its 1995 final report, which was not quite as bad as was feared in 1993. Being involved in the process was time-consuming and expensive for charities. But at least the final report was milder than the 1994 draft report and so the potential damage to charities was minimised.

The scope of the inquiry

The commission's terms of reference were either too narrow or too broad. On the one hand, the commission was not asked to examine all the charities in Australia. There is no accurate figure of the size of Australia's charitable sector. One of the results of the commission's work will be the increased involvement by the Australian Bureau of Statistics (ABS) in assessing the sector's size.

The commission's terms of reference dealt with what it called 'community social welfare organisations'. The commission's terms of reference focused the inquiry on 'services' under the headings of 'welfare', 'community', 'accommodation', 'nursing or convalescent homes', 'employment and training for unemployed persons and those with disabilities', 'advocacy, referral, counselling and legal', 'and emergency and development assistance overseas'.

Even so, according to the commission, there are at least 11 000 charitable social welfare organisations in Australia, with a combined total annual expenditure in 1992–93 of over $4.4 billion (of which government contributed more than $2.5 billion). Additionally, some of the organisations, such as Sydney's Wesley Mission, conduct many of the above services and are also active in the health field (for example, running hospitals). Thus the

focus on 'social welfare' was somewhat arbitrary. (Incidentally, there was dissatisfaction among some of the charities with the term 'community social welfare organisations' but there was no agreement on what would be a good alternative term.)

The commission's terms of reference were therefore narrow in the sense that many charities had only part of their work included and many others were not included at all (for example, health, education, sport and leisure).

On the other hand, the terms of reference may have been too broad in that what was lumped together for the inquiry's purpose was an odd assortment of functions, such as aged care (which was the largest single component of the inquiry) and foreign aid. There is little in common between running a retirement village at Darling Point or Toorak and a refugee camp in Rwanda or Pakistan.

The problem over the terms of reference was manifested in some of the commission's recommendations. For example, the commission recommended that government funding should be 'multi-year, typically three year'. This would make sense in a sector where there was a need for rapid review, such as employment training. But it makes little sense in nursing homes, where buildings are to meet certain specifications and cannot be bought and sold as easily as, say, factory warehouses, and whose clientele would not like the risk of being moved on after three years if a government contract is not renewed.

The relationship between government and charities

One level of analysis of the Industry Commission's work is the entire relationship between government and charities, especially those concerned with health, social welfare and community services.

The idea that a national government should have responsibility for health, community and social welfare services is comparatively recent. For well over a thousand years in western Europe, churches provided these services. Churches are the oldest charities in the western world (Suter 1995, pp 97–107).

The early churches were on the margin of the Roman Empire but they still had a community role. Under Roman law a person had no rights until they became an adult, and so they could be treated as well or as badly as parents felt like. Unwanted babies were thrown away in the garbage.

Christians used to rescue the babies and so they ran the world's first orphanages.

Emperor Constantine in the early fourth century was converted to Christianity and he gave a special role to the churches. Churches ran many of the Roman Empire's economic and social activities for approximately the next 1300 years. They formed the world's first transnational corporation, with a common language (Latin); with skilled staff (in an era when to be able to read and write was seen as a gift from God) which ran the economy on the basis of the common good (such as banning the charging of interest for loans – usury); with industrial relations policies (such as no trading on a Sunday); with premises that were the centre of the community and economic life of a town (church buildings were multi-use properties); and monasteries, built on major trading routes, which provided travellers with shelter so that they did not have to spend the night in the forests (the world's first hotel chain).

The rise of the modern nation-state system in 1648 (with the Treaty of Westphalia at the end of the Thirty Years War) meant that national governments became more important. The churches were beginning to be marginalised.

This process of marginalisation has continued to this day. Politicians, for example, will tolerate having church officials comment on personal morality issues (such as gambling, alcohol and sex) but they do not like comments being made on the bigger economic and social issues. This viewpoint ignores the role that the churches traditionally had in social advocacy and public policy.

There is now the risk that the process of marginalisation will be taken a step further in that government will see charities as an arm of government. In other words, government will see the charity sector as a cheaper, more efficient and (in some cases) less unionised sector than government services. Thus government will steer and not row (and so provide money to those that will row).

Returning to the Industry Commission's work, a theme in the continuing debate over the final report's implementation is the extent to which the increased regulation of charities will be done in the higher political interests of making them just an arm of government.

This development carries three risks. First, governments may be reluctant to provide funds to charities that criticise them.

Second, charities themselves may develop a policy of self-censorship.

If a charity were, for example, receiving funding from a department and yet developed doubts about some other aspects of that department's policy, it may be reluctant to criticise the department for fear of losing its funding on the next round of allocations.

Third, many of the services now being funded (often inadequately) by government were commenced by charities. They decided that this was important work that had to be done; as government was not doing it, charities took on the task. Charities are innovative. There is the risk that a tighter control over charity finances would restrict the ability of charities to be innovative.

Macro reforms

The second level of analysis is an examination of the major recommendations made by the Industry Commission.

Input taxes

Charities benefit from exemptions from certain rates and taxes. This privilege is of an historical nature, with the principle based in the era when charities were the main providers of welfare, and so the exemptions helped them to do their work. These exemptions occur in all three tiers of government: federal (sales tax), state (stamp duty, payroll tax) and local government (rates and taxes).

The commission called these exemptions 'input taxes'. The Industry Commission's philosophy is based partly on 'user pays'. The principle is that individuals and organisations need to have a clear idea of what each item or service costs. This is one manifestation of 'transparency'.

The Industry Commission recognised that charities provide a useful service and so it did not want to erode that service. On the other hand, it wanted all aspects to be out in the open.

In the commission's draft report it recommended that all input taxes be clearly identified (at present it is not possible to work out, for example, just how much the exemption from government rates and taxes represents in cash terms to charities – or as revenue foregone by the three tiers of government). The commission argued that the best way to identify the cost of exemptions would be to scrap the exemptions, with the charities keeping receipts of the taxes paid, and then claiming the money back from a government body (which the commission did not identify).

This recommendation attracted considerable criticism from the charities. Tax concessions enable charities to do unprofitable work – not to do their work unprofitably. The recommendation would have required the appointment of extra staff to handle all the paperwork and the commission did not explain in detail how the system could be made to work. Also, the present system works well because it requires the three tiers of government to do nothing. This recommendation was not included in the final report.

Fringe benefits tax exemption

Another aspect of transparency is the recommendation (which appeared in both the draft and the final reports) for charities to lose their fringe benefits tax exemption.

When the fringe benefits tax was introduced, one unintended consequence was that it also applied to the staff of charities, for example, the bedroom accommodation provided to staff who have to 'sleep over' while on a night shift at a residential institution or the cars used by domiciliary care nursing staff to visit patients.

Government agreed that it was not the intention to penalise these people and so charities were exempted from paying fringe benefits tax. The Industry Commission did not like this exemption. Partly it was concerned with the lack of transparency. It also argued that some charities were abusing the exemption by using fringe benefits tax 'packaging' as a way of recruiting staff: non-award people could take a large slice of their salary as part of the tax-exempt income. The commission did not, incidentally, provide specific evidence of this alleged abuse.

The commission's draft recommendation was criticised by charities, but it did not back down and repeated the recommendation in the final report. The Federal Government, in its initial response to the final report, rejected that recommendation, as has the Opposition.

Incorporation of religious bodies

A persistent problem for the commission's work was trying to categorise the various organisations to be included in the survey. The commission created a new term: 'community social welfare organisation'. But there were problems in applying the term by virtue of the differing legal status of 'charitable' organisations. In its draft report the commission admitted that

it did not know how to create a neat system of categories. Charities tended to respond with the advice: 'If it ain't broke, don't fix it'.

However, in its final report the commission has recommended: 'The Commonwealth and State/Territory governments should establish a form of incorporation under the Corporations Law for Community Social Welfare Organisations.'

This recommendation, if implemented, would have major implications for the churches. It would mean hiving off the social welfare work into an incorporated entity. This is a splitting of 'word' and 'deed'. Sydney's Wesley Mission believes that such a division is wrong theologically, contrary to what was intended in 1884 when the first mission (Sydney's Central Methodist Mission) was formed, and it will lead to a deterioration in the quality of the 'deed'.

Finally, the implementation of such a recommendation would be very complicated in that a division would need to be made in matters of ownership of property, control of finance, and allocation of trust funds. All this, of course, assumes that a clear split could in fact be made between 'word' and 'deed' activities.

But from a governmental point of view this recommendation has several advantages. One is that the 'word' is greatly reduced in size. Governments are restricted by the Australian Constitution as to what they can do to regulate religion, and so this recommendation reduces the area which is often inaccessible for their legislation. Another is that the 'deed' is then more vulnerable to increased government regulation and scrutiny. The government, in its initial response to the final report, has said that this recommendation requires further consideration.

Micro reforms

The third level of analysis of the Industry Commission's work deals with such matters as new accounting standards and quality management systems. The Industry Commission has recommended that more attention be given to the standardisation of quality management accreditation systems via the ISO 9000 series. But there is at present no system specifically designed for charities.

More fundamentally, charities in the different sectors are already covered by outcome standards monitoring programs of various sorts to fit the requirements of different government departments. The implication is that the existing requirements would have to be relinquished by

government departments. This may not be acceptable to those departments. After all, the present programs have been devised to meet the specific requirements of each department; a generalised ISO 9000 series system may not be specific enough to cover such diverse areas as, say, nursing homes and refugee operations.

Finally, the draft and final reports place emphasis on benchmarking. The problem for charities is that they can demonstrate a great deal but can actually measure very little. How, for example, is the Lifeline telephone counselling operation to measure its performance? If it were to do so, say, on the basis of the number of callers dealt with per hour, there is the risk that counsellors would cut short telephone counselling sessions in order to increase their rating on the number of people dealt with.

Conclusion

To conclude, first, it is still not clear why the Industry Commission was asked to examine charities. There are, of course, periodic concerns about some actions of some charities, such as the financial difficulties of the CARE Australia overseas aid organisation. But these difficulties could be addressed by creating new accounting standards and other administrative changes. To ask the Industry Commission to do this work was like using a sledge hammer to crack a nut. This mystery is all the more so when it is recalled that charities operate outside the usual economic paradigm of the Industry Commission.

Second, not all of the country's charities were examined. It is not clear what is to happen to them in the implementation of the commission's recommendations. To take the controversial example which has been ruled out by the present government: the commission's recommendation on scrapping the exemption from the fringe benefits tax would have been inequitable if it had only applied to some charities and not all of them (such as those in health, education and sport).

Third, the commission remained troubled by the term 'community social welfare organisation'. It could not provide a clear definition of what is a 'charitable' organisation (or, for that matter, 'social welfare'). The laws regarding charities/public benevolent institution are, it is widely agreed by people in these organisations, a mess. But the commission could not sort out that mess because it was dealing with only one, arbitrarily created, slice of the charities.

Fourth, taking these points together, there is still a task to be done in trying to sort out the laws regarding charities. My perception is that the charities would prefer to stick with what they have and to deal with their daily tasks rather than have yet another government inquiry to try to sort out the laws. But there remains the chance that a government in the future will try to address the issue. This is especially so if such a government would like to bring charities more clearly within the government's scope and make them more an arm of government, for example, in the delivery of services.

Finally, the entire episode says a great deal about the politics of public inquiries. One lesson is the importance of lobbying and the way in which the charities were able to use the mass media and their own contacts with politicians to blunt the impact of the commission's work, such as the speed with which the Federal Government and Opposition both agreed that the recommendation on scrapping the fringe benefits tax exemption should not be implemented.

A second lesson is the issue of timing. The final report has appeared too close to the federal election; all the parties have decided that this is not a good time to be making enemies among the charities.

A third lesson is that ideas in official reports never disappear entirely. The proposals regarding input taxes and the fringe benefits tax, for example, will linger in the Treasury's mind and could be revived during a budget when there is a long gap before the next federal election.

To sum up, we have not heard the last of the Industry Commission report.

Note

The views expressed in this article are personal, and not necessarily those of the organisations to which the author has provided advice.

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