

# ***TR 2019/6 - Income tax: the 'in Australia' requirement for certain deductible gift recipients and income tax exempt entities***

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 There is a Compendium for this document: **TR 2019/6EC** .



## Taxation Ruling

### Income tax: the ‘in Australia’ requirement for certain deductible gift recipients and income tax exempt entities

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#### **❶ Relying on this Ruling**

This publication (excluding appendix) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

If this Ruling applies to you, and you correctly rely on it, we will apply the law to you in the way set out in this Ruling. That is, you will not pay any more tax or penalties or interest in respect of the matters covered by this Ruling.

Further, if we think that this Ruling disadvantages you, we may apply the law in a way that is more favourable to you.

## Summary – what this Ruling is about

1. This Ruling provides the Commissioner’s view on the following conditions in the *Income Tax Assessment Act 1997*<sup>1</sup> dealing with deductible gift recipients (DGRs) and exempt entities:

- the condition that certain<sup>2</sup> DGRs be ‘in Australia’ before a gift or contribution to them is tax deductible (the DGR in Australia condition)<sup>3</sup>
- the condition that certain entities have a ‘physical presence in Australia’, and to that extent, incur their expenditure and pursue their objectives principally ‘in Australia’, before their income is exempt from tax (the Division 50 in Australia condition)<sup>4</sup>
- the condition that a registered charity or DGR have a ‘physical presence in Australia’ before it qualifies for a refund of franking credits.<sup>5</sup>

2. This Ruling does not consider the meaning of the words ‘in Australia’ in other parts of Australian taxation law.

<sup>1</sup> All legislative references are to the *Income Tax Assessment Act 1997* unless otherwise indicated.

<sup>2</sup> For those funds, authorities or institutions covered by a table item in Subdivision 30-B.

<sup>3</sup> See paragraph 3 of this Ruling for the definition of DGR in Australia and the DGR in Australia condition from paragraph 4 of this Ruling.

<sup>4</sup> See paragraph 3 of this Ruling for the definition of Division 50 in Australia condition and the Division 50 in Australia condition from paragraph 48 of this Ruling.

<sup>5</sup> Section 207-117.

## Definitions

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3. The following terms are used in this Ruling:
- **ACNC** means the Australian Charities and Not-for-profits Commission.
  - **DGR in Australia condition** refers to the special condition that a fund, authority or institution be 'in Australia' to be entitled to DGR endorsement.<sup>6</sup>
  - **Division 50 in Australia condition** refers to the special condition that certain entities have a physical presence in Australia and, to that extent, incur their expenditure and pursue their objectives principally 'in Australia', in order to be tax exempt.<sup>7</sup>

## Ruling

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### DGR in Australia condition

4. The DGR in Australia condition<sup>8</sup> requires a fund, authority or institution to be 'in Australia'. The phrase 'in Australia' is not defined<sup>9</sup>, and so carries its ordinary meaning.

5. In this context, the word 'be' is considered to mean 'to exist', 'have reality', or be 'to be found or located'<sup>10</sup>; whereas the word 'in' is considered to mean 'inclusion within'.<sup>11</sup> Accordingly, a DGR will be 'in Australia' where Australia can be described as its real location, taking into account its legal form and substance.

6. The DGR in Australia condition is concerned with the location of the fund, authority or institution as an entity or organisation, rather than the physical presence of particular assets or transactions.<sup>12</sup> It therefore requires Australia to be the focal point of the DGR in a legal or organisational sense.

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<sup>6</sup> Special condition (a) of table item 1 in subsection 30-15(2).

<sup>7</sup> Paragraphs 50-50(1)(a), 50-55(1)(a) and 50-70(1)(a).

<sup>8</sup> Special condition (a) in table item 1 in subsection 30-15(2).

<sup>9</sup> Subdivision 960-T provides an extended definition of the word 'Australia', when used in a geographical sense.

<sup>10</sup> Macmillan Publishers Australia, *The Macquarie Dictionary* online, [www.macquariedictionary.com.au](http://www.macquariedictionary.com.au), viewed 25 November 2019.

<sup>11</sup> Macmillan Publishers Australia, *The Macquarie Dictionary* online, [www.macquariedictionary.com.au](http://www.macquariedictionary.com.au), viewed 25 November 2019.

<sup>12</sup> In this regard, the test can be contrasted with the physical presence in Australia requirement. See paragraph 53 of this Ruling. Refer also to paragraphs 5.28-5.29 of the Explanatory Memorandum to the Taxation Laws Amendment Bill (No. 4) 1997.

7. Whether a fund, authority or institution is located in Australia is a question of fact, to be determined based on the circumstances in each case. A DGR would satisfy this requirement where it:

- is established or legally recognised in Australia, and
- makes operational or strategic decisions mainly in Australia.

8. In this context, 'legally recognised' means being given status by the Australian legal system. A fund, authority or institution could be legally recognised in a number of ways, including being registered under the *Australian Charities and Not-for-profits Commission Act 2012* (ACNC Act), *Corporations Act 2001*, or *A New Tax System (Australian Business Number) Act 1999* (ABN Act); or being an incorporated association under an Act of Parliament of a State or Territory.

### **Fund**

9. The word 'fund' is not defined and so carries its ordinary meaning. For the purposes of the DGR in Australia condition, a 'fund' is an arrangement where a stock of money or pecuniary resources is held or managed in accordance with a trust deed or similar instrument such as a set of fund rules.<sup>13</sup>

10. A fund will be 'in Australia' where the arrangement for holding the relevant stock of money or pecuniary resources:

- is established or legally recognised in Australia, and
- is managed by way of operational or strategic decisions<sup>14</sup> made mainly in Australia.

11. Typically, a fund would be established in Australia by way of a will or instrument of trust settled in Australia. Alternatively, it may be established by another entity that is legally recognised in Australia and which holds and operates the fund. It may also be legally recognised in Australia by obtaining an ABN or registering as a charity.

12. Where a fund is not a separate trust, it is usually operated as part of an entity. In these cases it is the fund that must satisfy the DGR in Australia condition, rather than the entity that holds or controls the fund.<sup>15</sup> While such a fund will not qualify for an ABN or registration as a charity in its own right, recognition of the entity (for example, an incorporated association or company limited by

<sup>13</sup> This meaning is consistent with the meaning adopted for the purposes of Division 50. Refer to paragraph 224 of Taxation Ruling TR 2011/4 *Income tax and fringe benefits tax: charities*.

<sup>14</sup> In the case of a fund, strategic and operational decisions will typically be effectively the same thing; that is, decisions to make, hold and dispose of investments reflect both strategic and operational management of the fund.

<sup>15</sup> The entity that operates the fund may still need to satisfy the Division 50 in Australia condition. See paragraph 50 of this Ruling.

guarantee) operating the fund will be sufficient to provide the fund with legal recognition for these purposes.

13. The location of decision making is determined on the basis of where the fund's decision-making powers are mainly exercised.

14. The DGR in Australia condition does not require funds to have purposes or beneficiaries located in Australia.

*Example 1 – fund ‘in Australia’*

15. *The Cambodian Education Society (the CES) is a not-for-profit organisation in Australia, registered as a charity by the ACNC. The CES was established by an instrument of trust settled in Australia. It is a public fund solely for providing money for the construction of a building to be used by the CES as a school for disadvantaged children in Cambodia.*

16. *The CES public fund seeks endorsement as a DGR under table item 2.1.10 in subsection 30-25(1).*

17. *The trustee of the CES public fund is a company and its directors manage the company in Australia. The trustee opens a bank account in Australia and receives donations from members of the Australian public and from ancillary funds. The monies received are held by the trustee in accordance with the terms of the fund's trust deed.*

18. *The CES public fund meets the DGR in Australia condition. It is established and legally recognised in Australia, since it is established by a trust deed in Australia and legally recognised under the ACNC Act. Further, it is managed by way of decisions made in Australia. It does not matter that the fund has purposes and beneficiaries located in Cambodia.*

19. Where the decision makers are ordinarily located in more than one place, a fund would make operational or strategic decisions mainly in Australia if the balance of decision-making power in relation to operational or strategic matters mainly lies in Australia.

*Example 2 – fund ‘in Australia’*

20. *The Kitsune Foundation, a global not-for-profit organisation founded in Japan, has set up an Australian entity called the Megitsune Foundation. The Megitsune Foundation, a company limited by guarantee, is a registered charity that has a principal purpose of protecting the arctic fox from habitat loss, exploitation and hunting.*

21. *The Megitsune Foundation operates a public fund to raise money from the Australian public to help fund global research projects to address the declining arctic fox population. It is seeking endorsement as a DGR under table item 6.1.1 in subsection 30-55(1).*

22. *Funds raised from the Australian public are controlled by an executive committee. The executive committee is made up of:*

- *three members of the Megitsune Foundation who are responsible persons<sup>16</sup> and reside in Australia, and*
- *two members of the Kitsune Foundation who reside in Japan.*

23. *Committee members meet regularly using teleconferencing facilities in their respective countries. At these meetings, the committee makes all high-level and operational decisions concerning the fund. In making these decisions, each committee member has an equal vote.*

24. *The Megitsune Foundation fund satisfies the DGR in Australia condition. The fund is legally recognised in Australia as it is held by an Australian company that is a registered charity. Further, the balance of the fund's decision-making powers is exercised in Australia so the fund is managed by way of decisions made mainly in Australia. This outcome would not change if the fund's Australian committee members occasionally meet and make decisions whilst outside of Australia, provided overall the fund's decisions are mainly made in Australia.*

### **Authority**

25. The word 'authority' is not defined and so carries its ordinary meaning. For the purposes of the DGR in Australia condition, an 'authority' is an agency or instrument of government, established to exercise control or execute a government function in the public interest.<sup>17</sup>

26. Accordingly, an authority will be 'in Australia' where the relevant government agency or instrument:

- is established or legally recognised in Australia, and
- makes its operational or strategic decisions mainly in Australia.

27. Typically, an authority would be established or legally recognised in Australia by way of a statute created by the Commonwealth, a State or Territory government.

### **Example 3 – authority 'in Australia'**

28. *The Southern Abalone Authority (SAA) is established by a State government to manage the abalone fishery in parts of the State.*

<sup>16</sup> Refer to paragraph 9(f) of Taxation Ruling TR 95/27 *Income tax: public funds*.

<sup>17</sup> *Committee of Direction of Fruit Marketing v Australian Postal Commission* [1980] HCA 23; *Renmark Hotel Inc v Commissioner of Taxation* [1949] HCA 7; *General Steel Industries Inc v Commissioner for Railways* [1964] HCA 69; *Re Anti-Cancer Council (Vic)*; *State Public Services Ex p* [1992] HCA 53.

*The SAA engages in research and development and investment on mitigating abalone-related diseases. It operates from leased premises in a regional centre.*

29. *The SAA funds its activities from research donations, grants, commercial abalone licences and policing fines.*

30. *The SAA is an Australian government agency and is seeking endorsement as a DGR under table item 1.1.4 in subsection 30-20(1).*

31. *The SAA satisfies the DGR in Australia condition. The SAA is established by a State government in Australia and is operated in Australia because it executes a function in the public interest in Australia.*

### ***Institution***

32. The word 'institution' is not defined and so carries its ordinary meaning. For the purposes of the DGR in Australia condition, an 'institution' is an establishment, organisation or association instituted for the promotion of some object, especially one of public or general utility. Such a body is called into existence to translate a defined purpose into a living and active principle.<sup>18</sup>

33. An institution will be 'in Australia' where it:

- is established or legally recognised in Australia, and
- makes its operational or strategic decisions mainly in Australia.

34. An institution could be established or legally recognised in Australia in a number of ways, including<sup>19</sup>:

- registration under the *Corporations Act 2001*
- incorporation under State or Territory legislation
- registration as a charity under the ACNC Act
- registration under the ABN Act.

35. The location of decision making is determined on the basis of where the institution's decision-making powers are mainly exercised. Where decision makers are ordinarily located in more than one place, their decisions would be in Australia where the balance of decision-making power usually lies in Australia.

36. An institution that makes operational decisions in Australia may be in Australia, even though its strategic decisions are made offshore.

<sup>18</sup> *Stratton v Simpson* [1970] HCA 45; paragraph 165 of TR 2011/4.

<sup>19</sup> Whilst an institution may hold funds under the terms of a trust settled under Australian law, the fund will not be an 'institution' in its own right. Refer to paragraph 225 of TR 2011/4.

*Example 4 – institution ‘in Australia’*

37. The Neuromuscular Disease Foundation Australia (NDFA) is a company limited by guarantee, and registered as a health promotion charity by the ACNC. The NDFA is seeking endorsement as a DGR under table item 1.1.6 in subsection 30-20(1).

38. The NDFA has a charitable purpose of promoting the prevention of neuromuscular disease by raising public awareness of the disease and its causes. The NDFA has sibling organisations in the UK, USA and Canada. The NDFA works closely with the UK entity which acts on behalf of the other organisations.

39. The majority of the directors of the NDFA are ordinarily located in the UK. The other directors are based in Australia. Key strategic decisions concerning the NDFA are made at board meetings that are held twice a year by videoconferencing facilities. In making these decisions, each director has an equal vote.

40. The NDFA's activities require active day-to-day management. The NDFA's Australian directors perform this function from an office in Sydney. These directors apply their independent judgment to ensure the effective operation of the institution, in accordance with guidelines and decisions of the board.

41. The NDFA satisfies the DGR in Australia condition. It is established and legally recognised in Australia under the Corporations Act 2001 and ACNC Act. The NDFA also makes operational decisions in Australia, since the decision-making powers regarding operational matters are exercised in Australia.

42. Conversely, an institution that makes strategic decisions in Australia may be ‘in Australia’, even though its operational decisions are made offshore.

*Example 5 – institution ‘in Australia’*

43. Assume the facts in Example 4, but with the following changes:

- A majority of NDFA's directors are based in Australia.
- Day-to-day administration of the NDFA's operations is mainly undertaken by the NDFA's UK-based directors from an office in London.

44. The NDFA satisfies the DGR in Australia condition, since the balance of decision-making power in relation to strategic matters is in Australia.

45. In contrast, an institution would not be ‘in Australia’ where neither operational nor strategic decisions are made in Australia.



*Example 6 – institution not ‘in Australia’*

46. Assume the facts in Example 4, but with the following changes:

- *The NDFA was originally established in Australia as an unincorporated association, registered as a charity with the ACNC.*
- *Although the NDFA was originally intended to operate programs in Australia using funds raised from the Australian public, it now raises funds globally and is effectively controlled by managers based in London.*
- *In practice, NDFA’s UK managers make all strategic and operational decisions relating to the operation of the institution.*
- *The NDFA has an Australian-based agent who performs administrative tasks necessary to implement its decisions in Australia.*

47. *The NDFA fails the DGR in Australia condition. Although it was established in Australia, no decisions made in Australia play a substantial role in the management of NDFA or its operations, which involve raising and distributing funds and undertaking other activities on a global basis.*

**Division 50 in Australia condition**

48. An entity satisfies the Division 50 in Australia condition if it has a physical presence in Australia and, to that extent, incurs its expenditure and pursues its objectives principally in Australia.

49. Apart from the exceptions in paragraphs 50 and 51 of this Ruling, the following entities must satisfy the Division 50 in Australia condition:

- registered charities
- scientific institutions
- public educational institutions
- public hospitals and hospitals carried on by a society or association
- societies, associations or clubs established for the encouragement of science
- societies, associations or clubs established for community service purposes
- societies, associations or clubs established for the encouragement of animal racing, art, a game or sport, literature or music, and

- societies, associations or clubs established for musical purposes.<sup>20</sup>

50. An entity does not need to meet the Division 50 in Australia condition if the entity itself meets the qualifying conditions to be a DGR, including the DGR in Australia condition.<sup>21</sup> In contrast, an entity that merely controls a fund which is a DGR is not a DGR itself and so may still need to meet the Division 50 in Australia condition (see Example 12 of this Ruling).

51. Further, an entity does not need to meet the Division 50 in Australia condition if it is:

- a prescribed institution, society, association or club located outside Australia and exempt from income tax in the country in which it is resident, or
- a registered charity that is a prescribed institution that has a physical presence in Australia but which incurs its expenditure and pursues its objectives principally outside Australia.<sup>22</sup>

### ***First requirement – physical presence in Australia***

52. 'Physical presence' is not defined and so carries its ordinary meaning. Ordinarily, the word 'physical' means 'of or relating to material nature'<sup>23</sup> and 'presence' as 'the state or fact of being present, as with others or in a place'.<sup>24</sup>

53. In the context of the Division 50 in Australia condition, an entity has a physical presence in a place where it employs assets or people to conduct its range of physical operations. The entity may be legally established in Australia, or conduct its operations through a division, subdivision or branch in Australia.<sup>25</sup> However, an entity would not have a physical presence in Australia merely because it operates through an agent based in Australia.<sup>26</sup>

<sup>20</sup> Table items 1.1, 1.3, 1.4 and 1.7 in section 50-5, table item 2.1 in section 50-10, table items 6.1 and 6.2 in section 50-30, and table items 9.1 and 9.2 in section 50-45.

<sup>21</sup> These entities have met the special conditions in Division 50 by satisfying an alternative test. Refer to paragraphs 50-50(1)(b) to (d), 50-55(1)(b) and 50-70(1)(b).

<sup>22</sup> These entities have met the special conditions in Division 50 by satisfying an alternative test. Refer to paragraphs 50-50(1)(b) to (d), 50-55(1)(b) and (c), and 50-70(1)(b) and (c).

<sup>23</sup> Macmillan Publishers Australia, *The Macquarie Dictionary Online*, [www.macquariedictionary.com.au](http://www.macquariedictionary.com.au), viewed 25 November 2019.

<sup>24</sup> Macmillan Publishers Australia, *The Macquarie Dictionary Online*, [www.macquariedictionary.com.au](http://www.macquariedictionary.com.au), viewed 25 November 2019.

<sup>25</sup> Paragraph 5.28 of the Explanatory Memorandum to the Taxation Laws Amendment Bill (No. 4) 1997 and paragraph 3.12 of the Explanatory Memorandum to the Taxation Laws Amendment Bill (No. 3) 1998.

<sup>26</sup> Paragraph 5.28 of the Explanatory Memorandum to the Taxation Laws Amendment Bill (No. 4) 1997.

***Second requirement – incurs expenditure and pursues objectives principally in Australia***

54. To meet the Division 50 in Australia condition an entity that has a physical presence in Australia must also, to that extent, incur its expenditure and pursue its objectives principally in Australia.

55. The words ‘to that extent’ require an examination of the degree to which the entity has a physical presence in Australia, as opposed to other places. Accordingly, all of the entity’s operations and objectives must be identified and compared.

56. Where an entity has a physical presence in Australia only, it must incur its expenditure, and pursue its objectives, principally in Australia.

57. Where an entity has a physical presence in Australia and also overseas, only the expenditures incurred and objectives pursued which are attributable to that entity’s physical presence in Australia are examined. For example, if an entity has a physical presence in Australia through the operation of a division, the second requirement applies only to expenditure and objectives which are attributable to the Australian division.

***Principally***

58. The word ‘principally’ is not defined, and so carries its ordinary meaning of mainly or chiefly. While each case turns on its facts, more than 50% would ordinarily be considered to meet the ‘principally’ requirement.<sup>27</sup>

***Incurs its expenditure***

59. The phrase ‘incurs its expenditure’ is not defined and so carries its ordinary meaning. Expenditure<sup>28</sup> is incurred when the entity pays out or disburses money or is liable to do so.<sup>29</sup>

60. The place where an entity ‘incurs its expenditure’ requires a characterisation of the expenditure, based on the facts in each case.

61. An entity does not incur expenditure in Australia merely because the expenditure relates to a physical presence of the entity in Australia.

62. The required connection will ordinarily exist where the decision to pay is made in Australia, and payment is to occur from an

<sup>27</sup> Paragraph 3.14 of the Explanatory Memorandum to the Taxation Laws Amendment Bill (No. 3) 1998.

<sup>28</sup> Examples of expenditure include payments, or accounts payable, for rent, utilities, salary and wages, and goods or services. It also includes the distribution of gifts and grants that an entity has received.

<sup>29</sup> Refer to paragraph 6 of Taxation Ruling TR 97/7 *Income tax: section 8 1 – meaning of ‘incurred’ – timing of deductions* for additional guidance on the meaning of incurred.

Australian source, for example, an account held with an Australian financial institution (see Examples 7 and 8 of this Ruling).<sup>30</sup>

*Pursues its objectives*

63. Similarly, the phrase ‘pursues its objectives’ is not defined and so carries its ordinary meaning.

64. The place where an entity ‘pursues its objectives’ requires a characterisation of the entity’s activities, based on the facts in each case.

65. An entity does not pursue its objectives in Australia merely because it undertakes some of its activities in Australia.

66. An entity ordinarily pursues its objectives in the place where it seeks to realise its purposes, whether by making distributions to other entities or supplying goods or services in the course of its operations.

67. An entity does not pursue its objectives in Australia merely because it incurs expenditure in Australia. However, the expenditure incurred by an entity may be an indication of where its objectives are being pursued.

68. For instance, an entity may pursue its objectives in Australia by:

- making a distribution to a recipient located in Australia (see Example 7 of this Ruling)<sup>31</sup>, or
- purchasing goods or services for, or for the purposes of, consumption in Australia (see Examples 8 and 9 of this Ruling).<sup>32</sup>

69. On the other hand, an entity may pursue its objectives outside Australia by:

- making a distribution to a recipient located outside of Australia (see Example 7 of this Ruling), or
- purchasing goods or services for, or for the purposes of, consumption outside of Australia (see Example 10 of this Ruling).

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<sup>30</sup> *Commissioner of Taxation of the Commonwealth of Australia v Word Investments Limited* [2008] HCA 55 (*Word Investments*) at [73].

<sup>31</sup> In *Word Investments* [at [73], a majority of the High Court held that the purpose of Word Investments Limited could be fulfilled by, among other things, making distributions to other institutions which had charitable purposes

<sup>32</sup> We consider the purchase of goods and services to be distinguishable from the making of a distribution, as was considered by the High Court in *Word Investments*.

*Continuous periodic testing*

70. To maintain Division 50 income tax exemption, an entity must continue to satisfy the Division 50 in Australia conditions, including the condition that the entity incurs its expenditure and pursues its objectives principally in Australia.

71. Whilst the test applies continuously and requires an overall assessment of the entity's operations, it operates periodically<sup>33</sup>, with a focus on the current income year.

72. Accordingly, it may be inferred that an entity no longer incurs its expenditure and pursues its objectives principally in Australia where it chooses to incur expenditure relating to the pursuit of its objectives primarily outside of Australia in a given income year (see Examples 7 and 10 of this Ruling).

73. On the other hand, the weight attached to current year expenditure may be reduced where it arises in circumstances that are not reasonably reflective of the entity's overall operations, purposes or objectives. This may be the case where the expenditure is unusual and arises from a mistake or from circumstances that are beyond the entity's control. In these cases, the conclusion to be drawn may be affected by evidence of past or intended expenditure (see Example 11 of this Ruling).

***Disregarded amounts – certain distributions may be made overseas***

74. In determining whether an entity incurs expenditure and pursues objectives principally in Australia, section 50-75 disregards any distributions that the entity makes out of amounts (disregarded amounts) received:

- 'as a gift'
- by way of government grant, or
- from a DGR operated by the entity.

75. This means that where an entity distributes disregarded amounts offshore, this will not affect whether it satisfies the Division 50 in Australia condition.

76. For the purposes of section 50-75, the phrase 'as a gift' is considered to refer to circumstances which involve an element of benefaction. This covers money or property which is a 'gift' in the ordinary meaning of the word<sup>34</sup>, as well as receipts from fundraising by raffles, dinners, auctions, jumble sales<sup>35</sup>, the purpose of which are

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<sup>33</sup> *Word Investments* at [34].

<sup>34</sup> This Ruling does not consider the ordinary meaning of the word 'gift'. Refer to Taxation Ruling TR 2005/13 *Income tax: tax deductible gifts – what is a gift*.

<sup>35</sup> Paragraph 3.18 of the Explanatory Memorandum to the Taxation Laws Amendment Bill (No 3) 1998.

to benefit the entity in a material sense.<sup>36</sup> It excludes amounts received from commercial activities or contracts for services.

77. The phrase 'government grants' is not defined and so takes its ordinary meaning. Government grants include payments made by government to entities for specific purposes, whether or not the entity is placed under an obligation to ensure that the grant is applied for those purposes, but do not include payments made by government by way of a fee for services.

78. When and where a gift or government grant is distributed is a question of fact, to be determined based on the circumstances in each case.

79. Section 50-75 requires an entity to determine the extent to which a distribution is sourced from an amount received as a gift, by way of government grant or from a DGR. For these purposes, the entity can choose to appropriate distributions from a particular source<sup>37</sup>, provided it maintains records which clearly identify each source, and such a treatment is not inconsistent with any conditions attached to the gift or grant (see Example 12 of this Ruling).

*Example 7 – expenditure incurred by way of distributions to other organisations or funds*

80. *The Faithism Foundation is a company limited by guarantee that is a registered charity under table item 1.1 in section 50-5.*

81. *The Faithism Foundation's charitable purpose is to advance the Faithism religion. Its objectives are to inform the public about the beliefs of the Church of Faithism and to make funds available to organisations which run websites and conduct public seminars regarding Faithism.*

82. *The Faithism Foundation receives income from commercial activities and investments.*

83. *Evangelical organisations contact the Faithism Foundation and request funding. The Faithism Foundation evaluates each request and decides whether to make a distribution and, if so, in what amount and on what conditions.*

84. *The Faithism Foundation is governed by a board of directors. The activities of the Faithism Foundation are carried out by a mix of volunteers and paid employees.*

85. *The Faithism Foundation has its headquarters in Melbourne. It employs a project officer who vets incoming requests from charitable*

<sup>36</sup> *Leary, B.A. v Commissioner of Taxation for the Commonwealth of Australia* [1980] FCA 134, per Deane J.

<sup>37</sup> This is analogous to the ability of a liquidator to appropriate distributions to a particular fund of profit or income. Refer to Taxation Determination TD 95/10 *Income tax: what is the significance of the Archer Brothers principle in the context of liquidation distributions?* and paragraph 5.70 of the Explanatory Memorandum to the Taxation Laws Amendment Bill (No 4) 1997.

organisations. The project officer makes a recommendation to the board, which decides whether to make a distribution. The guidelines provided to the project officer for vetting applications place no limit or preference on favouring contributions that are made to organisations that are in Australia.

86. For the purposes of this example:

- ABC Fund is an organisation headquartered in Sydney that promotes the Faithism religion in Australia.
- DEF Fund is an organisation headquartered in Melbourne whose activities consist primarily of paying the expenses of Faithism missionaries in overseas countries.
- XYZ Society is headquartered in New York and promotes the Faithism religion in the USA only.
- Australian operating costs comprise general operating expenses paid to persons or entities located in Australia.

#### Scenario a

87. In the 20X1 income year, the Faithism Foundation incurred the following expenditure:

<b>Expenditure</b>	<b>Amount</b>	<b>% of total</b>
Distribution to ABC Fund	\$10,000	11%
Distribution to DEF Fund	\$50,000	56%
Australian operating costs	\$30,000	33%
Total	\$90,000	100%

88. Distributions to the ABC Fund and DEF Fund comprise expenditure incurred in Australia because the payments are made to an organisation in Australia. It does not matter that the DEF Fund ultimately expends the funds overseas.

89. In the absence of further evidence about its expenditure and activities, it can be inferred that the Faithism Foundation incurs its expenditure principally in Australia. It can also be inferred that the Faithism Foundation pursues its objectives in Australia because it has sought to realise its objectives by making distributions to entities in Australia.

Scenario b

90. *In the 20X2 income year, the Faithism Foundation incurred the following expenditure:*

<b>Expenditure</b>	<b>Amount</b>	<b>% of total</b>
<i>Distribution to ABC Fund</i>	<i>\$10,000</i>	<i>5%</i>
<i>Distribution to DEF Fund</i>	<i>\$50,000</i>	<i>25%</i>
<i>Distribution to XYZ Society</i>	<i>\$110,000</i>	<i>55%</i>
<i>Australian operating costs</i>	<i>\$30,000</i>	<i>15%</i>
<i>Total</i>	<i>\$200,000</i>	<i>100%</i>

91. *In the 20X2 income year, 55% of the Faithism Foundation's total expenditure is distributed to an organisation which is not in Australia. Accordingly, this expenditure does not relate to the pursuit of objectives in Australia. In the absence of further evidence about its expenditure and activities, it can be inferred that the Faithism Foundation no longer pursues its objectives principally in Australia and therefore fails the Division 50 in Australia condition.*

*Example 8 – expenditure incurred to pursue objectives in Australia*

92. *Life Learning is an association incorporated in South Australia and registered as a charity with the ACNC.*

93. *Life Learning produces educational materials which are designed for use by teachers and primary school aged children in Australian schools. Materials created by Life Learning are distributed electronically via the Life Learning website.*

94. *All decisions relating to Life Learning's operations are made by staff located in Adelaide. Life Learning pays employees and contractors to create its educational materials and maintain its website, as well as general operating costs. These amounts are paid from an account held with an Australian bank.*

95. *Life Learning owns all intellectual property associated with the materials produced for it, but allows those materials to be used by schools, teachers and students. Whilst the material is designed for Australian schools, Life Learning is aware that its materials are used extensively by overseas users.*

96. *Life Learning is incurring its expenditure and pursuing its objectives principally in Australia. Decisions to pay expenditure are made in Australia, and payments are made from an Australian source. Further, Life Learning's expenditure on services to be consumed in Australia indicates that it is pursuing its objectives in Australia. It does not matter that material produced by Life Learning is then also accessible and used by persons outside of Australia.*



*Example 9 – expenditure incurred to pursue objectives in Australia – offshore recipient*

97. *Pastoral Care is an Australian registered charity, whose charitable purpose is to advance religion in Australia. Its objectives are to inform the Australian public about its religious beliefs and provide pastoral care to the Australian community.*

98. *All decisions relating to Pastoral Care's operations are made by staff located in Brisbane. Pastoral Care purchases printed literary material from a supplier located in the USA, solely for the purpose of distribution to recipients in Australia. Pastoral Care also pays for freight, handling and facilitation services necessary to have this material sent from the supplier to Australia. These purchases, which are funded from an account held with an Australian bank, amount to 60% of Pastoral Care's expenditure in the 20X1 income year.*

99. *Pastoral Care is incurring its expenditure and pursuing its objectives principally in Australia. Decisions to pay expenditure are made in Australia, and payments are made from an Australian source. Further, the incurring of expenses to obtain goods for consumption in Australia indicates that Pastoral Care is pursuing its objectives principally in Australia.*

*Example 10 – expenditure incurred to pursue objectives outside of Australia*

100. *The Melbourne-based Australian Accounting School (AAS) is a company limited by guarantee that is a public educational institution under table item 1.4 in section 50-5.*

101. *The main objective of AAS is to provide accounting-based training to the Australian community. Due to increased demand to provide training to overseas-based students, AAS establishes a separate entity in China, the China Accounting School (CAS), from which overseas-based students will be trained.*

102. *CAS has administrative staff only. AAS provides the educational function by sending subcontractors from Australia to China to provide training. AAS pays the fees and travel expenses for the teacher providing training in China. CAS does not reimburse AAS for this expenditure. In the 20X1 income year, this represents 60% of the total expenditure of the AAS.*

103. *In the absence of further information about AAS's expenditure and activities, it can be inferred that AAS does not pursue its objectives principally in Australia. AAS's expenditure on services consumed in China indicates that it is principally pursuing its objectives outside of Australia.*

*Example 11 – expenditure incurred to pursue objectives in Australia – unusual circumstances*

104. Prior to its destruction in an accident in 20X3, the observatory operated by the Hilltop Astronomy Association (HAA) had been a nationally popular venue used to teach groups of Australian schoolchildren about the universe.

105. The HAA's committee of management formulate a plan to rebuild and extend the facilities. Funds of \$3 million will be accumulated in the two years prior to the commencement of reconstruction activities in 20X6. During this period, the expenditure of the HAA in Australia is limited to the initial costs of building design, office administration and the maintenance of an interactive educational website. The amount of Australian expenditure is marginally less than the ongoing contribution that the HAA makes to school training programs in three South Pacific Island nations. The total of expenditure in each of the years is approximately \$400,000.

106. In the 20X4 and 20X5 income years, less than 50% of the actual expenditure of the HAA relates to the objectives of HAA in Australia. However, it is necessary to consider whether HAA remains the type of association which can be characterised as pursuing its objectives principally in Australia. In this regard, it is relevant to consider the history of the association and the current planning for the reconstruction of the observatory. Based on the whole of the facts, the HAA has not at any time ceased to be an entity that incurs its expenditure and pursues its objectives principally in Australia. The HAA at all times satisfies the Division 50 in Australia condition.

*Example 12 – disregarded amounts*

107. The Vandalay Association is a charitable performing arts company established for the purpose of the promotion of Australian ballet. Vandalay Association is a registered charity which operates a fund listed on the register of cultural organisations under table item 12.1.1 in subsection 30-100(1). This fund is known as the Vandalay Cultural Development Fund.

108. While the Vandalay Association can disregard amounts it receives from the Vandalay Cultural Fund<sup>38</sup>, it does not satisfy the Division 50 in Australia condition merely because it operates this DGR. In order to satisfy the Division 50 in Australia condition, the Vandalay Association must examine its expenditure and the pursuit of its objectives as they relate to its physical presence in Australia.

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<sup>38</sup> Subsection 50-75(2).

109. *The Vandalay Association keeps records that clearly indicate the sources of its income and its use of these funds. In the 20X1 income year, The Vandalay Association's income of \$150,000 comprises the following amounts:*

<b>Income</b>	<b>Amount</b>
<i>Investments</i>	\$13,000
<i>Performance fees</i>	\$50,000
<i>Distributions from the Vandalay Cultural Development Fund</i>	\$75,000
<i>Conditional government grant</i>	\$12,000
<b>Total</b>	<b>\$150,000</b>

110. *The government grant of \$12,000 is provided on the condition that the funds are spent only on ballet performances occurring in Australia.*

111. *In the 20X1 income year, the Vandalay Association made a distribution of \$87,000 to a performing arts company in China. Of the remaining receipts, \$53,000 is spent on organising performances in Australia and the remaining \$10,000 is held in reserve. The \$53,000 amount includes \$3,000 which was spent on sending a performer on a 10-day intensive training course in Asia in preparation for Australian performances. The Vandalay Association's use of funds for the 20X1 year is summarised as follow:*

<b>Expenditure</b>	<b>Amount</b>	<b>% of total</b>
<i>Distribution to performing arts company in China</i>	\$87,000	58%
<i>Australian performances (including the \$3,000 training course)</i>	\$53,000	35%
<i>Reserves</i>	\$10,000	7%
<b>Total</b>	<b>\$150,000</b>	<b>100%</b>

112. *In determining where its expenditure is incurred and its objectives are pursued, the Vandalay Association can disregard \$75,000 of its \$87,000 offshore distribution, by treating that amount as having been sourced from the DGR distribution. Therefore:*

- *\$12,000<sup>39</sup> in expenditure (18% of total expenditure) would reflect the pursuit of objectives outside of Australia*

<sup>39</sup> Being the amount of the offshore gift which is not disregarded (that is, \$87,000 less \$75,000). This amount cannot be treated as having been sourced from the government grant, which is conditional on the funds being spent on Australian objectives.

- *the remaining \$53,000<sup>40</sup> in expenditure (82% of total expenditure) would reflect the pursuit of objectives in Australia.*

113. *In the absence of further information about its expenditure and activities, it can be inferred that the Vandalay Association incurs its expenditure and pursues its objectives principally in Australia.*

### **Refund of franking credits**

114. In order to be entitled to the refund of franking credits for a franked distribution that it receives during an income year, a registered charity or DGR must at all times during that year:

- have a physical presence in Australia, and
- to that extent, incur its expenditure and pursue its objectives principally in Australia.<sup>41</sup>

115. For these purposes, the terms 'physically present', and 'incurs its expenditure and pursues its objectives principally in Australia' are considered to have the same meaning as they have in the Division 50 in Australia condition (as described at paragraphs 52 to 73 of this Ruling).<sup>42</sup>

## **Date of effect**

116. This Ruling applies to years of income commencing both before and after its date of issue. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10 *Public Rulings*).

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**Commissioner of Taxation**

18 December 2019

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<sup>40</sup> Including the \$3,000 spent on the intensive training course in Asia for the purpose of performances occurring in Australia.

<sup>41</sup> Section 207-117.

<sup>42</sup> Disregarded amounts do not apply in the context of the conditions in section 207-117.

## Appendix – Detailed contents list

117. The following is a detailed contents list for this Ruling:

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## References

### *Previous draft:*

TR 2018/D1

### *Related Rulings/Determinations:*

TR 95/27; TR 97/7; TR 2005/13;  
TR 2006/10; TR 2011/4;  
TD 95/10

### *Legislative references:*

- ITAA 1997 Subdiv 30-B
- ITAA 1997 30-15
- ITAA 1997 30-20
- ITAA 1997 30-25
- ITAA 1997 30-55
- ITAA 1997 30-100
- ITAA 1997 Div 50
- ITAA 1997 50-5
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- ITAA 1997 50-30
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- ITAA 1997 50-50(1)(a)
- ITAA 1997 50-50(1)(b)
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- ITAA 1997 50-55(1)(b)
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- ITAA 1997 50-70(1)(c)
- ITAA 1997 50-75
- ITAA 1997 50-75(2)
- ITAA 1997 207-117
- ITAA 1997 Subdiv 960-T
- TAA 1953
- ANTS(ABN)A 1999
- ACNC Act 2012
- Corporations Act 2001

### *Cases relied on:*

- Committee of Direction of Fruit Marketing v Australian Postal Commission [1980] HCA 23; (1980) 144 CLR 577
- Federal Commissioner of Taxation of the Commonwealth of Australia v

Word Investments Limited

[2008] HCA 55; (2008) 236  
CLR 204; 2008 ATC 20-072;  
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- Re Anti-Cancer Council (Vic); State Public Services Ex p [1992] HCA 53; (1992) 175 CLR 442
- Renmark Hotel Inc v Commissioner of Taxation [1949] HCA 7; (1949) 79 CLR 10
- Stratton v Simpson [1970] HCA 45; (1970) 125 CLR 138

### *Cases distinguished:*

- Commissioner of Taxation of the Commonwealth of Australia v Word Investments Limited [2008] HCA 55; (2008) 236 CLR 204; 2008 ATC 20-072; (2008) ATR 225

### *Other references:*

- Explanatory Memorandum to the Taxation Laws Amendment Bill (No 4) 1997
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- Exempt entities ~~ Charity / education / science ~~ Scientific institution ~~ Special conditions
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