the bonfire of the charities

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1 In 2004, National Party members of the Social Services Select Committee considering the original Charities Bill made the following comments in the Select Committee's report at page 20:

> *"The consultation process was inadequate with the original [charities] bill and we have major concerns that the redrafted sections of the bill should have been made available for a further period of sector wide consultation. We all know the devil is in the detail and if the bill gets it wrong, as the first draft definitely did* ***the charitable sector will pay the price and we will see many charitable organisations close****. There is the possibility that there are a number of structural issues in the bill remaining unaddressed and without a further period of consultation with the sector it is difficult to fully identify these." [Emphasis added]*

2 In the writer's view, there are indeed a number of structural issues in the Charities Act 2005 as passed, and the New Zealand charitable sector is indeed paying the price.

3 In July 2013, an IRD issues paper *(Clarifying the tax consequences for deregistered charities,* http://taxpolicy.ird.govt.nz/publications/2013-ip-clarifying-tax-consequences-deregistered-charities/overview) noted that 3,902 charities had been deregistered in the period from the charities register opening in February 2007 to November 2012 (see page 10). This figure constitutes almost 15%, or 1 in 6, of the 27,099 charities that are currently registered. The number of charities deregistered is undoubtedly higher now, some 17 months later.

4 This level of deregistration has occurred despite the discretionary power to deregister a charity having been intended to be used in "only in the most extreme circumstances" (Select Committee report, page 8). As then Minister of Consumer Affairs, Hon Judith Tizard, noted at the Committee stage of the Charities Bill (NZPD Vol 625 12 April 2005 page 19967):

> ...the deregistration power is discretionary – it is not obligatory. I would expect the Charities Commission to go through a range of choices and discussions with any charity before that charity is deregistered, but the commission should have the power, if it is clear that fraudulent behaviour is systemic in a charity, to deregister that charity quite quickly.

5 This reflects the original rationale for the Charities Act: the charitable sector had fought for decades to see a Charities Commission established, so that "bad" charities, such as those involved in fraud, or tax avoidance, or money laundering, and the like, could be "weeded out", and the public could have confidence in those that remained (see for example the discussion in Barker, Gousmett and Lord, The Law and Practice of Charities in New Zealand, LexisNexis May 2013, chapters 4 and 5).

6 However, of the 3,902 charities deregistered by November 2012, only 3 were deregistered for "serious wrongdoing".

7 2,489 were deregistered for failing to file an annual return, a transgression the charities regulator (previously the Charities Commission, and now the Department of Internal Affairs) advises will be dealt with less abruptly in future (see http://www.charities.govt.nz/news/non-filing-of-annual-returns/).

8 The balance of 1,410 charities are said to have been deregistered for the following reasons: "non-charitable purposes"; "did not meet registration requirements"; "did not produce evidence of charitable purposes"; and "voluntary deregistration". In the writer's experience, a large proportion of these will be "good" charities deregistered on the basis of fine, technical, and often controversial points of legal interpretation surrounding the definition of charitable purpose; alternatively, they will have "seen the writing on the wall" and deregistered voluntarily to avoid having a formal deregistration decision displayed on the charities regulator's website.

9 It should also be noted that this figure of 1,410 does not include the many hundreds of other good charities that have been declined registered charitable status, or otherwise been simply "burned off" by the process.

10 While some charities manage to survive non-

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registration (the Sensible Sentencing Trust being a notable example), they are the exception rather than the rule. Most charities that are denied registration struggle to survive: they struggle to challenge decisions of the regulator in the framework as it is currently structured; they struggle to gain funding as busy funders rightly or wrongly restrict funding to registered charities only; they struggle with issues of confidence and credibility, as the reasons for having been rejected by their own regulator are difficult to communicate to their stakeholders. As foreshadowed by the National Party in 2004, many are forced to close.

11 Some have argued that this "bonfire of the charities", and the consequential chilling effect it gives rise to, is causing a systematic deconstruction of the New Zealand charitable sector.

12 The Government appears to have sought to deal with controversy by disestablishing the Charities Commission from July 2012, and transferring its functions to a Charities Registration Board comprised of 3 persons appointed by the Minister and the Department of Internal Affairs.

13 Submitters had overwhelmingly opposed the disestablishment of the Charities Commission, arguing that "throwing the baby out with the bathwater" would not fix the underlying problem (which, as expected, it has not). However, the Government refused to listen, and Part 3 of the Crown Entities Reform bill passed by 1 vote.

14 Submitters on the original Charities Bill had been appeased by the promise of a post-implementation review of the Charities Act, scheduled for completion by 2015. However, in November 2012, only a few months after controversially disestablishing the Charities Commission, the Minister then cancelled the review, arguing, ironically, that the disestablishment of the Charities Commission had rendered a review "no longer appropriate". The Minister also stated that the definition of charitable purpose was "still working reasonably well" so the need for a review was not "pressing". Such reasoning is surprising: while the definition of charitable purpose is capable of working reasonably well, it cannot be said to be working reasonably well for the many hundreds of good charities that are being denied registration on the basis of controversially narrow interpretations.

15 The problem will be exacerbated if provisions requiring deregistered charities to pay tax on the value of their net assets are passed by Parliament (see proposed new ss CV 17 and HR 12 of the Income Tax Act 2007, as proposed to be inserted by the Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Bill, at the time of writing awaiting its second reading). For charities that voluntarily deregister, these provisions are proposed to apply retrospectively from 14 April this year.

16 In addition, the exemption which allowed non-profits to offer debt securities to the public without needing to comply with the usual trustee, prospectus, and investment statement requirements is now limited to registered charities only (see the Securities Act (Charity Debt Securities) Exemption Notice 2013, which replaced the previous Securities Act (Charitable and Religious Purposes) Exemption Notice 2003).

17 While not the case yet, there are concerns that eligibility for donee status, and the fringe benefit tax exemption for "charitable organisations", may come to be limited to registered charities only.

18 Increasingly, registered charitable status is the gateway to survival for a charity.

19 This makes it vital that the definition of charitable purpose is interpreted correctly, and that good charities with charitable purposes are able to gain registration. As part of that process, it is also vital that charities have an effective mechanism for holding their regulator to account. Whether the current approach to appeals under section 59 of the Charities Act is delivering such a mechanism, and delivering on the purpose of the Charities Act to "encourage and promote the effective use of charitable resources" (section 3(b)), are important questions that need to be asked (see Deregistered charities NZLJ April 2014 at 87).

20 In the writer's view, it is important that the charitable sector "push back", through collaboration and communication, particularly in this pre-election environment. ■

About the Author

Sue Barker is the director of Sue Barker Charities Law, a boutique law firm based in Wellington specialising in charities law and public tax law. In November 2013, the firm was voted New Zealand's boutique law firm of the year, and first runner-up for the Tax Law Firm of the Year Award, at the New Zealand Law Awards. Sue is also is co-author of the text, The Law and Practice of Charities in New Zealand, published by LexisNexis in May 2013. Sue can be contacted at susan.barker@charitieslaw.co or +64 (0) 21 790 953 or PO Box 3065, Wellington 6140.