

9 December 2008

Tax Law E-alert

Commissioner of Taxation –v– Word Investments Limited

The Word Investments decision is important due to the implications for Income Tax Exempt Charities. These are now known as “Tax Concession Charities”.

Facts

Wycliffe Bible Translators (International), a missionary organisation seeking to spread the Christian religion through literacy and translation work, set up Word Investments Ltd (“Word”) as a means of financial and fund-raising support to it. In 2002, Word invested in Bethel Funerals, with the profits derived distributed to two main ministry organisations, one of which was Wycliffe Bible Translators (International).

The ATO refused to endorse Word as an income tax exempt charity because it considered that Word was a commercial enterprise. The fact that Word gave its income to charitable institutions was irrelevant to the ATO. The ATO’s argument was that because Word’s profit generating activity went beyond what was incidental or ancillary to the exempt purposes, Word was deprived of its charitable character.

High Court ruling

On 3 December 2008, the High Court of Australia ruled in favour of Word and held that its profits from its business enterprises were exempt from tax. In doing so, the High Court upheld a Full Federal Court ruling that business activities did not disqualify a charity from income exemption status. The majority said that the principal issue in deciding whether an institution was charitable was its purposes and not just its income raising activities.

Issues discussed by the High Court

First issue: whether Word was prevented from being a “charitable institution” by reason of the fact that its objects were not confined to charitable purposes.

The majority found that Word’s company constitutional objectives were still charitable, being that of advancing religious charitable purposes. Both the intention at the time Word was formed and its activities since indicated that it was charitable. The Court noted that this test had to be applied and assessed for each income tax year.

Second issue: can an institution be charitable where it does not engage in charitable activities beyond making profits which are directed to charitable institutions which do engage in charitable activities?

The court endorsed the decision in *Inland Revenue Commissioners –v– Helen Slater Charitable Trust Ltd [1982]*. In that case, Mr Andrew Park QC for the successful taxpayer submitted that it would be “revolutionary, unworkable and unacceptable in practice” for money subject to charitable trusts not to be “applied for charitable purposes” unless actually expended in the field.

The majority specifically stated in the Word decision that the position in Australia would be likely to be similar.

Third issue: whether Word was prevented from being a “charitable institution” by reason of the fact that the institutions to which it gave its profits “were not confined as to the use to which they may put the funds distributed to them”.

The majority decided that the evidence did not support this conclusion. Just because the body to which Word gave its money, Wycliffe, was at liberty to select, this was not sufficient to imperil its income exempt status.

Fourth issue: did Word Investments have a physical presence in Australia and pursue its objectives in Australia?

Section 50-50(a) of the *Income Tax Assessment Act 1997 (Cth)* required Word to have both a physical presence in Australia and incur its expenditure and pursue its objectives in Australia. The argument by the ATO was that compliance with s 50-50(a) was necessary otherwise the ATO would face great difficulty in monitoring the use of funds where those funds are paid to organisations that pursued their objectives outside of Australia.

The majority concluded that Word was compliant with section 50-50 as it did have a physical presence in Australia and to that extent incurred its expenditure and pursued its objectives principally in Australia. The decisions by Word to pay were made in Australia, the payments were made in Australia, the payments were made to Australian organisations, and the objects of Word included giving financial assistance to those organisations.

Implications of the case

The decision is significant for the whole charitable sector including private Christian schools. It should eliminate concerns that Christian schools may have that fund raising activities if considered to be of a commercial nature would no longer be exempt from income tax.

The case also has implications for other bodies such as the Salvation Army running furniture businesses, the YMCA running swimming pools and fitness centres, Hillsong selling CDs and the Diabetes Foundation selling used clothing.

The case also calls for careful attention to be given to the “Objects” clause of a charitable institution’s constitution in that this clause should appropriately establish the institution’s charitable purpose.

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