



PS LA 2014/1 - Administration of penalties for failure to comply with Ancillary Fund Guidelines

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PS LA 2014/1

Administration of penalties for failure to comply with Ancillary Fund Guidelines

This Law Administration Practice Statement provides guidance on the penalties for failure to comply with Ancillary Fund Guidelines.

This practice statement is an internal ATO document, and is an instruction to ATO staff.

Taxpayers can rely on this practice statement to provide them with protection from interest and penalties in the following way. If a statement turns out to be incorrect and taxpayers underpay their tax as a result, they will not have to pay a penalty. Nor will they have to pay interest on the underpayment provided they reasonably relied on this practice statement in good faith. However, even if they don't have to pay a penalty or interest, taxpayers will have to pay the correct amount of tax provided the time limits under the law allow it.

1. What is this practice statement about?

The *Private Ancillary Fund Guidelines 2009* and the *Public Ancillary Fund Guidelines 2011* (Guidelines) provide the rules that ancillary funds and their trustees must comply with if the funds are to be, or are to remain, endorsed as Deductible Gift Recipients (DGR).

If a fund breaches the Guidelines, an administrative penalty may be payable by the trustee of the fund.

This practice statement provides guidance on the administration of these penalties, including their imposition and remission.¹

2. Administrative penalties – general rules

Section 426-120 of Schedule 1 to the *Taxation Administration Act 1953* (TAA) sets out the general rules for the imposition of the penalties.

The purpose of the penalty regime is to ensure that trustees are properly accountable and act in the manner expected of a trustee holding philanthropic funds for a broad public benefit.

The persons who will be liable for the penalty are:

- The trustee of the ancillary fund, and/or
- If the trustee is a constitutional corporation² from which the penalties cannot reasonably be recovered, the directors of that corporation.

Liability to the penalty is joint and several, meaning that any amount paid by one trustee or director will reduce the amount that the other trustees and/or directors are liable to pay by the same extent.

The liability cannot be reimbursed from the ancillary fund.

3. Administration of the penalties

The following are relevant when administering the penalties (including in any review process undertaken):

- The principles underpinning the compliance model, including being fair to those trustees wanting to do the right thing, and being firm but fair with those choosing to disengage and avoid their taxation obligations.
- The statements and principles in the Taxpayers' Charter. This means a trustee should be presumed to have been honest, unless there is information which suggests otherwise.
- Penalty decisions must be supported by the available facts and evidence. Conclusions about the trustee's actions or behaviour should only be made where they are supported by facts, or where reasonable inferences can be drawn from those facts.
- The trustee should normally be contacted and given the opportunity to explain their actions before making a penalty decision.

There are four basic steps which must be followed:

Step 1 – Determine if a penalty is imposed by law

Step 2 – Determine who to make liable for the penalty

Step 3 – Determine if all or a part of the penalty should be remitted.

Step 4 – Notify each trustee and/or each director of the corporate trustee of the liability to pay the penalty.

These steps are explained in sections 4 to 7 of this practice statement.

¹ For guidance on the transitional rules which were in place for the period when the Guidelines were introduced, refer to prior versions of this practice statement.

² Provided the constitutional corporation is not a licensed trustee company (under Chapter 5D of the *Corporations Act 2001*) nor the Public Trustee of a State or Territory.

4. Step 1 – Determine if a penalty is imposed by law

Once a breach of a guideline is established, the relevant Guidelines determine the amount of the penalty and this is tailored to the severity or consequence of the breach.

A list of guidelines in each Ancillary Fund Guideline and the corresponding penalty for the breach are contained in Appendix 1 and Appendix 2 of this practice statement.

5. Step 2 – Determine who to make liable to the penalty

Where an ancillary fund has a corporate trustee, you must determine whether, in addition to the corporate trustee, the directors of the corporate trustee are also liable to the administrative penalty.

We can seek to recover from any or all of the directors of the corporate trustee if it is clear that the penalty, or part of it, cannot be recovered from the corporate trustee alone.

In making this decision, you need to take into account

- any potential defences available to the directors (explained further below)
- the director's capacity to pay, and
- other relevant factors including the director's history with other entities.

If we have information regarding the financial position of the directors, we would usually take action against those directors from whom recovery would be expected to be achieved in the most timely way. However, if our knowledge of the directors is limited, it may be necessary to initiate action against all directors.

Potential defences available to the directors in relation to the breach

A statutory defence is available to directors³ in the following instances.

The director was not aware of the breach, and it would not have been reasonable to expect them to have been aware of the breach

As a general principle, it is expected that the directors should be aware of the decisions being made by the corporation, as governed by the *Corporations Act 2001*.

³ Paragraph 426-120(5).

This defence needs to be decided by applying an objective test – viewing the facts as they would be by a reasonable and prudent director of reasonable ability, who in the proper discharge of duties as a director had reasonable grounds for expecting the breach.

In the same circumstances, a director of the corporate trustee who is a 'responsible person' would also need to comply with the same degree of responsibility in the proper discharge of his or her duties. The meaning of the word 'expect'⁴ is to be understood according to its ordinary use, that is 'to regard as likely to happen' or 'to expect to find'.

Overall, the director must act in a manner consistent with a director of a constitutional corporation that is a trustee of a trust holding philanthropic funds for broad public benefit. The effort required is one commensurate with all the director's circumstances, including the director's knowledge, education, experience and skill.

The director took all reasonable steps to ensure that the breach did not occur

This means that the director acted with care and diligence in complying with the guidelines. In deciding what is 'reasonable' you need to have regard to all relevant circumstances, for example when and for how long the person was a director, what the director did in the context of his or her knowledge of the options available to the director, and the director's continuing efforts to achieve compliance with his statutory obligations.

There were no such steps that the director could have taken

The onus of proving that one of the defences applies to them is on the director, and a decision on whether they are able to meet the terms of that statutory defence will depend on the facts of each case.

The power of the court under section 1318 of the *Corporations Act 2001* to grant relief in case of breach of director's duty does not apply to a liability of a director for this administrative penalty.

6. Step 3 – Determine if all or a part of the penalty should be remitted

We have the unfettered discretion to remit all or part of the penalty imposed under section 426-120.⁵

The decision to exercise the discretion needs to be made separately for each trustee or director liable to an administrative penalty.

⁴ In paragraph 426-120(5)(a).

⁵ Under section 298-20 of Schedule 1 to the TAA.

The following points need to be considered when making your remission decision – noting that your decision may result in no remission, partial remission or full remission of the penalty. These are not exhaustive and are not intended to prescribe the only factors. They are intended to encourage an analytical approach to each case and the application of sound judgment in making the remission decision.

- As a starting point, the quantum of penalties prescribed is considered appropriate for the breaches of the Ancillary Fund Guidelines.
- You need to undertake an objective analysis of all the relevant factors in a case
- You must have regard to the purpose of the provision. Remember that:
 - a high level of care is expected of trustees of philanthropic funds – they are required to act with care, skill and diligence
 - a major objective of the penalty regime is to promote consistent treatment by specifying the amount of penalty for the breach of each guideline. That objective would be compromised if the amount of penalties specified in the law were remitted without just cause, arbitrarily or as a matter of course.
- You should consider if the trustee has acted as would reasonably be expected of a competent trustee in the same circumstances, and this needs to be based on an objective test. The fact that the trustee genuinely tried to act with care and diligence is not the test – what is relevant is whether, on an objective analysis, a trustee in the same position and circumstances would have acted in the same way as the trustee in question.
- Your decision needs to be fair and reasonable, and ensure that the prescribed amount of penalty does not cause unintended or unjust results, having regard to all the relevant acts or omissions leading to the breach of the Guidelines. For example, an unjust result may occur in situations where multiple administrative penalties from various breaches of the Guidelines could arise. If this is the case, you should consider whether the cumulative penalty applied is defensible, proper and just having regard to the overall circumstances of the case. Were they connected, and the penalties arise from a single course of conduct, or a single error? If so, it would be unjust to apply multiple penalties and the administrative penalty that applies should be the one that is the most specific to the situation.

- Guidelines 34 to 37 and 41 to 42 are integrity assurance measures to ensure appropriate practices and processes are in place to safeguard moneys donated to the ancillary fund, and that tax deductible donations are used for an appropriate approved purpose. Therefore, remission of the penalty in relation to breaches of these Guidelines would only occur in exceptional cases.

7. Step 4 – Notify each trustee and/or each director of the corporate trustee of the liability to pay the penalty

We must give a written notice to the trustee and/or director informing them of their liability to pay the penalty, and of the reason why they are liable to pay the penalty. If the penalty has not been remitted in full, we must also provide an explanation of why this has not occurred either before, or at the same time.

We must ensure the reasons are supplied prior to or at the same time as the trustee and/or director are given the written notice.

If there was a part payment made in respect of the administrative penalty, we also need to notify the remaining trustees and/or directors that their liabilities have been reduced to the extent of the payment.

A trustee or director who is dissatisfied with a decision to refuse to remit, in full or in part, an amount of penalty may object in the manner set out in Part IVC of the TAA if the amount of penalty remaining after the decision is more than two penalty units.

8. Examples

The following examples are indicative only. They also assume that the trustee of the ancillary fund is a constitutional corporation that is neither a licensed trustee company nor a Public Trustee of a State or Territory.

Example 1

Guideline 19 requires a private ancillary fund to distribute at least 5 per cent of the market value of the fund's net assets (as at the end of the previous financial year).

A private ancillary fund, prior to the start of a taxation audit, disclosed that it had failed to comply with Guideline 19 in its second year of operation.

The trustee had distributed 5 per cent of the fund's net assets, including a large distribution to a Children's Hospital Foundation in a major city. The trustee subsequently discovered that the Children's Hospital Foundation was a public ancillary fund, and was not eligible to receive a distribution from the private ancillary fund.

The trustee rectified the mistake immediately by making a matching distribution to an eligible deductible gift recipient. The trustee also arranged for training and education for those responsible for making grants on behalf of the private ancillary fund to ensure the same mistake would not reoccur.

In this instance, a full penalty remission is warranted. The trust was in its second year of operation, and the trustee's actions in this case were in accordance with what is reasonably expected of a competent trustee in the same circumstances. Once the discrepancy was discovered, the trustee took immediate steps to rectify the problem and ensure it would not happen again. The trustee also voluntarily disclosed this breach to the ATO auditor prior to the start of the audit.

Example 2

Guideline 24 requires the maintenance of proper accounts in respect of all receipts and payments of the fund and all financial dealings connected with the fund, and must retain those accounts for a period of at least five years.

The trustee did not maintain proper accounts for the public ancillary fund. For instance, the trustee did not always record the payments. Where receipts for a deductible contribution were issued, the trustee left out relevant details or issued receipts with incorrect details. The trustee admitted that several donors had queried the incomplete information in their receipts. The trustee promised to re-issue the receipts but had been continually engaged in big fund raising events, and had not found time to correct the errors and re-issue the receipts.

The trustee had greatly neglected the accounting and financial administration of the ancillary fund. It was not inadvertent book-keeping errors only.

It was also clear that the trustee was aware of the contravention, or should have been aware, and did not take steps to remedy the breach.

There was no specific reason for the trustee not to pay attention to its proper record keeping. A busy professional role would not justify the application of a lower standard of care in meeting obligations nor compromise the trustee's capacity to comply with Guideline 24. A reasonable trustee in the same circumstances would be expected to devote sufficient time to maintaining proper accounts of receipts and payments. No remission of penalty was warranted.

Example 3

For one financial year subject to a review, a trustee of a private ancillary fund was found not to have kept proper accounts in respect of all receipts and payments of the fund and all its financial dealings in contravention of Guideline 24. The fund's net assets were not sizeable.

A director of the corporate trustee advised he had a serious illness. He provided documentary evidence to show that he had two major surgeries in that financial year. The director's illness affected his ability to complete his duties. While recovering from both surgeries, the director depended on a part-time bookkeeper to manage the payments and receipts. The bookkeeper retained all documentation but did not use a proper accounting system to record transactions.

The director provided all the receipts and invoices for that financial year to an ATO auditor but the accounting of all the fund's dealings was not completed. During the audit, the director had to reconcile the records again to provide an accurate accounting of the fund for that financial year. Further evidence showed the director had properly administered the money in the fund (that is, consistent with its investment strategy and in accordance with other guidelines).

Under these circumstances, the ATO was satisfied that the statutory defence was available to the director. The following matters were relevant to support his defence:

The director's illness contributed to his failure to correctly record and manage the financial dealings of the private ancillary fund. Similarly, an appropriate conclusion is that a trustee in the same circumstances might not be as thorough or as organised in keeping records as a trustee who was not dealing with major health issues.

Given his ill health and the size of the fund, it is also reasonable for the trustee to rely on a part-time book-keeper. Therefore, it was reasonable to form the view that the director took all reasonable steps to ensure that the breach did not occur.

The same statutory defence would not apply to the other directors of the corporate trustee. The other directors may still be liable for the penalty and consideration of the facts should be conducted for each director's case.

Example 4

Guideline 27 requires ancillary funds to make financial statements available to the ATO upon request.

The ATO requested various details from an ancillary fund, including its last financial statement. The ancillary fund was large, and the funds at risk sizeable.

The fund did not supply the requested financial statement. No responses were forthcoming after three requests.

A decision was made not to remit the penalty imposed for breach of Guideline 27, as the notices had not been complied with and there was no evidence to suggest the trustee was unable to provide the information requested. It is reasonable to expect that a competent trustee in the same circumstances would have made those financial statements available.

A penalty for not preparing the financial statement under Guideline 26 could also apply. If the evidence supported this conclusion, then the trustee would be liable for both penalties under Guideline 27 and 26.

Consideration should be given to whether maintaining both penalties would produce an unjust result. In this case, the penalties relating to the two breaches of Ancillary Fund Guidelines are from two separate actions (that is, failure to prepare a financial statement, and failure to comply with the ATO request). Therefore, there is no unjust result justifying any remission.

Example 5

Following on from example 4 of this practice statement, it was clear from the facts that the corporate trustee had no available funds. The ATO personnel, therefore, should seek to recover the penalty from the directors of the corporate trustee who are jointly and severally liable for the penalty.

The facts showed the three directors of the corporate trustee had different roles and responsibilities: one director concentrated on organising fund-raising activities and dealing with charitable institutions; the other two directors were responsible for the financial management.

Six months before the fund review, the fund-raising director became concerned that the two other directors were not performing their duties proficiently. The fund-raising director reviewed the accounting records and engaged an external professional accountant to help. However, the two other directors were unco-operative and did not provide the relevant information to allow the accountant to review the records.

When considering whether to commence action against some or all of the directors, the ATO personnel should take into account the potential defences available to the directors, the directors' capacity to pay and other relevant factors.

In this case, it was reasonable to form the view that the fund-raising director took all reasonable steps. To the extent that he did not take steps, there were no more effective steps available to him. He was faced with non-co-operative co-directors. This strongly suggested that the statutory defence was available to the fund-raising director.

The ATO considered it appropriate to commence actions against the two other directors only.

Example 6

Guideline 40 states the fund must not carry on a business.

A private ancillary fund was originally established for philanthropic purposes. It held a small number of shares and rental properties for the purpose of deriving income to be distributed to deductible gift recipients. This was not considered to be carrying on a business at that time.

However, a couple of years after formation, the fund achieved good results from its investments and started to undertake more substantial investigation and investment activities to take advantage of the potential. The activities undertaken were planned, organised and carried out in a similar manner to those of other investment companies.

For instance, it did not only manage rental properties to maximise returns, it also engaged in property development. The activities were of reasonable size and scale. The fund engaged consultants and employed staff to manage its investment function.

After considering all the factors, it was determined that Guideline 40 was breached and a penalty of 25% of the net profits for each financial year was imposed. Although the fund was not set up to breach Guideline 40 intentionally, given the sizeable activities and the change in the nature of trade, it was concluded that the fund was no longer merely holding investments – it had started a business.

There were no grounds for remission of the penalty, as the trustees did not act with care regarding Guideline 40. It was considered that in the same circumstances, other trustees could be expected to have known that the activities undertaken by the fund constituted the carrying on of a business. The fund was in breach of Guideline 40.

Example 7

A private ancillary fund provided interest-free loans to family members of the founder and paid an excessive salary to the founder incommensurate to the minimal activities undertaken by him on behalf of the fund. The trustee had also failed to make any payments in pursuit of its charitable purposes, and advised it did not have immediate plans to do so.

There was evidence the fund had been set up to provide material tax and other benefits to the founder, and was not being maintained solely for charitable purposes.

The fund had been in existence for some years. It had access to advice and had sizeable funds. Given the sophistication of technical resources available to the fund, it was clear the trustee was or should have been aware of the contraventions but chose to deliberately disregard its obligations.

Under these circumstances, the trustee was potentially liable for penalties relating to breaches of: Guideline 36 (loans and financial assistance); Guideline 41 (uncommercial transactions); and Guideline 42 (benefits to founder/donor). After further investigation, the trustee was also considered likely to have contravened: Guideline 19 (not meeting minimum annual distributions); Guideline 28 (not auditing the financial statements of the fund); Guideline 31 (failure to implement and follow the investment strategy); and Guideline 32 (investment strategy and decision-making processes not in writing).

The ATO personnel followed the four main steps in sections 4 to 7 when assessing the administrative penalties for the trustee. The following factors were relevant in establishing the breaches of the Ancillary Fund Guidelines:

- a high level of care is expected of a trustee of a philanthropic fund. There was no evidence showing the trustee made any attempt to comply with the obligations imposed by the guidelines. It is a reasonable conclusion that a trustee in the same circumstances was expected to have known it should not have provided these loans and financial assistance.
- the related parties (that is, founder and its family members) gained a real benefit from the breaches of these guidelines. The evidence supported the conclusion that the trustee intended to provide a benefit to those parties, and chose to deliberately disregard its obligations.
- the trustee's actions were contrary to a philanthropic fund's intent, which is providing for a broad public benefit.

Each of these are serious breaches and all relevant administrative penalties would be imposed without remission in respect of each breach. The Commissioner would also consider the suspension of the trustee under section 426-125. ATO personnel should also consider whether a referral to the State Attorney General for action under State Trust law is appropriate.

Example 8

Following on from Example 7 of this practice statement, the ATO also sought to initiate action against all three directors of the corporate trustee. The ATO's knowledge about the directors was limited (for example, information regarding the financial position of the directors), however, the evidence showed the corporate trustee had limited funds.

One director raised a defence after he was issued a notice to pay. He argued he was unaware of the breach, and it would not have been reasonable to expect him to have been aware of the breach.

The director presented evidence that the two co-directors acted fraudulently and kept their actions from him. He was a newly appointed director. He was not a director when the co-directors made the pertinent decisions which resulted in the breaches. Furthermore, the co-directors made false representations and provided bogus financial statements to him. The director reviewed the financial statements and relied on them to be true and accurate.

The facts pointed towards the director taking a proper responsible role in the management of the fund. It was found that the director had not been negligent, or failed to make inquiries, or otherwise participate in the decision-making processes of the fund, because he was not a director at the time and he later relied on the information provided by the co-directors. The director had no access to legitimate financial information, which could have otherwise led him to make further inquiry or seek clarification of the fund's activities.

The ATO accepted the director's defence. Based on the available facts of this case, the director was not aware of the breaches and it is not reasonable to expect a prudent director of reasonable ability to have been aware of these breaches. The penalty was not therefore imposed on this director.

Example 9

A private ancillary fund was established without a written investment strategy because the trustees thought it was obvious that the fund should have its assets in cash in the first year. The founder had an investment strategy in the first year of term deposits in Australian financial institutions.

The following year, the trustees produced a written investment strategy that the composition of the fund's investment as a whole could only be blue-chip shares in Australian companies and term deposits in Australian financial institutions.

However, at the urging of the founder, the trustees purchased speculative shares in a little known company overseas. But there was no change in the fund's written investment strategy. The trustee failed to document any associated decision-making processes used in acquiring the international shares.

Under these circumstances, the trustee was potentially liable for penalties relating to breaches of: Guideline 31 (Implement the investment strategy) and Guideline 32 (Written form).

It was determined the trustee was liable for the penalties relating to breaches of Guideline 32 in the first year of operation and Guideline 31 in the subsequent year. The breaches arose from separate courses of conduct.

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Appendix 1: Private Ancillary Fund Guidelines and Penalty Units

Private Ancillary Fund Guidelines	Description	Penalty Units
Guideline 17 Changes to governing rules	<p>17. The trustee must notify the Commissioner in the *approved form (within 21 days) of any change to the fund's governing rules.</p> <p><i>Note: Certain changes to the governing rules may require the fund to seek re-endorsement as a deductible gift recipient</i></p>	5 penalty units
Guideline 19 Minimum annual distribution	<p>19. During each *financial year, a *private ancillary fund must distribute at least 5 per cent of the *market value of the fund's net assets (as at the end of the previous *financial year).</p> <p><i>Note: While net assets are used to determine the fund's minimum distribution, the amount of the distribution itself is not net of any amount (for example, expenses of the fund).</i></p> <p>19.1 The fund must distribute at least \$11,000 (or the remainder of the fund if that is worth less than \$11,000) during that *financial year if:</p> <ul style="list-style-type: none"> the 5 per cent is less than \$11,000; and any of the expenses of the fund in relation to that financial year are paid directly or indirectly from the fund's assets or income. <p><i>Note: This means that if a fund's expenses are met from outside the fund, its minimum annual distribution is 5 per cent of the market value of the fund's net assets. If a fund's expenses are paid out of the fund's assets or income, its minimum distribution is \$11,000 or 5 per cent, whichever is greater.</i></p> <p>19.2 No distribution is required during the *financial year in which the fund is established.</p> <p>19.3 A distribution includes the provision of money, property or benefits. If the fund provides property or benefits, the *market value of the property or benefit provided is to be used in determining whether the fund has complied with this guideline.</p> <p><i>Example 1: If a private ancillary fund makes a gift of land to a public benevolent institution, it would include the market value of the land in calculating how much it has distributed.</i></p> <p><i>Example 2: If a private ancillary fund leases office space to a deductible gift recipient at a discount to the market price, the fund is providing a benefit whose market value is equal to the discount.</i></p> <p>19.4 The penalty for a contravention of this guideline is 30 penalty units if the shortfall is greater than \$1,000.</p>	<p>30 penalty units if the shortfall is greater than \$1,000</p>
	<p>19.5 If the Commissioner requests the trustee to rectify a shortfall in the distribution for a *financial year, the trustee must comply with the request within 60 days. If the trustee does not, the penalty is 10 per cent of the shortfall as at the end of the 60 days reduced by any penalty (but not below nil) under guideline 19.4.</p> <p>19.6 A distribution made to rectify a contravention of this guideline does not count towards compliance with this guideline for the year of the rectification.</p>	10% of shortfall reduced by penalty under Guideline 19.4
Guideline 24 Accounts	<p>24. The trustee must keep, or cause to be kept, proper accounts in respect of all receipts and payments of the fund and all financial dealings connected with the fund, and must retain those accounts for a period of at least 5 years after the completion of the transactions or acts to which they relate.</p> <p><i>Note: See also Subdivision 382-B in Schedule 1 to the Taxation Administration Act 1953 for rules about record keeping obligations of deductible gift recipients.</i></p>	10 penalty units

Private Ancillary Fund Guidelines	Description	Penalty Units
Guideline 25	25. The trustee must make the accounts available to the Commissioner upon request.	10 penalty units
Guideline 26 Financial statements	<p>26. The trustee must prepare, or cause to be prepared, financial statements showing the financial position of the fund at the end of each *financial year.</p> <p>26.1 The financial statements must be prepared in accordance with the *accounting standards.</p> <p>26.2 All transactions between the fund and a founder of the fund, a donor to the fund, the trustee, a director, officer, *agent, *member or employee of the trustee, or an *associate of any of these entities must be disclosed in the financial statements.</p> <p>26.3 The financial statements must be prepared before the fund is required to give to the Commissioner its *income tax return for the relevant *financial year.</p>	10 penalty units
Guideline 27 Request for financial statements	27. The trustee must make the financial statements available to the Commissioner upon request.	10 penalty units
Guideline 28 Audit	<p>28. Each *financial year the trustee must arrange for an auditor to audit:</p> <ul style="list-style-type: none"> the financial statements of the fund; and compliance with these Guidelines by the fund and the trustee. <p>28.1 The auditor must be registered under Part 9.2 of the <i>Corporations Act 2001</i>.</p> <p>28.2 The auditor must provide the fund with an audit report in accordance with the *auditing standards.</p> <p>28.3 The audit must be finalised before the fund is required to give to the Commissioner its *income tax return for the relevant *financial year.</p>	10 penalty units
Guideline 29 Request for audit report	29. The trustee must make the audit report available to the Commissioner upon request.	10 penalty units
Guideline 30 Investment strategy	<p>30. The trustee must prepare and maintain a current investment strategy for the fund.</p> <p>30.1 An appropriate investment strategy should set out the investment objectives of the fund and detail the investment methods the trustee will adopt to achieve those objectives.</p> <p>30.2 The strategy must reflect the purpose and circumstances of the fund and have particular regard to (but not be limited to):</p> <ul style="list-style-type: none"> the risk involved in making, holding and realising, and the likely return from, the fund's investments, having regard to the fund's objectives and its expected cash flow requirements (including distribution requirements); and the composition of the fund's investments as a whole, including the extent to which the investments are diverse or involve the fund being exposed to risks from inadequate diversification; and the liquidity of the fund's investments, having regard to its expected cash flow requirements (including distribution requirements); and 	10 penalty units

Private Ancillary Fund Guidelines	Description	Penalty Units
	<ul style="list-style-type: none"> the ability of the fund to discharge its existing and prospective liabilities; and the investment requirements imposed by *State laws or *Territory laws. 	
Guideline 31 Implement the investment strategy	31. The trustee must implement the investment strategy, and must ensure that all investment decisions are made in accordance with it.	10 penalty units
Guideline 32 Written form	32. The investment strategy (and a record of the associated decision-making processes) must be available in a written form so that the trustee, an auditor or the Commissioner can determine whether the fund has complied with these Guidelines and other *Australian laws.	10 penalty units
Guideline 33 Investment limitations – borrowings	<p>33. The trustee must not *borrow money or maintain an existing borrowing of money.</p> <p>33.1 However, this guideline does not prohibit a trustee from *borrowing money if:</p> <ul style="list-style-type: none"> the purpose of the borrowing is to enable the trustee to make a distribution to a *deductible gift recipient, which the trustee must make under these guidelines and which, apart from the borrowing, the trustee would be unable to make; and the period of the borrowing does not exceed 90 days; and the borrowing, when made, would not result in total borrowings exceeding 10 per cent of the *market value of the fund's assets. <p>33.2 This guideline also does not prohibit a trustee from *borrowing money if:</p> <ul style="list-style-type: none"> the purpose of the borrowing is to enable the trustee to cover settlement of a transaction for the acquisition of a financial instrument; and at the time the relevant investment decision was made, it was likely that the borrowing would not be needed; and the period of the borrowing does not exceed 14 days; and the borrowing, when made, would not result in total borrowings exceeding 10 per cent of the *market value of the fund's assets. <p>33.3 Guideline 33 also does not apply to the acquisition of a financial instrument excluded by the Commissioner from that guideline.</p>	30 penalty units
Guideline 34 Investment limitations – arms length	34. The fund's investments must be made and maintained on an *arm's length basis.	30 penalty units
Guideline 35 Investment limitations – assets not to be offered as security	<p>35. The trustee must not give a security over, or in relation to, an asset of the fund.</p> <p>35.1 However, this guideline does not apply to the acquisition of a financial instrument excluded by the Commissioner from that guideline.</p>	30 penalty units

Private Ancillary Fund Guidelines	Description	Penalty Units
Guideline 36 Investment limitations – assets acquired at arms length	<p>36. The fund must not acquire an asset (except by way of gift) from, and must not make a loan or provide any other kind of financial assistance to, a founder of the fund, a donor to the fund, the trustee, a director, officer, agent, *member or employee of the trustee, or an *associate of any of these entities except:</p> <ul style="list-style-type: none"> • by way of an arms' length commercial transaction; or • on terms more favourable to the fund than would otherwise be expected under an arms' length transaction. 	30 penalty units
Guideline 37 Investment limitations – assets kept separate	37. The trustee must keep the assets of the fund separate from all other assets.	30 penalty units
Guideline 38 Investment limitations – Collectables	<p>38. The fund must not acquire an asset (except by way of gift) if the asset is capable of being a *collectable.</p> <p>38.1 If the fund acquires such an asset by way of gift, it must sell or distribute the asset within 12 months after acquiring it.</p>	30 penalty units
Guideline 40 Investment limitations – carrying on a business	<p>40. The fund must not *carry on a *business.</p> <p><i>Note: The holding of investments, such as shares or rental properties, for the purpose of deriving income that can be distributed to deductible gift recipients is not considered to be carrying on a business.</i></p> <p>40.1 The penalty for a contravention of this guideline is an amount equal to 25 per cent of the net profits of the business for each *financial year during all or part of which the contravention continues.</p>	25% of the net profits of the business
Guideline 41 Uncommercial transactions	<p>41. The fund must not enter into any transaction that is uncommercial when entered into, unless the transaction is:</p> <ul style="list-style-type: none"> • with a *deductible gift recipient covered by item 1 in the table in section 30-15 of the ITAA 1997; and • in the course or furtherance of the fund's purpose. <p>41.1 However, the fund may enter into an uncommercial transaction if it is on terms more favourable to the fund than would otherwise be expected under an arms' length transaction.</p>	30 penalty units
Guideline 42 Benefits to founder/donor or associates	<p>42. The fund must not *provide any benefit (except as set out in guideline 43), directly or indirectly, to:</p> <ul style="list-style-type: none"> • the trustee; or • a *member, director, employee, *agent or officer of the trustee; or • a donor to the fund; or • a founder of the fund; or • an *associate of any of those entities. 	Penalty amount equal to the amount or value of the benefit provided
Guideline 45 Donors – public appeals	45. The fund must not solicit donations from the public.	30 penalty units

Private Ancillary Fund Guidelines	Description	Penalty Units
Guideline 46 Donors – sources of donations	<p>46. In any *financial year, the fund must not accept donations totalling more than 20 per cent (in total) of the *market value of its assets (determined at the end of the previous financial year) from entities other than:</p> <ul style="list-style-type: none"> • a founder of the fund; or • *associates of the founder; or • employees of the founder; or • a deceased estate of any of those entities. 	10 penalty units

Appendix 2: Public Ancillary Fund Guidelines and Penalty Units

Public Ancillary Fund Guidelines	Description	Penalty Units
Guideline 17 Changes to governing rules	<p>17. The trustee must notify the Commissioner in the *approved form (within 21 days) of any change to the fund's governing rules.</p> <p><i>Note: Certain changes to the governing rules may require the fund to seek re-endorsement as a deductible gift recipient.</i></p>	5 penalty units
Guideline 19 Minimum annual distribution	<p>19. During each *financial year, a *public ancillary fund must distribute at least 4 per cent of the *market value of the fund's net assets (as at the end of the previous *financial year).</p> <p><i>Note: While net assets are used to determine the fund's minimum distribution, the amount of the distribution itself is not net of any amount (for example, expenses of the fund).</i></p> <p>19.1 The fund must distribute at least \$8,800 (or the remainder of the fund if that is worth less than \$8,800) during that *financial year if:</p> <ul style="list-style-type: none"> the 4 per cent is less than \$8,800; and any of the expenses of the fund in relation to that financial year are paid directly or indirectly from the fund's assets or income. <p><i>Note: This means that if a fund's expenses are met from outside the fund, its minimum annual distribution is 4 per cent of the market value of the fund's net assets. If a fund's expenses are paid out of the fund's assets or income, its minimum distribution is \$8,800 or 4 per cent, whichever is greater.</i></p> <p>19.2 No distribution is required during the *financial year in which the fund is established or during the next 4 financial years.</p> <p><i>Note: While these guidelines do not set a minimum annual distribution for the first four financial years, the trustee should consider making an appropriate distribution each year in accordance with the purpose of the fund.</i></p> <p>19.3 A distribution includes the provision of money, property or benefits. If the fund provides property or benefits, the *market value of the property or benefit provided is to be used in determining whether the fund has complied with this guideline.</p> <p><i>Example 1: If a public ancillary fund makes a gift of land to a public benevolent institution, it would include the market value of the land in calculating how much it has distributed.</i></p> <p><i>Example 2: If a public ancillary fund leases office space to a deductible gift recipient at a discount to the market price, the fund is providing a benefit whose market value is equal to the discount.</i></p> <p><i>Example 3: If a public ancillary fund invests in a social impact bond issued by a deductible gift recipient with a return that is less than the market rate of return on a similar corporate bond issue, the fund is providing a benefit whose market value is equal to the interest saved by the deductible gift recipient from issuing the bond at a discounted rate of return.</i></p> <p>19.4 The penalty for a contravention of this guideline is 30 penalty units if the shortfall is greater than \$1,000.</p>	30 penalty units if the shortfall is greater than \$1,000
Guideline 19 Failure to comply with a request under Guideline 19	<p>19.5 If the Commissioner requests the trustee to rectify a shortfall in the distribution for a *financial year, the trustee must comply with the request within 60 days. If the trustee does not, the penalty is 10 per cent of the shortfall as at the end of the 60 days reduced by any penalty (but not below nil) under guideline 19.4.</p> <p>19.6 A distribution made to rectify a contravention of this guideline does not count towards compliance with this guideline for the year of the rectification.</p>	10% of shortfall reduced by penalty under Guideline 19.4

Public Ancillary Fund Guidelines	Description	Penalty Units
Guideline 24 Accounts	<p>24. The trustee must keep, or cause to be kept, proper accounts in respect of all receipts and payments of the fund and all financial dealings connected with the fund, and must retain those accounts for a period of at least 5 years after the completion of the transactions or acts to which they relate.</p> <p><i>Note: See also Subdivision 382-B in Schedule 1 to the Taxation Administration Act 1953 for rules about record-keeping obligations of deductible gift recipients.</i></p>	10 penalty units
Guideline 25 Request for accounts	25 The trustee must make the accounts available to the Commissioner upon request.	10 penalty units
Guideline 26 Financial statements	<p>26. The trustee must prepare, or cause to be prepared, financial statements showing the financial position of the fund at the end of each *financial year.</p> <p>26.1 The financial statements must be prepared in accordance with the *accounting standards.</p> <p>26.2 All transactions (except for gifts) between the fund and a founder of the fund, a donor to the fund, the trustee, a director, officer, *agent, *member or employee of the trustee, or an *associate of any of these entities must be disclosed in the financial statements.</p> <p>26.3 The financial statements must be prepared before the fund is required to give to the Commissioner its *income tax return for the relevant *financial year.</p>	10 penalty units
Guideline 27 Request for financial statements	27. The trustee must make the financial statements available to the Commissioner upon request.	10 penalty units
Guideline 28 Audit	<p>28. Except as set out below, each *financial year the trustee must arrange for an auditor to audit:</p> <ul style="list-style-type: none"> the financial statements of the fund; and compliance with these Guidelines by the fund and the trustee. <p>28.1 The auditor must be a registered company auditor (within the meaning of the <i>Corporations Act 2001</i>).</p> <p>28.1.1 The Public Trustee of a state or territory may have the Auditor-General of that state or territory undertake the audit.</p> <p>28.2 Unless the Commissioner, by written notice, provides otherwise, a public ancillary fund with revenue and assets of less than \$1 million in relation to a particular financial year, may instead have its financial statements and compliance with these guidelines reviewed rather than audited.</p> <p>28.2.1 A reviewer must be a registered company auditor (within the meaning of the <i>Corporations Act 2001</i>). However, an individual who is taken to be a registered company auditor under section 324BE of the <i>Corporations Act 2001</i> is taken to be a registered company auditor for the purpose of this guideline.</p> <p><i>Note: This has the effect of widening the class of individuals who can undertake a review.</i></p> <p>28.3 The auditor or reviewer must undertake the review or audit, and provide the fund with a report, in accordance with the *auditing standards.</p>	10 penalty units

Public Ancillary Fund Guidelines	Description	Penalty Units
	28.4 The audit or review must be finalised before the fund is required to give to the Commissioner its *income tax return for the relevant *financial year.	
Guideline 29 Request for audit report	29. The trustee must make the report available to the Commissioner upon request.	10 penalty units
Guideline 30 Investment strategy	<p>30. The trustee must prepare and maintain a current investment strategy for the fund.</p> <p>30.1 An appropriate investment strategy should set out the investment objectives of the fund and detail the investment methods the trustee will adopt to achieve those objectives.</p> <p>30.2 The strategy must reflect the purpose and circumstances of the fund and have particular regard to (but not be limited to):</p> <ul style="list-style-type: none"> • the risk involved in making, holding and realising, and the likely return from, the fund's investments, having regard to the fund's objectives and its expected cash flow requirements (including distribution requirements); and • the composition of the fund's investments as a whole, including the extent to which the investments are diverse or involve the fund being exposed to risks from inadequate diversification; and • the liquidity of the fund's investments, having regard to its expected cash flow requirements (including distribution requirements); and • the ability of the fund to discharge its existing and prospective liabilities; and • the investment requirements imposed by *State laws or *Territory laws. 	10 penalty units
Guideline 31 Implement investment strategy	31. The trustee must implement the investment strategy, and must ensure that all investment decisions are made in accordance with it.	10 penalty units
Guideline 32 Written form	32. The investment strategy (and a record of the associated decision-making processes) must be available in a written form so that the trustee, an auditor or the Commissioner can determine whether the fund has complied with these Guidelines and other *Australian laws.	10 penalty units
Guideline 33 Investment limitations – Borrowings	<p>33. The trustee must not *borrow money or maintain an existing borrowing of money.</p> <p>33.1 However, this guideline does not prohibit a trustee from *borrowing money if:</p> <ul style="list-style-type: none"> • the purpose of the borrowing is to enable the trustee to make a distribution to a *deductible gift recipient, which the trustee must make under these guidelines and which, apart from the borrowing, the trustee would be unable to make; and • the period of the borrowing does not exceed 90 days; and • the borrowing, when made, would not result in total borrowings exceeding 10 per cent of the *market value of the fund's assets. 	30 penalty units

Public Ancillary Fund Guidelines	Description	Penalty Units
	<p>33.2 This guideline also does not prohibit a trustee from *borrowing money if:</p> <ul style="list-style-type: none"> the purpose of the borrowing is to enable the trustee to cover settlement of a transaction for the acquisition of a financial instrument; and at the time the relevant investment decision was made, it was likely that the borrowing would not be needed; and the period of the borrowing does not exceed 14 days; and the borrowing, when made, would not result in total borrowings exceeding 10 per cent of the *market value of the fund's assets. <p>33.3 Guideline 33 also does not apply to the acquisition of a financial instrument excluded by the Commissioner from that guideline.</p>	
Guideline 34 Investment limitations – arms length	34. The fund's investments must be made and maintained on an *arm's length basis.	30 penalty units
Guideline 35 Investment limitations – security over funds assets	<p>35. The trustee must not give a security over, or in relation to, an asset of the fund.</p> <p>35.1 However, this guideline does not apply to the acquisition of a financial instrument excluded by the Commissioner from that guideline.</p>	30 penalty units
Guideline 36 Investment limitations – assets acquired at arms length	<p>36. The fund must not acquire an asset (except by way of gift) from, and must not make a loan or provide any other kind of financial assistance to, a founder of the fund, a donor to the fund, the trustee, a director, officer, agent, *member or employee of the trustee, or an *associate of any of these entities except:</p> <ul style="list-style-type: none"> by way of an arm's length commercial transaction; on terms more favourable to the fund than would otherwise be expected under an arm's length transaction. 	30 penalty units
Guideline 37 Investment limitations – assets kept separate	<p>37. The trustee must keep the assets of the fund separate from all other assets.</p> <p>37.1 However, this guideline does not prevent a licensed trustee company or the Public Trustee of a state or territory from operating common funds for investment purposes.</p>	30 penalty units
Guideline 38 Investment limitations – collectable	<p>38. The fund must not acquire an asset (except by way of gift) if the asset is capable of being a *collectable.</p> <p>38.1 If the fund acquires such an asset by way of gift, it must sell or distribute the asset within 12 months after acquiring it.</p>	30 penalty units
Guideline 40 Investment limitations – not carrying on a business	<p>40. The fund must not *carry on a *business.</p> <p>40.1 However, a fund does not contravene this guideline merely because its investment activities, because of repetition, volume and regularity, mean that it is *carrying on a *business.</p> <p>40.2 A fund also does not contravene this guideline if it undertakes public fundraising appeals.</p> <p><i>Note 1: The holding of investments, such as bonds, shares or rental properties, for the purpose of deriving income that can be distributed to deductible gift recipients is not subject to the carrying on a business restrictions.</i></p>	25% of the net profits of the business for each *financial year during all or part of which the contravention continues.

Public Ancillary Fund Guidelines	Description	Penalty Units
	<p><i>Note 2: Fundraising appeals, such as public donation appeals, lamington drives, raffles, and charity balls, are not subject to the carrying on a business restrictions.</i></p> <p>40.3 The penalty for a contravention of this guideline is an amount equal to 25 per cent of the net profits of the business for each *financial year during all or part of which the contravention continues.</p>	
<p>Guideline 41 Uncommercial transactions</p>	<p>41 The fund must not enter into any transaction that is uncommercial when entered into, unless the transaction is:</p> <ul style="list-style-type: none"> • with a *deductible gift recipient covered by item 1 in the table in section 30-15 of the ITAA 1997; and • in the course or furtherance of the fund's purpose. <p>41.1 However, the fund may enter into an uncommercial transaction if it is on terms more favourable to the fund than would otherwise be expected under an arm's length transaction.</p>	<p>30 penalty units</p>
<p>Guideline 42 Material benefits</p>	<p>42 The fund must not *provide any material benefit (except as set out in guideline 43) directly or indirectly, to:</p> <ul style="list-style-type: none"> • the trustee; or • a *member, director, employee, *agent or officer of the trustee; or • a donor to the fund; or • a founder of the fund; or • an *associate of any of those entities (other than a *deductible gift recipient). 	<p>Penalty amount equal to the amount or value of the benefit provided</p>
<p>Guideline 43 Fees and Expenses</p>	<p>The trustee may apply income or capital of a *public ancillary fund:</p> <ul style="list-style-type: none"> • to reimburse the trustee for reasonable expenses incurred on behalf of the fund; and • to pay fair and reasonable remuneration for the trustee's services in administering the fund. <p><i>Note: A trustee incurs reasonable expenses on behalf of a fund when providing reasonable remuneration benefits to some if the individuals listed in guideline 42 (including providing benefits of a minor or incidental nature to an employee).</i></p>	