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Private Ancillary Funds A guide



Private Ancillary Funds

A private ancillary fund (PAF) enables an individual, family or organisation to put aside a chunk of money in a trust to support charities over the long term. It is an efficient, satisfying and tax effective way to put a structure around your philanthropy.

By setting up a PAF, you can:

- Make a tax deductible donation now and decide which charities to support later.
- Invest your charitable funds over the long-term.
- Provide an enduring revenue stream to charities.
- Involve family members, children, grandchildren and generations to come.
- Create a legacy.

Australian Philanthropic Services (APS) is a not-for-profit organisation that ensures that setting up and running a PAF is a simple, hassle-free and rewarding experience. The APS administration service is a one-stop-shop for PAFs, including all accounting, secretariat, compliance and reporting requirements.

This brochure outlines the key features and advantages of a PAF and explains how APS can help.

Key features of a PAF

Feature	Private Ancillary Fund (PAF) Setting up your own PAF with APS
Establishment	
How long does it take to get started?	6-8 weeks
Donations	
How much do I need to get started?	\$1 million is recommended
How often do I have to contribute to my fund?	As often or as infrequently as you like. There is no requirement to contribute on a regular basis
Can I get a tax deduction?	Yes – can be spread over 5 years
Can the general public contribute to my fund?	Restricted
Control	
Who is the trustee?	You can choose. APS will arrange a special purpose company, for whom you nominate directors, to act as trustee
Who are the directors of the trustee?	You can choose. Directors will generally be family members and/or business associates and one independent person (the 'Responsible Person')
Can I have a say in grantmaking decisions?	Yes. The directors of the trustee company have the final say
Grantmaking	
Who can receive grants?	Charities with Deductible Gift Recipient (DGR) Item 1 status
How much has to be distributed each year?	At least 5% of net assets
Investments	
Who manages the investments?	You choose the wealth manager or can manage investments yourself. APS does not manage investments in your PAF
Are the investments tax-exempt?	Yes
Are franking credits refunded?	Yes
Administration & compliance	
Who is responsible for compliance with the Law and PAF Guidelines?	The Directors of the trustee company (with guidance and support from APS)
What does the APS Administration Service include?	All accounting, administration, governance and compliance functions, and grantmaking support
What are the costs?	As a not-for-profit organisation, APS charges modest fees to establish and administer PAFs
Is an audit required?	Yes - APS will facilitate

What is a private ancillary fund?

A private ancillary fund (PAF) is a type of charitable trust, which exists for the purpose of providing grants to eligible charities over time.

Key features of a PAF:

- A PAF is a charitable trust controlled by a company as trustee. The board is usually comprised of family members but must contain at least one independent director (the 'Responsible Person').
- Donors receive a tax deduction for donations, which can be spread over five years.
- The investment strategy is set by the directors. Earnings are income tax exempt with franking credits reclaimable and testamentary gifts have Capital Gains Tax (CGT) exemption.
- Distributions are made to charities with Deductible Gift Recipient (DGR) status, and a minimum of 5% of the value of the fund must be distributed each year.
- PAFs are governed by Australian Taxation Office (ATO) Guidelines and have Australian Charities and Not-for-profits Commission (ACNC) compliance obligations.

Is a PAF right for me?

A PAF may be appropriate for individuals, families and companies that:

- Want control of all investment and grantmaking decisions
- Would like to provide a sustainable gift to a chosen cause(s)
- Have a recommended minimum of \$1 million for an initial donation
- Would like a tax deduction for donations.



The benefits of having a PAF

- **Satisfaction and enjoyment** - By establishing something in your lifetime, you can see the benefits of giving first-hand and, if you choose, be directly involved with the causes you support.
- **Family engagement** - Giving through a PAF is a satisfying way to engage and bring together other family members. It can increase children's and grandchildren's social awareness and help to inspire future generations.
- **Tax effectiveness** - A PAF enables you to take advantage of tax benefits while having a positive impact on the lives of others. Donations are tax deductible, the funds in the PAF are tax exempt and franking credits are refunded, so your philanthropic dollar goes much further.
- **Control** - You can act as a director of the trustee company that controls the PAF, directing all investment and grantmaking decisions.
- **Flexibility** - PAFs break the link between the timing of the tax deduction and the timing of your grantmaking decisions. You can take the tax deduction now and decide where to distribute the money over the coming years.
- **Sustainable funding** - Establishing a trust in perpetuity allows you to provide charitable causes with long term sustainable funding even when financial situations change.
- **Community impact** - Having a PAF allows you to be more considered in your grantmaking. You can plan for multi-year grants and redirect support as community needs change.
- **Leaving a legacy** - By setting up a PAF, you can create an enduring legacy to support charitable causes that are important to you, or establish a PAF in memory of a loved one.

Donations

How much do I need to start?

The recommended minimum donation for a PAF is \$1 million.

Tax deductibility

Individuals can claim a tax deduction on donations made to their PAF:

- › Deductions for a donation can be spread over a period of up to five years.
- › Cash donations are generally deductible up to the limit of an individual's taxable income.

Contributions

You can contribute to your PAF as often or as infrequently as you like. There is no requirement to contribute on a regular basis.

Donating non-cash assets

In addition to cash, the following types of assets can be donated and may be able to be claimed as a tax deduction:

- › Assets acquired during the 12 months before making the donation
- › Shares of \$5,000 or less
- › Assets including shares and property in excess of \$5,000 (valuation requirement applies).

Donors should obtain advice from their tax adviser or accountant.

PAFs and estate planning

When a Capital Gains Tax (CGT) asset owned by a deceased person passes to a beneficiary in their estate, the estate may incur a capital gain on which tax is payable. This is referred to as CGT Event K3. CGT Event K3 is disregarded if the beneficiary is an existing entity with DGR status, such as a PAF.

The trustee

Who can be a trustee of a PAF?

A PAF is a charitable trust controlled by a company as trustee. Most of the directors of the trustee company can be family members or business associates provided that at least one of the directors is an independent person who is a 'responsible person' who is not:

- › The founder
- › A donor who has contributed more than \$10,000 to the fund or an associate of such a donor.

The responsible person must have a degree of responsibility to the Australian community as a whole. Examples of such people as provided by the ATO are:

- › Clergy
- › School principals
- › Lawyers
- › Doctors
- › Other people who perform a public function and belong to a professional body, such as the Institute of Chartered Accountants Australia New Zealand (CAANZ) or the Australian Institute of Company Directors (AICD).

Duties and responsibilities of the trustee

The trustee is responsible for carrying out the terms of the trust and preserving safely the trust property. The duties of trustees include:

- › Administration – The processes of managing the fund to meet its compliance obligations.
- › Investment – The investment of fund assets to protect and grow the real value of the fund.
- › Distributions/Grantmaking – The distribution or granting by the fund to eligible entities.

Administration

Administration and compliance

Like any trust or other legal structure, good basic housekeeping is required. The trustee must:

- › Keep the assets of the fund separate from all other assets and not provide any benefit to donors or trustees.
- › Prepare financial statements showing the financial position of the fund at the end of each financial year, and have those financial statements and compliance with the PAF Guidelines audited.
- › Obtain a valuation of any land in the fund every three financial years and revalue other assets annually.
- › Lodge the Annual Information Statement with the ACNC which includes the ATO Ancillary Fund Return.
- › Ensure adherence with the PAF Guidelines 2009 and ACNC Governance Standards.
- › Prepare, maintain and adhere to an investment strategy for the fund.
- › Ensure the fund's investments are made and maintained on an arm's length basis.

- › Ensure the fund does not carry on a business, and does not borrow money.

If a compliance breach occurs, administrative penalties can be imposed which must be paid by the trustee or the directors of the trustee.

If you use an administrator, managing a PAF and ensuring you meet your compliance obligations needn't be difficult. The Australian Philanthropic Services PAF administration service includes all accounting, secretariat and compliance requirements.

Investments

What investments can be held in my PAF?

PAFs can invest in a wide range of investments including cash, shares, fixed interest securities and property. A PAF must have and adhere to a written investment policy and a review of investment assets is required at least annually.

Investment limitations:

- › PAFs cannot run a business.
- › PAFs cannot borrow other than in exceptional circumstances.
- › Investments must be made on an arm's length basis.
- › Collectibles cannot be purchased and any donated must be sold within 12 months.

Prudent Person considerations

In considering trust investments, trustees must 'exercise the care, diligence and skill that a prudent person engaged in that profession, business or employment would exercise in managing financial affairs of others.' Where the trustee's profession includes being a trustee or managing investments, the duty of care is higher.

In managing trust investments, trustees are required to consider:

- › The benefits of diversification
- › Investing not speculating
- › The purpose and objectives of the fund
- › Balancing risk
- › Maintaining real value of capital and income
- › Tax consequences of investment decisions
- › Liquidity of the investments
- › Costs of investment alternatives and transactions.

Grantmaking

Annual distributions

During each financial year, a PAF must distribute at least 5% of the market value of the fund's net assets (as at the end of the previous financial year).

If the 5% is less than \$11,000, the PAF must distribute at least \$11,000 during that financial year. No distribution is required in the year in which the PAF is established.

It is important to record any conditions attached to grants and monitor grants to ensure they are properly allocated and expended.

Who can I make grants to?

PAFs can only make distributions to Deductible Gift Recipient (DGR) Item 1 charities and, if incorporated in the Deed, to Government entities that have a purpose that is "charitable" i.e. public hospitals and public museums.

DGR endorsement

A deductible gift recipient (DGR) is a fund or organisation that can receive tax deductible gifts. The deduction is claimed by the person or organisation that makes the gift. DGR endorsements are managed by the Australian Taxation Office (ATO).

There are two distinct categories of DGR endorsement. It is critical to understand this as PAFs are limited to funding only one of these types.

- › **DGR Item 1** – known informally as a 'doing' DGR. Most organisations which are endorsed as DGRs will fall into this category, including public benevolent institutions, universities, health promotion charities, environmental organisations and cultural organisations.
- › **DGR Item 2** – known informally as a 'giving' DGR. This category includes public and private ancillary funds. These organisations exist only for the purposes of providing donations to 'doing' DGRs.

DGR Item 2 organisations must only provide funds to DGR Item 1 organisations. A DGR Item 2 may not fund another DGR Item 2, i.e under no circumstances can a PAF distribute funds to another ancillary fund.

To check the DGR status of an organisation you can check the Australian Business Register at www.abn.business.gov.au

International giving

PAFs can make grants internationally if they are made to a charitable organisation that is a registered DGR Item 1, income tax exempt and based in Australia. This includes some 200 approved overseas development organisations.

Which charities should I support?

Deciding which organisations you'll support can be hugely rewarding, but can also be a challenge. The not-for-profit sector in Australia is complex. There are over 20,000 charities with DGR Item 1 status that are able to accept donations from PAFs.

If you are unsure where to start, APS can help you to identify and articulate philanthropic goals, gain insight into particular areas of community need and measure the impact of your giving, as well as providing practical tools to help make your grantmaking seamless and rewarding.

Getting started

How do I establish a PAF?

Australian Philanthropic Services (APS) does all the work to set up your PAF and handles the paperwork from day one. To start the process, all you need to do is complete a simple establishment form and we will do the rest. We will:

- Arrange the incorporation of the trustee company
- Prepare the PAF deed and supporting documentation
- Manage all approvals with the ACNC and ATO
- Brief all directors on their duties and responsibilities.

How long does it take?

It can take between 6-8 weeks for APS to establish a PAF.

How can Australian Philanthropic Services help with ongoing administration?

The administration service provided by APS is a one-stop-shop for PAFs, including all accounting, secretariat and compliance requirements. This means you can decide how much or how little involvement in the PAF you would like – from attending just one annual meeting to being actively involved in the charities you support.

The APS PAF administration service includes:

- Taking care of all ongoing administration, preparation of accounts, organising meetings, overseeing compliance, arranging the annual audit, and all dealings with the ACNC and ATO, including preparation of returns.
- Checking the eligibility of organisations you wish to support.
- Providing you access to our online system with all the information on your PAF available 24/7.
- Briefing the Directors of the PAF trustee and guiding them through compliance issues.
- Providing a range of grantmaking support services to help you make the most of your giving.
- Allocating you a dedicated Governance and Giving Adviser, with extensive experience in managing PAFs.

Who manages the investments in the PAF?

Importantly, APS doesn't manage the investments in the PAF. Your trusted adviser can manage the investments without the hassle of worrying about administration and compliance.

Fees

As a not-for-profit organisation, APS charges modest fees for the establishment and administration of your PAF. Contact us for a full list of services and fee schedule.

Online access

Once you have established your PAF you will be given online access to all your PAF information, including documentation, statutory records, and regularly updated accounts and investment reports.

Australian Philanthropic Services

Australian Philanthropic Services is a not-for-profit organisation that inspires and supports effective philanthropy. Our team is highly regarded in the sector and is backed by a vastly experienced Board, all of whom are philanthropists.

- › We set up and administer private ancillary funds for individuals and families, and work with wealth advisers to help them help their clients do the same.
- › We offer a public ancillary fund, the APS Foundation, in which people can open a named sub-fund.
- › We provide grantmaking support and advice.

We're unique because we're completely independent, not-for-profit, and charge very modest fees.

Contact us

If you have any questions, would like more information, or you would like to arrange an introductory conversation, **call us on 02 9779 6300**.

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This publication is intended as a guide only. For details of the APS service and private and public fund regulations please contact APS on 02 9779 6300 or hello@australianphilanthropicservices.com.au

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