

# Impact Summary: New Zealand Memorial Museum Trust – Le Quesnoy: tax benefits for monetary donations

## Section 1: General information

Purpose
Inland Revenue is solely responsible for the analysis and advice set out in this Regulatory Impact Assessment, except as otherwise explicitly indicated. This analysis and advice has been produced for the purpose of informing policy decisions to be taken by Cabinet.
Key Limitations or Constraints on Analysis
<p><b>Quality of data used for impact analysis</b></p> <p>In developing this Regulatory Impact Assessment (RIA), Inland Revenue used information provided by the New Zealand Memorial Museum Trust – Le Quesnoy (the Trust) in an in-confidence business case, and subsequent telephone and email contact. External information about tourism patterns in France were used to verify or test some of the assumptions underpinning the business case. Not all information in the business case could be verified, however, and the level of donor support beyond 2021–22 cannot be readily determined.</p>
Options considered
This RIA considers whether the Trust should be granted overseas donee status. The decision is binary, and as such, this RIA considers only two options. There are other options that would provide direct Government assistance to the Trust, such as grants. The Trust, however, has signalled that it is not seeking such assistance at this time.
Consultation
Consultation on this issue was in the form of email and telephone conversations between Government agencies, the Trust's Chair and the Trust's advisor. Private sector consultation was not carried out.
Sensitivity to tax benefits
Inland Revenue has been informed by the Trust that its potential donors are sensitive to the tax effects of their donations in their decision-making whether to donate. Inland Revenue does not have information to assess the effect of tax benefits on donor decision to donate.
Responsible Manager (signature and date):
Brandon Sloan Policy and Strategy Inland Revenue 26 July 2018

## Section 2: Problem definition and objectives

### 2.1 What is the policy problem or opportunity?

This RIA considers whether a New Zealand charity, the New Zealand Memorial Museum Trust – Le Quesnoy (pronounced le-ken-wah) should be granted overseas donee status by Cabinet.

The main objective behind the policy underpinning overseas donee status is to indirectly support New Zealand's overseas development aid programme by providing tax benefits, such as tax credits or tax deductions, under the Income Tax Act 2007, to a specified class of charity whose purposes are largely directed at the relief of poverty, or improving education or economic outcomes in developing countries, as set out in criteria set out by Cabinet in 1978. The Trust's purposes fall outside the main objective, and its approval would be an exception to the current policy framework.

A decision to grant the Trust overseas donee status could therefore create a precedent for tax purposes, and raise expectations that Cabinet will look more favourably on future requests from charities whose purposes are not directed at overseas development.

#### New Zealand Memorial Museum Trust – Le Quesnoy

The Trust is proposing to create a memorial museum (the Museum) in Le Quesnoy, France. The Trust is currently raising funds to support the project and wants monetary donations to the Trust to be eligible for tax benefits, so that it can further its objects and tell the story of Le Quesnoy as the cornerstone of the New Zealand First World War military story.

Specifically, the Trust's purposes are:

- To own and operate a Museum in Le Quesnoy, France, that will provide information and learning resources to visitors, and raise awareness of New Zealand's participation in and contribution to the First World War; and
- Develop a programme of cultural and educational exchanges between New Zealand and Le Quesnoy, France, for all people in New Zealand and in France.

The trustee's vision for the Trust is to establish a permanent war memorial in Le Quesnoy, in the form of a Museum, in remembrance of the New Zealanders who fought in France. The proposed Museum would create a complex with functional exhibition space and include self-catering accommodation facilities, which the Trust believes by 2021 will fund the Museum's ongoing operations. Inland Revenue notes that the project is likely to support economic development (tourism) in the region by adding accommodation capacity to the town.

The liberation of Le Quesnoy on 4 November 1918 was New Zealand's last major action during the First World War and, as such, has been viewed as a significant milestone in our military history. The liberation was achieved without the loss of any civilian lives. The town of Le Quesnoy maintains links with New Zealand, and a special connection exists between New Zealand and the people of Le Quesnoy.

Le Quesnoy is located in Northern France (12 km from the Belgium boarder) and its current population is approximately 5,000. Le Quesnoy has fairly limited local amenities (shopping, accommodation and entertainment). The Mayor of Le Quesnoy supports and is an advocate of, the development of the Museum and accommodation project. The Museum is one of a

number of economic development activities being carried out in the region.

The Trust is not part of any Government initiative relating to the First World War Centenary Programme (WW100). The project is a private endeavour.

## Problem definition

The Trust's purposes are outside New Zealand and its donations do not currently qualify for tax benefits. Further, the Trust's purposes fall outside the normal framework used by Cabinet to grant overseas donee status (see **Overseas donee status – Cabinet's approval criteria** below). The Trust is therefore seeking to be granted overseas donee status as an exceptional case.

As with all overseas donee status approvals, legislation is needed to specify that the Trust is a donee organisation (with overseas donee status) for the purposes of the Income Tax Act 2007 and allow donations to qualify for tax benefits (such as the donations tax credit or tax deductions – see **Tax benefits for monetary donations to charities**).

The trustees want to advise potential donors about the Government's decision to facilitate fundraising well before the commemorations at Le Quesnoy on 4 November 2018.

A decision to grant overseas donee status to the Trust would result in the Government indirectly committing funds (through reduced tax revenue) to the Le Quesnoy project, albeit on a successful efforts basis given that the support ultimately depends on the trustees' success in fundraising.

## Tax policy

### Tax benefits for monetary donations to charities

Since 1962, the tax system has provided tax benefits for monetary donations to New Zealand charities (including benevolent, philanthropic, or cultural organisations) whose purposes are largely limited to New Zealand.

Under current tax policy settings, the tax benefits include:

- the donation tax credit of 33 $\frac{1}{3}\%$  of the value of any monetary donations made by a New Zealand resident individual taxpayer, capped to the amount of their taxable income; and
- income tax deductions if the monetary donation is from a New Zealand resident company or Māori authority, capped to the amount of their net income.

Eligibility for the tax benefits is subject to certain statutory limitations on the charities' purposes and application of funds, which must relate "wholly or mainly" to purposes in New Zealand.<sup>1</sup> Generally, the availability of tax benefits for donations is limited to charities with New Zealand purposes only. New Zealand charities that support activities overseas and want their donors to be eligible for tax benefits (in particular, the donation tax credit) must be specifically listed in the Income Tax Act 2007 (overseas donee status).

Broadly, governments seek to promote charitable giving:

<sup>1</sup> There are a number of interpretations of the phrase "wholly or mainly". Inland Revenue is currently analysing submissions on a draft interpretation statement PUB00295 Income Tax: Donee organisations – meaning of wholly or mainly applying funds to specified purposes within New Zealand.

- to further social objectives,
- for the wider benefits to society (externalities), which may be over and above the value of the benefit provided via the tax system, and
- because donations can be effective indicators of when extra goods and services should be provided in market conditions that might otherwise not exist.

### **Overseas donee status – Cabinet’s approval criteria**

In 1978, Cabinet refined the policy position set in 1962,<sup>2</sup> by setting the parameters of overseas charitable activities that may be supported by the tax system:

*The basic criteria for adding an organisation to the list of approved “overseas” charities:*

- (i)     *the funds of the charity should be principally applied towards:*
  - the relief of poverty, hunger, sickness or the ravages of war or natural disaster; or*
  - the economy of developing countries\*; or*
  - raising the educational standards of a developing country\*;*
- (ii)    *charities formed for the principal purpose of fostering or administering any religion, cult or political creed should not qualify;*

*\* developing countries recognised by the United Nations.*

[CM 78/14/7 refers]

The criteria set out in CM 78/14/7 have, except in a few instances, been applied consistently in Cabinet decision-making over the last forty years. Currently 138 charities and other organisations are listed in the Income Tax Act and have overseas donee status. All but four of the charities named on the list meet Cabinet’s approval criteria (CM 78/14/7) and are engaged in overseas development. Of the four organisations that do not meet the criteria and granted overseas donee status, three are Government initiatives and have direct Government oversight or financial support. The other organisation is Amnesty International, a large internationally recognised charity with significant New Zealand donor support.

The eligible purposes set out in the criteria are aligned with the government’s overseas development objectives (disaster relief, provision of humanitarian aid, and assisting developing countries). The eligible purposes are narrower than the common-law meaning of “charitable purpose” and the legislative framework in the Charities Act 2005. Assessing donee status, including overseas donee status, remains the responsibility of Inland Revenue because of the tax benefits attached to monetary donations. The process does not overlap the work of the Department of Internal Affairs – Charities Services.

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<sup>2</sup> At the time, four charities with overseas purposes were specifically named as donee organisations for income tax purposes, and the government acknowledged that charities could be added to the list of names from time to time as comparable cases arise. The four charities were: the Red Cross Society Incorporated, the Council of Organisations for Relief Services Overseas (CORSO), and two leprosy missions. Source: 1962 Budget statement.

Decisions to grant overseas donee status are implemented using legislation.

In 2016, advice to Inland Revenue from the Legislative Design and Advisory Committee confirmed that the use of legislation to implement decisions to give overseas donee status was appropriate, given that approvals are a special case, because:

- determining overseas donee status has (or might have) a political and moral dimension; and
- it ensures decision-making transparency, and promotes a bipartisan approach.

### **Analysing requests for overseas donee status**

Inland Revenue analyses a number of factors when considering a charity's request to be granted overseas donee status. The purpose of the analysis, consistent with CM 78/14/7 and CBC Min (09) 12/2,<sup>3</sup> is to establish whether the charity is capable of meeting its purposes and is accountable for the funds it collects by:

1. reviewing the charity's governing documents (constitution and trust deed) to ensure the activities and purposes are consistent with Cabinet's criteria,
2. requiring the purposes stated in the charity's governing documents to be entirely within the scope of paragraph (i) of the Cabinet criteria and that no personal pecuniary profit can be derived,
3. looking at the clauses governing the nature and extent of the trustees' discretionary powers, the winding-up clause, and the trustees' ability to amend the governing documents,
4. looking at the charity's past, current, and proposed activities,
5. requesting that the trustees provide Inland Revenue with the charity's financial statements,
6. considering the trustees' degree of control over the application of the charity's funds overseas, and procedures in place to ensure accountability for funds,
7. considering the planning, monitoring, and evaluation processes used by the trustees in respect of the application of the charity's funds, including how recipients use the funds, as well as the processes used to select beneficiaries and/or projects to support,
8. asking whether the charity has a legal presence in New Zealand and if it has registered under the Charities Act 2005,
9. considering each request on the basis of other generic tax policy objectives, such as fiscal implications (including risk to the New Zealand tax base), consistency with other current Government policy objectives, and the precedent effect, and
10. consulting with other Government agencies such as the Treasury and the Department of Internal Affairs – Charities Services. The Ministry of Foreign Affairs and Trade is also consulted to identify if any concerns exist with the charity or sensitivities with the countries in which the charity operates. Inland Revenue also uses the New Zealand Police's vetting service in connection with the charity's trustees or directors.

<sup>3</sup> In November 2009, Cabinet endorsed the processes used by tax policy officials to analyse charities requesting overseas donee status, resulting in the release of *Guidelines for using the Cabinet Criteria for Overseas Donee Status*.

In this particular case, points 1 and 2 were ignored, as the purposes of the Trust fall outside the scope of the Cabinet criteria. However, the Trust's deed has the required constraints prohibiting the trustees from deriving any personal pecuniary profit from the Trust's activities, over and above what would be expected from an arm's length transaction.

## 2.2 Who is affected and how?

The Trust is currently raising funds to support the project and wants monetary donations to the Trust to be eligible for tax benefits. The trustees have informed Inland Revenue that its potential donors are tax sensitive, and may not make donations to the Trust if they do not give rise to tax benefits.

## 2.3 Are there any constraints on the scope for decision making?

For present purposes, the Trust wants to influence donor decision-making by offering tax benefits for the monetary donations it receives. This has narrowed the options considered in this RIA to those that concern the tax system.

Alternative Government responses, such as financially supporting the Trust via grants or alternative co-governance structures (public/private partnerships) have not been considered. The Trust is not at this time wanting direct Government support.

This analysis therefore does not consider the wider issue of whether the New Zealand Government should directly support (financially or otherwise) the creation of a war memorial museum in France.

## Section 3: Options identification

### 3.1 What options have been considered?

Acknowledging that the Trust is seeking overseas donee status to support its fundraising efforts, the following criteria have been applied to assess the options:

- *Effectiveness*: Does the option incentivise donations to the Trust?
- *Sustainability*: Does the option maintain the integrity of the tax system and operate coherently with the frameworks used?
- *Fairness and equity*: Is the option consistent with previous decisions regarding granting overseas donee status?
- *Tax administration*: Does the option introduce complexity in tax administration?

Tax compliance implications have not been considered because there is little difference between the options in terms of impact on the Trust.

From the Trust's perspective, the main criterion is effectiveness in terms of encouraging donations to the Trust. From Inland Revenue's perspective, the main criterion is sustainability, that is, the option should be consistent with current tax frameworks.

As entitlement to tax benefits for monetary donations to charities with overseas purposes is prescribed by legislation, non-legislative responses, apart from the status quo, are not viable.

Two options have been considered:

- the Trust's request for overseas donee status is declined (status quo option); or
- the Trust's request for overseas donee status is accepted (exception option)

### **Option one: Decline the Trust's request for overseas donee status (maintain the status quo)**

Under the status quo, monetary donations to the Trust would be ineligible for tax benefits. This would affect the Trust's ability to fundraise and, among other things affect the completion of the proposed Museum. As such, this option does not meet the effectiveness criterion. It is noted that, irrespective of the Trust being granted overseas donee status, other environmental factors, such as the location of Le Quesnoy, and the absence of tourism infrastructure in the area, may have a more direct impact on the viability of the project promoted by the Trust.

Declining the Trust's request for overseas donee status meets the sustainability and fairness and equity criteria because:

- the Trust's purposes are outside the scope of Cabinet's approval criteria (CM 78/14/7 refers), and
- declining the request would be consistent with earlier Cabinet decisions to decline overseas donee status for charities that do not meet the criteria in CM 78/14/7.

There are wider issues to do with whether New Zealand should have a war memorial museum in France to commemorate the military service of New Zealand during the First and Second World Wars, but this question is beyond the immediate scope of this RIA.

Declining the Trust's request for overseas donee status does not impact on Inland Revenue's administration of the tax system and confirms existing policy frameworks and practices.

Feedback from government agencies who were consulted as part of Inland Revenue's analysis of the Trust supported its request for overseas donee status being declined.

### **Option two: Grant the Trust's request for overseas donee status**

Under option two, monetary donations to the Trust would be eligible for tax benefits. This meets the effectiveness criterion. Ultimately, however, the benefit accruing to the Trust depends on its fundraising efforts, as this option only provides indirect Government support to the Trust's project on a successful efforts basis. The trustees report that about \$6 million of donations would be made in the current tax year (2018–19) if the Trust received overseas donee status. The trustees estimate that \$15 million is needed to complete the complex to a point where it can open to the public.

Option two does not meet the other criteria because:

- From a sustainability process granting the Trust overseas donee status would create a precedent. It could raise expectations that Cabinet will look favourably on future requests from charities whose purposes are not directed at overseas development.
- From a fairness and equity perspective, granting the Trust overseas donee status would be inconsistent with previous historical Cabinet decisions that have declined charities with, for example, religious purposes, plant conservation purposes, animal welfare purposes, and animal conservation purposes.

- From a tax administration perspective, granting the Trust overseas donee status may introduce uncertainty about the decision-making process for granting overseas donee status. This could affect the cohesiveness of the approval process and make it more difficult to manage charities' expectations about being granted overseas donee status. Tax policy concerns aside, granting the Trust overseas donee status does not create any implementation concerns, provided that legislation implementing the approval is enacted before 31 March 2019. There are no implications for Inland Revenue's Business Transformation Programme.

### **3.2 Which of these options is the proposed approach?**

Inland Revenue's preferred option is that the Trust's request is declined for the following reasons:

#### **Concerns over visitor assumptions and financial viability**

The information and assumptions supporting the project suggest that the viability of the project, in the absence of an additional direct long-term financial commitment from the Government, is doubtful, if

- forecasting donor support does not materialise,
- expected visitor numbers to the Museum and the number of those who stay at the accommodation complex are not realised.

The business case notes that the Museum will be a loss-making exercise and relies on projected revenue from the accommodation complex to produce a surplus.

Le Quesnoy is in Northern France (12 km from the Belgium boarder) and the current population is approximately 5,000. There are fairly limited local amenities (shopping, accommodation and entertainment) in Le Quesnoy. Research to develop Ngā Tapuwae (a Government WW100 initiative, which developed a trail of key First World War sites relating to New Zealand, which includes Le Quesnoy) noted that many New Zealanders who visit the battlefields in France use Arras, which has well-developed tourist infrastructure, as a base to visit Le Quesnoy.

Revenue assumptions regarding visitors to the Museum and visitor occupation (30,000 per annum, from an unofficial estimated annual day-tripper visitor base of 100,000)<sup>4</sup> appear high, relative to official visitor numbers in the region and to more well-known and established memorials. For example, in 2017, the Tourism Office in Le Quesnoy had 5,205 in-person visitor centre enquiries and 10,000 visitors in its Leisure park, while official statistics record:<sup>5</sup>

- Mémorial Canadien, Vimy<sup>6</sup> (opened 2005); 121,000+ visits,
- La Carrière Wellington, Arras (opened in 2008);<sup>7</sup> 65,000+ visits, and

<sup>4</sup> The Trust notes that a planned cycle way connecting the local towns in the area may increase tourist numbers.

<sup>5</sup> Source: Hauts-de-France Tourism Council 2017/18.

<sup>6</sup> The Canadian National Vimy Memorial has iconic national status for Canadians.

<sup>7</sup> A local French funded project, the Wellington Quarry in Arras, is an underground museum founded to the memory of the British Army and Dominion Forces and tells the story of the New Zealand Tunneling Company. The community project charges €7 (euros), but this is situated in a big city and has an attraction beyond battlefield visitors. Arras is typically used as a base from which tourists visit other war memorials in the region, including Le Quesnoy.

- Australian Memorial at Fromelles (opened in 1998); 32,000 visits.

The Trust is proposing to charge €6 (euros) entry to the Museum. Comparable memorials are free – such as the Canadian National Vimy Memorial, and the St John Monash Centre, Australian National Memorial, Villers-Bretonneux (the latter is cutting edge in terms of museum design and content).

### **Concerns about whether the Trust can meet its charitable purposes**

Inland Revenue notes that detailed provisions have not been made for the cost of acquiring artefacts or curating the Museum. Artefacts that are over 100 years old are subject to an approval process under the Protected Objects Act 1975 if they are leaving New Zealand.

The Trust has not developed plans or policies to implement the cultural exchange programme that underpinned its registration as a charity under the Charities Act 2005. The Trust has explained that cultural exchanges are not a priority at this time.

### **Purposes of the Trust are inconsistent with current policy frameworks**

The project being advanced by the Trust is a private endeavour, and although it is not seeking direct Government assistance, it wants indirect assistance in the form of tax benefits for monetary donations. To achieve this aim, the Trust is asking to be granted overseas donee status as an exceptional case.

Granting overseas donee status is a Government decision, and it has in four instances granted overseas donee status to organisations that do not meet the normal Cabinet criteria to further wider government objectives. Typically, organisations granted overseas donee status in these circumstances are either directly funded by the Government or the Government has governance oversight. The only other exception is Amnesty International, which was granted overseas donee status in 1983 on the grounds that it was widely respected, recognised worldwide and was strongly supported in New Zealand. The last exception was made in 1987 for the Hillary Commission for Recreation and Sport, a public authority.

Neither the direct Government support principle nor all the grounds applying to Amnesty International are present in support of the Trust's request that it be granted overseas donee status.

### **Conclusion**

Inland Revenue considers the Trust should not be given overseas donee status because:

- the Trust's purposes are outside the normal policy parameters for approving overseas donee status, and
- the future viability of the Trust, at this point in time, is far from certain.

Neither option has areas of incompatibility with the Government's expectation for the design of regulatory systems.

## Section 4: Impact Analysis: granting overseas donee status to the New Zealand Memorial Museum Trust – Le Quesnoy

### 4.1 Summary table of costs and benefits

To make the impact analysis in this section more meaningful, it has been prepared illustrating the costs and benefits if the New Zealand Memorial Museum Trust – Le Quesnoy was granted overseas donee status. The cost and benefits are therefore those that may arise when contrasted against the status quo (no overseas donee status).

Affected parties (identify)	Comment: nature of cost or benefit (eg ongoing, one-off), evidence and assumption (eg compliance rates), risks	Impact <i>\$m present value, for monetised impacts; high, medium or low for non-monetised impacts</i>
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Additional costs if the Trust is granted overseas donee status, compared to taking no action		
Regulated parties	On-going compliance costs of the Trust's preferred option are comparable to the status quo.	Low
Regulators	Administration costs increase in response to uncertainty in the decision-making process for overseas donee status.	Medium
Wider government	It is possible that granting the Trust overseas donee status may raise the expectations of the Trust and the town of Le Quesnoy, that the New Zealand Government may contribute further additional funds (either directly or indirectly) to the project to ensure the Trust's continued operations.	Unknown
Other parties	None	N/A
<b>Total Monetised Cost</b>		\$5 million + reduction in Government revenue over the forecast period 2018 to 2021.
<b>Non-monetised costs</b>		<i>Medium</i>

Expected benefits if the Trust is granted overseas donee status, compared to taking no action		
Regulated parties	Improves the Trust's chances of raising the required \$15 million to complete the Memorial Museum project.	Medium
Regulators	None	N/A
Wider government	None	N/A
Other parties	Donors are eligible for monetary donations made to the Trust.	Estimated tax benefit to donors is \$5 million +.

<b>Total Monetised Benefit</b>		\$5 million + reduction in Government revenue over the forecast period 2018 to 2021.
<b>Non-monetised benefits</b>		<i>Medium</i>

#### 4.2 What other impacts is this approach likely to have?

Inland Revenue notes that, at this point of time, there are too many unknowns regarding the proposed operation of the Museum and accommodation complex, and it is hard to assess the viability of the proposal. A potential risk arising from the project promoted by the Trust is that it may put pressure on the Government to provide additional and ongoing Government contributions (either direct or indirect) to ensure the Trust's long-term and continued operations.

### Section 5: Stakeholder views

#### 5.1 What do stakeholders think about the problem and the proposed solution?

The Treasury, the Ministry of Foreign Affairs and Trade, the Ministry for Culture and Heritage, and the New Zealand Defence Force were consulted in the preparation of the attached Cabinet paper. Comments from agencies generally questioned the need for the war memorial museum as promoted by the Trust (there are a number of existing memorials commemorating New Zealand's service during the First World War, including a memorial wall at Le Quesnoy). The Department of Internal Affairs – Charities Services was also consulted, and the New Zealand Police's vetting service was used for the trustees of the Trust. The Department of the Prime Minister and Cabinet were informed.

### Section 6: Implementation and operation

#### 6.1 How will the new arrangements be given effect?

Legislative change to the Income Tax Act 2007 is necessary to implement option two. If the Trust is granted overseas donee status, a Supplementary Order Paper to the Taxation (Annual Rates for 2018–19, Modernising Tax Administration, and Remedial Matters) Bill will be prepared. The changes would apply to monetary donations made on and after 1 April 2018.

The Trust has not highlighted any concerns regarding compliance with the Inland Revenue Acts if is granted overseas donee status.

Inland Revenue would administer the proposed legislative changes. Enforcement of the changes would be managed by Inland Revenue as business as usual. Inland Revenue has assessed the magnitude of the administrative impacts and considers that a decision to grant the Trust overseas donee status can be implemented for the start of the 2018–19 income year (1 April 2018), subject to amending legislation being enacted before 31 March 2019.

## Section 7: Monitoring, evaluation and review

### 7.1 How will the impact of the new arrangements be monitored?

Inland Revenue would monitor the Trust to confirm that it is meeting its purposes if it is granted overseas donee status.

Monitoring the Trust would be done through existing relationships Inland Revenue has with relevant stakeholders and their advisors, as part of its administration of the Inland Revenue Acts (the Income Tax Act 2007, the Tax Administration Act 1994, and the Goods and Services Tax Act 1985).

### 7.2 When and how will the new arrangements be reviewed?

The process for granting overseas donee status is based on an upfront analysis and vetting process. Charities that are granted overseas donee status may be the subject of routine audit or investigation by Inland Revenue if information comes to hand that warrants administrative intervention.

Irrespective of Inland Revenue's tax administration, charities that are granted overseas donee status are required to comply with the requirements of the Charities Act 2005.

Non-compliance with the Charities Act, evidence of wrong-doing, or other action that is contrary to the application of the Inland Revenue Acts may warrant further advice to the Government to the effect that the charity's overseas donee status should be removed.