

18 August 2014

Civil Society Section
Civil Society & Programme Delivery
Policy Branch
Department of Social Services
PO Box 7576
CANBERRA BUSINESS CENTRE ACT 2610

By email: consultationwithcharities@dss.gov.au

Dear Minister Andrews

**Options Paper — Australia's Charities and Not-for-profits
Options for Replacement Arrangements following the abolition of the
Australian Charities and Not-for-profits Commission**

Governance Institute of Australia is the only independent professional association with a sole focus on the practice of governance. We provide the best education and support for practising chartered secretaries, governance advisers and risk managers to drive responsible performance in their organisations.

Our Members are all involved in governance, corporate administration and compliance with the Corporations Act 2001. Furthermore, many of our Members serve as officers of charities, or work for, or are involved with charities, many of which are companies limited by guarantee and various of which are entitled to tax concessions. As a result, they are also involved in the governance of charities and compliance with the Australian Charities and Not-for-profits Commission (ACNC).

Governance Institute of Australia (Governance Institute) is itself a charity operating in the legal form of a company limited by guarantee, established to promote and advance the efficient governance, management and administration of commerce, industry and public affairs and the development of secretaryship of organisations through education and the dissemination of information. Our Members therefore bring extensive knowledge of administration, governance and regulatory frameworks in the charity sector to bear on our comments in this submission.

We have provided a short submission on the Department's template as requested, but note that the Department's request for a two-page response does not accommodate the complexity attached to the changes proposed in the Options Paper. As the purpose of public consultation is to assist in the development of public policy that can be implemented, we have sought to provide sufficient detail in this letter to assist the government in managing the practical implications of the proposed policy. To not deal with the complexity attached to the proposals will introduce unprecedented confusion for the sector. It indicates a lack of appreciation of the many and varied circumstances, sizes, and legal structures used by organisations in the sector.

General comments

The Options Paper proposes significant changes to the regulation of the charities sector. The sector has only recently been subject to fundamental changes in its regulation. The government

is now proposing that the sector, which is under-resourced and largely volunteer-staffed, should implement further changes.

We are convinced that this will cause significant confusion in the sector. A number of issues will arise from this confusion:

- unless sufficient time is granted to the sector to accommodate the changes, the attention of senior members of staff will be turned to seeking to understand and meet their new obligations, which will divert them from attending to their responsibilities to provide charitable services
- without a clear line of communication from the government to each and every charity, including step-by-step instructions as to how to implement the changes, the majority of charities are likely to:
 - not have any knowledge or understanding that their regulatory framework has changed, and
 - be unable to implement the changes proposed in the Options Paper.

Governance Institute strongly recommends that the government provide step-by-step instructions to each charity currently registered on the Charities Register as to:

- what regulatory changes will occur and when
- what it will mean for each type of charity
- what each charity needs to do, and
- where each charity can go for assistance.

Furthermore, the pace of implementation of the proposed changes and the likely consequences for an under-resourced and largely volunteer-staffed sector of not being able to understand the process of change or its implications for their own compliance creates a real risk that the process will in fact fail to meet its objective, and in particular fail to reduce red tape.

Governance Institute strongly recommends providing time for consideration by the charities sector of the changes. To do otherwise risks imposing new and potentially unnecessary compliance costs on an already overburdened sector.

Our detailed comments on each question are set out below.

1 Proposed new reporting arrangements

We note that self-reporting is not necessarily effective in providing the accountability and transparency that donors, volunteers, funder and the general public seek when interacting with charities. In particular, small charities are likely to be unclear as to how best to facilitate self-reporting.

Charities will require from the Department significant guidance and direction as to:

- what self-reporting entails, including guidelines and templates suggesting good practice for providing the information required on websites in relation to:
 - the names of responsible persons
 - details of all funding received from government, both Commonwealth, state and local, and
 - financial reports
- why providing this information increases accountability and transparency and therefore assists the interaction of all stakeholders with the charity and develops trust that the charity is fulfilling its mission.

For example, those charities that are companies limited by guarantee will require a table showing which provisions of the Corporations Act will be 'switched on' again. Attached is an article that Governance Institute published in our journal in May 2013, including a table that showed which provisions in the Corporations Act had been 'switched off' for such charities when

the *Australian Charities and Not-for-profits Commission (Consequential and Transitional) Act 2012* came into effect. The equivalent of this information will be required to be issued to each company limited by guarantee, or a proprietary company limited by shares, that is also a charity, to clarify their compliance obligations.

To illustrate the practical challenges inherent in 'switching on' Corporations Act provisions again for such companies, under the governance standards applicable to charities under the regulations attached to the *Australian Charities and Not-for-profits Commission Act 2012*, charities registered with the Australian Charities and Not-for-profits Commission (ACNC) do not need to hold an annual general meeting (AGM). Governance Institute has been researching the declining attendance rates at AGMs for more than a decade, and supported the governance standard that allowed registered charities that are also companies limited by guarantee to explore other means of engaging with members that could significantly improve member engagement overall.

However, under the Corporations Act, a company limited by guarantee that is also a registered charity MUST hold an AGM. The directors of such companies will also be subject once more to the insolvent trading provisions of the Corporations Act, with attendant significant penalties attached to any breach of the provisions. It is vital therefore that these charities and their directors are provided with clear guidance on what their compliance obligations will be under the changes proposed in the Options Paper. There is a high risk of such charities finding themselves in breach of their compliance obligations due to a lack of understanding or lack of clarity as to what their changed obligations are without such guidance being issued.

Governance Institute notes that significant time will be needed for charities, particularly smaller charities, to develop their capacity in self-reporting. The Options Paper notes that all charities are to have this information available on their websites by 1 July 2015, but without support, instructions, guidance and templates from the government, small charities in particular will struggle to assess how to provide this information and therefore struggle to meet this deadline. Small charities have been supported by the provision of excellent educational materials and guidance issued by the ACNC, all of which is readily accessible on the regulator's website, and have become accustomed to being supported in this manner. It is vital that such support continue to be offered by the government as it changes the regulatory framework for charities.

Charities will also require clear instructions as to which of the following government agencies they can contact to answer any queries in relation to self-reporting, to find guidance and when these agencies will become the 'lead agency':

- the Australian Securities and Investments Commission (ASIC) — we note that ASIC has recently been subject to significant budget cuts and retrenchments, and therefore we have concerns that it may not have the resources to provide the guidance and support that charities will need
- the Australian Taxation Office (ATO) — as a revenue collection agency, this regulator has no experience or expertise in developing guidance and support for charities in relation to the reporting of responsible persons; funding received from government; or financial reporting and we have concerns that it will not be able to provide any guidance or support for charities on these matters
- the proposed National Centre of Excellence — as the Centre is still a concept under discussion and subject to consultation, it is impossible to speculate as to its capacity to provide the guidance and support on self-reporting that charities will be seeking
- the Department of Social Services — the Department also has no experience or expertise in relation to the reporting of responsible persons; funding received from government; or financial reporting and we have concerns as to the capacity of the Department to provide the guidance and support charities will need
- state government agencies — while it is not the role of the Australian Government to direct state governments as to what guidance will be required for charities that are

incorporated associations, particularly as each state has differing compliance requirements, charities that will be regulated by a state government agency will need direction as to which agency they should turn to under the new regulatory framework.

The Options Paper also provides no information to explain how the reform process will be coordinated between ASIC, the ATO, the Department and other regulators, and this makes it very difficult for stakeholders to comment in an informed manner on the likely impact of the proposed changes on charities.

Governance Institute strongly recommends that an integrated approach to the proposed changes at a more measured pace would reap better results in the longer term.

a) Do you believe that these proposed requirements will be less time consuming than current requirements?

It is difficult to determine any accurate response to this question or any of the other questions set out in the Options Paper, as it depends on the regulatory regime with which each particular charity must comply. For example, those charities that are companies limited by guarantee and that will be regulated by ASIC may see a significant increase in compliance obligations, which will inherently be more time-consuming. For example, such charities will revert to having to conduct a statutory AGM, which previous consultation identified as being of doubtful value and an unjustified cost and time imposition on many charities.

The provision of a clear and focused educational campaign accompanied by detailed instructions relevant to the regulatory regime with which each type of charity will have to comply will assist in reducing the time allocation required by charities to meet their self-reporting obligations.

b) What changes would your organisation need to make to meet the new requirements?

Governance Institute of Australia is a charity that is also a company limited by guarantee and will need to assess which provisions are 'switched on' again under the Corporations Act before being able to respond to this question. We may need to engage legal advisers, particularly as our compliance obligations are expanding, but possibly also to make sense of what we are meant to do. This will be time-consuming and expensive.

In relation to the impact on the charities sector generally, each charity will need to determine with which regulatory regime it must comply before being able to assess the changes it will need to make and may need to engage consultants and legal advisers.

Peak bodies in the sector — including Governance Institute — and in each industry in the sector will be required to try to assist members with guidance and support. This will place a strain on the resources of those bodies.

c) Do you foresee any impediments to charities complying with these requirements?

Please see our comments above about the confusion that will be created in the sector, given that charities are likely to:

- not have any knowledge of the changes to their regulatory framework
- not understand what the changes are, and
- be unable to implement the changes proposed in the Options Paper without step-by-step instructions.

Furthermore, we note that the Options Paper states that: 'While the new arrangements for regulators such as the ATO and ASIC will take effect straight away, charities will have until 1 July 2015 to update their websites with the details outlined in this paper'. Charities are likely to

read this as the government stating that ASIC and the ATO have been reintroduced to the regulatory framework as of now, and that a dual compliance regime has therefore been introduced. Companies limited by guarantee that are charities may believe they are subject once more to the 'switched off' provisions in the Corporations Act (with regulatory oversight by ASIC); and incorporated associations in the ACT and SA may believe they are subject once more to state legislation as well as reporting obligations under the ACNC Act. This will cause great confusion in the sector.

d) Do you believe these requirements will provide transparency? If not, what changes would you make?

A self-reporting regime was in place prior to the establishment of the ACNC. The reporting was highly variable in quality and depth and is likely to be so again with a return to this regime.

The information currently populating the Charities Register provides and promotes transparency and accountability by allowing all stakeholders who wish to donate, volunteer and be involved with charities easy access to information about the identity and operation of every charity. The information is provided in the same format and provides comparability. Without access to similar reporting by all charities operating in a similar field, as is currently provided for on the Charities Register, Australians cannot make decisions easily as to which organisation they wish to connect to and be involved with and donate to. They cannot assess if the charities are being prudently managed, so that they can retain confidence that their donations and support are fostering and facilitating the 'mission' they wish to support. The Charities Register provides stakeholders with comparability, which is essential for those wishing to support the activities of the sector. The loss of such quality, consistency and comparability that will come with self-reporting will mean there is less transparency for donors, volunteers and the public at large.

A centrally maintained national register of charities, which is free, online, credible and searchable more readily achieves the objective of public accountability. Moreover, national collection of data on the charities sector also ensures that its vital contribution to Australia can be recognised and policy decisions made about the sector can be properly informed and considered.

Governance Institute strongly recommends that the government develop templates suggesting good practice for self-reporting. This will:

- provide the guidance and directions charities seek in relation to self-reporting
- encourage consistency and quality of self-reporting
- allow for comparability which will increase transparency
- allow for the national collection of data on a charities register.

Unfortunately, funders that are government agencies are likely to continue seeking reporting from charities, which is highly problematic for charities, as each agency requests the information in different formats. This may provide the government agency with confidence that transparency has been maintained, but donors, volunteers and the public at large generally do not have access to this reporting, so there is a reduction in public transparency. Moreover, it does nothing to reduce the red tape for charities, as much of the reporting burden suffered by the charities sector rests with inconsistent accountability and reporting requirements in relation to government funding.

Governance Institute strongly recommends that the government seek consistency of government funding agreements at both the state and Commonwealth level, which would greatly reduce the compliance obligations of charities.

The ACNC had already entered into agreements with other regulators that it would accept reporting to those other regulators, which in turn reduced the reporting burden on various charities (for example, education and health charities). However, Australians will now need to

hunt down such reporting in different places rather than being able to access it in one place, as they currently can on the Charities Register. This will also reduce transparency, as it will become more difficult and time consuming to access reporting.

Governance Institute strongly recommends that the government collate reporting provided to a range of regulators so that donors, volunteers and the public can access easily all reporting by charities. A centrally maintained register of charities and reporting is the best means of providing accountability.

2 Determining charitable status

The ATO is set up for purposes other than to regulate charities. Its purpose is to administer taxation legislation, which is only one part of any organisation's regulatory framework. The ATO is an inappropriate regulator to determine eligibility for charitable status, given its expertise is in one aspect of company regulation alone. Determining charitable status requires a body with expertise in directors' duties, governance frameworks, and financial reporting obligations, rather than by one with expertise in administering taxation legislation.

Moreover, the ATO has a conflict of interest. It is a revenue-raising body. Its charter is to collect tax revenue on behalf of the government and it therefore cannot assist charities seeking to register, as this constitutes the provision of advice on accessing tax concessions. It has no independence in relation to determining charitable status, and is therefore an inappropriate regulator to undertake this task.

The historical circumstances prior to the establishment of the ACNC that held the ATO responsible for determining, under taxation legislation, if an organisation satisfies the definition of not-for-profit are insufficient reason to return the determination of charitable status to the ATO.

a) Which of these two options do you believe best guarantees the independence of the decision making process? Are there any other considerations that should be taken into account when these functions are undertaken?

The Options Paper mentions the conflict of interest to which the ATO is subject. The ATO lacks independence, because:

- it is set up to collect tax revenue on behalf of the government and
- therefore any determination of charitable status is inherently conflicted by its charter because
- the determination of charitable status consists of determining access to tax concessions.

Any assessment process by the ATO is therefore inherently conflicted.

However, neither option set out in the Options Paper adequately responds to the ATO's lack of independence, which makes it unable to manage this conflict of interest.

Option 1 sets out a proposal for an appeals panel. It does not address adequately the independence required to properly undertake assessment and determination of charitable status. Appeals can only be heard after an assessment and determination process. Moreover, charities will be required to incur time and expenses in order to appeal a conflicted assessment process. The ATO's conflict of interest is not addressed adequately by Option 1.

Option 2 proposes a 'Chinese Wall' within the ATO. 'Chinese Walls' are not an effective way of stopping the flow of information or conflicts of interest within an organisation, which is why a separate, independent body is required for determining charitable status. Moreover, the membership of the appeal group will consist of members of the ATO who by the nature of their employment will hold a subconscious assumption that the ATO is probably correct in its

assessment. The ATO cannot be independent in the process of determining charitable status, with or without a 'Chinese Wall'. The ATO's conflict of interest is not addressed adequately by Option 2.

3 Proportionate compliance framework

The proposed changes set out the Options Paper do not create a compliance framework.

With self-reporting, there is no dedicated supervising body assessing whether the reporting meets any compliance obligations. This is an essential component of a compliance framework.

Various threshold issues relating to a compliance framework are not addressed in the Options Paper:

- If a donor, or a volunteer, or a member of the public is concerned about a charity and whether it is fulfilling its mission in its expenditure of funds, or being prudently managed, who can they contact to register concern if there is no supervising body? For example, we refer to the recent media attention on the NSW-based registered charity and religious group Christian Assemblies International (CAI), where allegations of abuse of power and funding were made by members. The ACNC has pledged to investigate the allegations.
- If there is 'wilful non-compliance', who determines who is in breach of the self-reporting obligations? Without any templates or guidance for self-reporting, who determines if self-reporting is adequate or otherwise? Who supervises self-reporting?

These are not minor considerations but go to the heart of preserving trust in the charities sector. Overwhelmingly, registered Australian charities are honest, professional and deserve public support, but the ACNC has dealt with more than 900 complaints or concerns about charities since its inception in December 2012. While most of these have been resolved with education and advice or cooperative intervention by the ACNC, the question remains as to how public trust is to be maintained if the public has no supervising body to refer to if self-reporting is inadequate or raises concerns.

This poses a major risk to the sector. If the media is the only place where members, donors, volunteers and the public can raise concerns, the sector can be tarnished by ill-informed commentary or an absence of any supervising body to address matters where real damage is taking place.

4 Transitional arrangements

The Options Paper states that: 'While the new arrangements for regulators such as the ATO and ASIC will take effect straight away, charities will have until 1 July 2015 to update their websites with the details outlined in this paper ... In order to provide certainty for the sector, current arrangements will remain in place until the legislation receives Royal Assent'.

As the ACNC still exists, many charities may read this statement as advice that ASIC and the ATO have been reintroduced to the regulatory framework as of now and that a dual compliance regime has now been introduced. This creates an extremely challenging and complicated regulatory framework that charities must navigate. Further, given that the change may occur mid-period in terms of a charity's reporting year, it is unclear if the charity has to retrospectively comply with the new relevant authority or have reporting obligations to dual authorities for a transition period.

a) What other transitional arrangements might be required?

The most important question is: Under what legislative framework is the Options Paper suggesting that ASIC and ATO compliance obligations have been or will be reintroduced?

Until charities have certainty that the new arrangements for ASIC and the ATO have legislative grounds, they will lack confidence in any change to the regulatory framework.

A second important question therefore is: Will charities need to seek expensive legal advice to assist them to understand whether they do in fact have any compliance obligations in relation to ASIC and the ATO, given the Paper appears to suggest that this is in place as of now?

Governance Institute recommends that the government release information on the legislative underpinnings to the statement that the ATO, ASIC and other regulators have been or will be reintroduced to the regulatory framework.

b) Are there things the Department could undertake to assist charities with this transition?

The Department needs to urgently issue a clear and focused educational campaign accompanied by detailed instructions relevant to each regulatory regime that charities must comply with, providing step-by-step instructions on what each type of charity needs to understand and do.

The statement in the Options Paper that the new arrangements for regulators such as the ATO and ASIC will take effect straight away, without any accompanying advice on the legislative underpinnings of this statement, or when this takes effect and what charities need to do to navigate what appears to be a potential dual compliance regime introduces unprecedented uncertainty to the sector.

Governance Institute recommends that the Department issue detailed communication and instructions to the charities sector.

c) What factors should be considered in relation to the timing of the new arrangements?

The pace of implementation of the proposed changes and the likely consequences for an under-resourced and largely volunteer-staffed sector of not being able to understand the process of change or its implications for their own compliance creates a real risk that the process will in fact fail to meet its objective, and in particular fail to reduce red tape.

Governance Institute strongly recommends providing at least one year from the enactment of the legislation repealing the ACNC to allow charities sufficient time to:

- consider and comprehend the changes set out in the Options Paper
- understand and then implement the step-by-step instructions yet to be issued by the Department (and possibly other regulators).

To do otherwise risks imposing new and potentially unnecessary compliance costs on an already overburdened sector.

Referral of powers

It would be a credit to the Australian Government if it provided the charities sector with the degree of consistency and support offered to the 'for-profit' sector more than a decade ago when the states referred corporations power to the Commonwealth. This can be achieved by the Australian Government providing leadership on reaching COAG agreement on harmonisation of regulation or a referral of powers. This should also incorporate fundraising legislation.

For any regulatory reform of the sector to succeed, it is essential that the sector is granted the same national context as the private sector. The existing two-tiered regulatory system (state/territory-based incorporated associations and a federal company law regime) is inefficient, costly and does not meet the needs of small or large charities.

Charities deserve to be granted the same national context as the private sector. National regulation of 'for-profit' companies through a referral of powers to establish the *Corporations Act 2001* (Cth) has been of immense economic benefit and value to Australia. There is no public policy argument to support the continuing imposition of dual regulation on charities when our private sector companies have already been freed of such onerous obligations for more than a decade.

Returning regulation to the ATO and maintaining dual state/territory and federal regulation is regressive and imposes more onerous compliance obligations on charities than those regulating the private sector.

One regulatory framework for all charities would bring certainty to the sector and reduce red tape.

Conclusion

Governance Institute has provided our feedback on the Options Paper in order to assist with the many practical complications attached to the proposals it sets out.

Notwithstanding our comments which are intended to assist the government, Governance Institute remains supportive of the retention of the ACNC. We are of the view that returning the charities sector to being heavily but ineffectively regulated is not a reduction of red tape or in the best interests of the sector.

Our preference is to retain the ACNC, but importantly, we support retaining the features of the current regulatory framework for charities, regardless of the identity of the regulatory agency.

Yours sincerely

A handwritten signature in black ink, reading "Tim Sheehy". The signature is written in a cursive, flowing style.

Tim Sheehy
Chief Executive

Table 1: Duties of directors and officers of companies limited by guarantee that are also registered with ACNC

Up to 30 June 2013, in Corporations Act	From 1 July 2013, in governance standards
Exercise due care and diligence — s 180 (business judgment rule protection applies)	<ol style="list-style-type: none"> 1. Directors must be made subject to similar duty (with business judgment rule protection) — Standard 5(2)(a) and protection 2. Section 180 no longer applies
Exercise powers in good faith and for a proper purpose — s 181 (business judgment rule protection does not apply)	<ol style="list-style-type: none"> 1. Directors must be made subject to similar duty (with business judgment rule protection) — Standard 5(2)(b) and protection 2. Section 181 no longer applies
Not improperly use position to gain advantage for self or others or cause detriment to company — s 182 (business judgment rule protection does not apply)	<ol style="list-style-type: none"> 1. Directors must be made subject to similar duty (with business judgment rule protection) — Standard 5(2)(c) and protection 2. Section 182 no longer applies
Not improperly use company information to gain advantage for self or others or cause detriment to company — s 183 (business judgment rule protection does not apply)	<ol style="list-style-type: none"> 1. Directors must be made subject to similar duty (with business judgment rule protection) — Standard 5(2)(d) and protection 2. Section 183 no longer applies
Recklessly or dishonestly fail to act in good faith and for a proper purpose — s 184(1)	Criminal offence in s 184(1) continues to apply
Dishonestly or recklessly use position or information to gain advantage for self or others or cause detriment to company — s 184(2) and (3)	Criminal offences in s 184(2) and (3) continue to apply
Protection for good faith acting in interests of holding company, when director of a subsidiary — s 187	Section 187 protection continues to apply
Officers of company also bound by ss 180 to 184	Officers who are not responsible entities, no longer bound by ss 180 to 183. Remain liable for criminal offences under s 184
Employees of company also bound by ss 182 and 183	Employees no longer subject to these statutory duties
Failure of directors or secretary to make lodgments with ASIC — strict liability offence in s 188	Offence continues in relation to lodgments still required to be made with ASIC
Reliance on information or advice provided by others — s 189	Section 189 still applies and in addition protection 1 to Standard 5 also applies
Power to delegate to committees, employees and others and responsibilities for delegate's actions — ss 198D and 190	Sections 198D and 190 continue to apply. No equivalent in the standards
Disclosure of directors' interests — ss 191 to 194	Simplified obligation to disclose 'perceived or actual material conflicts of interest' — Standard 5(2)(e) and 5(3)
Not to engage in insolvent trading — s 588G and related provisions imposing personal liability on directors	<ol style="list-style-type: none"> 1. Insolvent trading regime in Corporations Act continues to apply. 2. Standard 5(2)(g)