

28 February 2018



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Individuals and Indirect Tax Division  
The Treasury  
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Parkes ACT 2600

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Dear Murray

### **Review of Australian Charities and Not-for-profits Commission legislation**

CPA Australia represents the diverse interests of more than 160,000 members in 118 countries. We make this submission on behalf of our members and in the broader public interest.

CPA Australia's interest in the charities and not-for-profit (NFP) sector stems from the organisation's public interest remit and the significant role our members play in this sector. Our members provide valuable services (both paid and pro-bono) to the charities and NFP sectors both as public practitioners and through direct involvement in the governance and management of charitable and NFP entities.

The Review of the Australian Charities and Not-for-profits Commission (ACNC) legislation presents a timely opportunity for sector stakeholders to provide views on the ACNC's role in regulating the nation's charities sector, and how the ACNC's regulatory oversight could be improved through modifications to the ACNC and other relevant legislation and regulatory requirements.

CPA Australia supported the formation of the ACNC as a national regulator for charities that would, over time, end the disparate and complicated regulatory landscape that imposes an unnecessary and excessive regulatory burden on the sector. The ACNC was established to serve as a lynchpin for the charities sector with responsibility for reducing unnecessary red tape, but equally importantly, to support the effective functioning of the sector and public confidence in it. These attributes are reflected in the three objects applicable to the ACNC under the Australian Charities and Not-for-profits Commission Act 2012 (ACNC Act).

Although the ACNC was established on 3 December 2012, uncertainty over its future brought about by the change in government in 2013 hampered its ability to fulfil its objectives. Understandably, some government agencies were reluctant to enter discussions with an organisation the government of the day had undertaken to abolish. Red tape reduction initiatives were particularly affected. We commend the ACNC staff for their continuing commitment to red tape reduction and other initiatives during uncertain times.

The government's subsequent announcement in March 2016 securing the ACNC's future has removed the uncertainty and should allow the ACNC to achieve better outcomes in red tape reduction and other initiatives. When assessing the ACNC's performance against its objects over the five-year period, the Review Panel should give regard to the initial uncertainty over its existence as discussed above.

The ACNC's Regulatory Approach Statement<sup>1</sup> describes a regulatory pyramid approach founded on providing education and advice to charities in meeting their regulatory obligations. Any subsequent action for regulatory non-compliance is taken where considered necessary and proportionate to address the non-compliance through a stepped approach. CPA Australia strongly supports the continuation of this supportive approach to regulating the sector, with graduated regulated actions depending on the circumstances surrounding non-compliance.

Key areas where CPA Australia believes there is room for improvement within the ACNC legislation are highlighted below, with more detailed comments provided in Attachments 1 and 2 to this letter:

- There is scope for improving the Governance Standards and other provisions in the ACNC legislation to reinforce the responsibilities and obligations of *responsible entities* (registered charities) and *responsible persons* (directors and other board members). We also believe that improvements to transparency can be made to the ACNC legislation, to further assist in the fulfilment of Object 1 of the ACNC Act. Our detailed comments on these matters are provided in response to question 2 in Attachment 1.
- In considering whether the ACNC's regulatory oversight should be extended beyond the current scope of charities, we suggest it could include charitable fundraising currently vested in State/Territory regulators. Such an expansion will require the cooperation of relevant State/Territory regulators.
- There is scope for improving the financial reporting requirements in Division 60 of the ACNC Act and associated legislation. There is also scope to improve the financial reporting framework applicable to charities. We suggest the ACNC, the Australian Accounting Standards Board (AASB), the Auditing and Assurance Standards Board (AUASB) and other stakeholders work together in developing suitable solutions in identified areas for improvement.
- The ACNC has achieved red tape reduction in financial reporting, through various initiatives in cooperation with State/Territory regulators. This however remains a work in progress as duplicate reporting requirements exist in the following areas:
  - Incorporated associations in some States/Territories
  - Fundraising licensing in most States/Territories
  - Grant acquittals at Commonwealth and State/Territory levels

### **Administration matters**

In responding to the Independent Review of the Public Governance, Performance and Accountability Act 2013 (PGPA Act), CPA Australia noted that the ACNC relies on the Australian Taxation Office (ATO) for many of its resources. It is also noted that the ATO Commissioner is the accountable authority for the operations of the ACNC under the PGPA Act. This administrative arrangement creates a tension between the necessity for the ACNC to be an independent agency whilst relying on the ATO for resourcing.

While the scope of this Review does not include funding and resourcing of the ACNC, CPA Australia takes this opportunity to highlight this matter and draw attention to the need to ensure the ACNC is appropriately resourced and structured such that it is able to fulfil its role as an independent agency as intended.

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<sup>1</sup> <https://www.acnc.gov.au/CMDownload.aspx?ContentKey=7e30ef69-7d9b-4b62-980b-540352b2f5a2&ContentItemKey=edf3abba-dd40-4d2f-8dc7-f170263d16a7>

CPA Australia's detailed responses to the questions raised as part of this consultation are provided in the enclosed attachments. If you require further information on the views expressed in this submission, please contact Ram Subramanian, Policy Adviser – Reporting, on +61 3 9606 9755 or at [ram.subramanian@cpaaustralia.com.au](mailto:ram.subramanian@cpaaustralia.com.au).

Yours sincerely

A handwritten signature in grey ink, consisting of a stylized, cursive 'S' followed by a horizontal line extending to the right.

Stuart Dignam  
General Manager, Policy & Corporate Affairs

## **Attachment 1**

### **1. Are the objects of the ACNC Act still contemporary?**

CPA Australia is of the view that the objects of the ACNC Act accurately and comprehensively reflect the legislation's purpose and the role of the ACNC in best supporting the Australian charities sector fulfil its objectives. We do not believe there is any need to modify or add to the three objects of the ACNC Act.

### **2. Are there gaps in the current regulatory framework that prevent the objects of the Act being met?**

#### **Governance**

The Corporations Act 2001 section 111L, Item 5, 'turns off' Part 2D.1 general duties and civil obligations applicable to directors. CPA Australia is aware of some views that this places a greater expectation on the individual charity's appointment processes and constitution rules. There is a risk that these expectations may be unreasonable for individual charities and may not serve the interests of the charities sector or the public interest. Nevertheless, CPA Australia is mindful that the ACNC considers Governance Standard 5 is effective in ensuring responsible persons follow the duties applicable to them. Moreover, undoing the 'turn off' may present challenges around the interaction with other provisions of the Corporations Act 2001, such as those dealing with declaration of contravention (s 1317E), pecuniary penalties (s 1717G) and compensation orders (s 1717H).

On the matter of Governance Standard 5 itself, there is a strong case for significant strengthening of its breadth and comprehensiveness. On the point of concern about driving awareness of the consequences of negligent behaviour and misuse of position and information, it may be worthwhile to give some reference to the powers of the ACNC, say for example, under s 85.10 capacity to issue directions, and under Division 90 to impose enforceable undertakings. Governance Standard 5 could also be strengthened to alert responsible persons as to the expectation that they remain informed of the charity's activities and apply this knowledge to a critical understanding of major decisions.

It is understood also that the ACNC proposes in its submission to the Review, a limited number of changes to remove confusion and minor inconsistencies in the operation of section 111L. CPA Australia broadly supports these changes.

CPA Australia would like to draw attention to two matters around the continuity of application of the criminal law offences in s 184 of the Corporation Act and the rules combatting insolvent trading under Division 3 of Part 5.7B (Recovery of property or compensation for the benefit of creditors of insolvent company).

Each of these extensions of corporate law provisions into the charities and not-for-profit sectors is sound. Treasury will be aware of the ASIC Enforcement Review (Position Paper 7 'Strengthening Penalties for Corporate and Financial Sector Misconduct', October 2017) developments which might have implications for the Commission's oversight and enforcement activities. Also in 2017, the Treasury Laws Amendment (2017 Enterprise Incentives No. 2) Bill passed which, amongst other reforms, introduced a safe harbour mechanism within the insolvent trading provisions (s 588GA – Safe harbour - taking course of action reasonably likely to lead to better outcome for company and creditors). CPA Australia suggests that consideration be given to whether, or not, this relief designed to encourage business turnarounds is fair and reasonable in the charities and not-for-profit sectors and, as such, potentially 'turned off' via the section 111L mechanism.

The ends to which any regulatory and enforcement regime should be applied is achievement of the overarching objectives of the enabling legislation. The first of the current three objectives of the ACNC Act is very much around transparency. Against this, CPA Australia raises some concerns as to whether the almost blanket secrecy provisions within Part 7-1 impede achievement of this objective.

ASIC in its Information Sheet 151 (ASIC's approach to enforcement) states: "We also assert a right to make an enforcement outcome public, unless the law requires otherwise. We will not agree to keep enforcement outcomes secret. This is important for regulatory transparency and effective deterrence." As such, the educative and behavioural power of measured enforcement publication should not be underestimated. Treasury, in the above mentioned ASIC Enforcement Review, discussed the value of an enforcement pyramid model of sanctions and the capacity to coax compliance through enforcement escalation.

The disclosure prohibitions under Subdivision 150-1A and the limited exceptions in Subdivision 150-1C may unduly constrain the Commission in its educative activities. CPA Australia recommends that consideration be given to amending those parts of the ACNC Act to either grant the Commissioner discretionary power to publish decisions and reasons, or make disclosure the default-norm with discretionary power to withhold.

### **Auditor's Report Requirements**

Section 60-45(3)(b) of the ACNC Act requires the auditor's report to describe "any deficiency, failure or shortcoming in respect of the matters mentioned in paragraph 60-30(3)(b), (c) or (d)." Those sub-sections relate to provision of information, explanation and assistance to the auditor, keeping of financial records and other records as required by Part 3-2. As this reporting requirement applies to any matter, all matters whether or not they are material must be reported. It may be more relevant for the ACNC if the auditor's report only included material deficiencies, failures or shortcomings, or else, those matters that are not trivial.

CPA Australia also notes that section 60-30(3) & (4) of the Act requires the auditor to form an opinion (audit) or conclusion (review) about whether all information, explanation and assistance has been given, and sufficient financial records and other required records have been kept.

The nature of the other required records is very broad (Section 55-5), being "records that correctly record its operations, so as to enable any recognised assessment activity to be carried out in relation to the entity", which includes assessment of compliance with the ACNC Act or taxation law. This requirement seems inconsistent as the auditor is not reporting on compliance with the ACNC Act or taxation law and does not fall within the scope of the audit or review of the financial report. CPA Australia recommends the focus of the auditor's opinion or conclusion be the financial report and the financial records and only other records relevant to the financial report. Therefore, section 60-30(3)(d) should be deleted and section 60-45(3)(b) should be amended so that the auditor's report refers to "any deficiency, failure or shortcoming in respect of the matters mentioned in paragraph 60-30(3)(b) or (c)".

### **Winding up**

When a charity applies for registration with the ACNC, the ACNC confirms that the entity's constitutional document includes a "winding-up" clause. Such a clause should include a restriction on winding-up of the distribution of the remaining assets of the entity to a charity or charities that are also not-for-profit, and have charitable purposes that are similar to the charitable purposes of the entity that is winding up. However, once a charity is de-registered, for any reason, the ACNC no longer has jurisdiction over the charity and its remaining assets. The responsibility to ensure the charity's remaining assets are continued to be applied for a charitable purpose will fall on the State/ Territory Attorneys-General in their

capacity as guardians of the public interest. CPA Australia suggests that measures be introduced into the ACNC legislation that provides the ACNC with regulatory powers to ensure the charity's assets are appropriately distributed following de-registration.

### **3. Should the regulatory framework be extended beyond just registered charities to cover other classes of not-for-profits?**

Development of the ACNC legislation was premised on the presumption that the scope of the legislation, whilst initially applying to charities, at some time in the future would also apply to the broader Australian NFP sector. We do not believe this is the right time to extend the scope of the ACNC legislation to apply to the entire NFP sector.

A large proportion of the NFP sector, excluding registered charities, either remains unregulated (e.g. unincorporated associations) or comes under State/ Territory regulation (e.g. incorporated associations). To extend the scope of the ACNC legislation and the regulatory reach of the ACNC to the entire NFP sector would require significant additional resources and expertise being made available to the ACNC. It is also likely that without the acceptance of a national regulator by State/ Territory regulators that would result in the removal of duplicated regulatory requirements, extending the scope of the ACNC to the entire NFP sector will increase unnecessary regulatory burden.

CPA Australia suggests considering a limited and timely extension of the ACNC legislation to cover the regulation of charitable fundraising. In our organisation's submission to the New South Wales Charitable Fundraising Review Discussion Paper, we recommended that the NSW Fundraising regulator could work with the ACNC to establish a framework that allows the ACNC's regulatory oversight, including reporting requirements, to be applied to entities involved in fundraising activities in NSW.

It is noteworthy that a recent report<sup>2</sup> released by the NSW State Government following an inquiry under the NSW Charitable Fundraising Act 1991 states in paragraph 14.8, page 544; "It is recommended that consideration be given to the introduction of a single, unified Australian statutory regime for the regulation of charitable fundraising".

### **4. What activities or behaviours by charities and not-for-profits have the greatest ability to erode public trust and confidence in the sector?**

Activities or behaviours by charities can include unlawful activities such as fraud or terrorist financing. These activities and behaviours are fairly well understood and monitoring and enforcement actions are already being undertaken to address any potential or actual issues arising from such activities.

In addition to the above, other activities or behaviours which can adversely affect public trust and confidence in the sector are listed below, along with some suggestions for remedial action:

- The misuse of charitable resources for private benefit is a significant risk. Regulatory and legal actions are regularly undertaken to address issues arising from the misuse of charitable resources for private benefit and are likely to continue. Updates to the ACNC Act through improvements to the requirements applicable to responsible persons, improved governance standards, enhanced transparency through financial and other reporting requirements should all assist in addressing this issue.

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<sup>2</sup> [https://www.finance.nsw.gov.au/sites/default/files/inquiry\\_report\\_cfa.pdf](https://www.finance.nsw.gov.au/sites/default/files/inquiry_report_cfa.pdf)

- Inappropriate or unlawful practices pursued by NFPs or charities not registered with the ACNC. It is not necessary that the public distinguish between a charity registered with the ACNC from a charity or other NFP not registered with the ACNC. For example, poor fundraising practices and misconduct is often highlighted as a concern that undermines public trust and confidence. Fundraising activities are not currently regulated under the ACNC Act. As noted in response to question 3 above, whilst a long-term solution could be to expand the scope of the ACNC Act to include all NFPs, a short-term solution could include extending the scope to certain activities such as fundraising. The continuation of awareness and education initiatives that better inform the public about the charity and NFP sector and the applicable regulatory frameworks will also be helpful.
- The inappropriate or unlawful actions of individual employees or sub-contractors of a charity could damage a charity's reputation, and also erode public trust and confidence in the sector as a whole. An example is the questionable fundraising tactics adopted by employees or sub-contractors when engaging in public fundraising activities. We suggest strengthening the Governance Standards, including Governance Standard 3 to enhance requirements to comply with Australian laws, and Governance Standard 5 to place specific obligations on Responsible Persons for the behaviours and actions of individuals and organisations acting on behalf of the charity.
- Poor governance practices arising from board or committee members with insufficient knowledge, experience or commercial know-how. In addition to selection of boards or committees with a suitable skills mix, training and education are also vital to ensure board members have the relevant knowledge and experience.

**5. Is there sufficient transparency to inform the ACNC and the public more broadly that funds are being used for the purpose they are being given?**

CPA Australia appreciates that the Review focuses primarily on the ACNC legislation, but it is our view that achieving improvements in transparency may require modifications not only to the financial reporting requirements in the ACNC legislation but also to the applicable financial reporting framework represented by the Australian Accounting Standards (AAS) issued by the Australian Accounting Standards Board (AASB).

The AASB has developed and published a Discussion Paper *Improving Financial Reporting for Australian Charities*<sup>3</sup> (AASB DP) to inform stakeholder views and facilitate discussion to improve financial reporting by charities. We suggest the Review Panel take into consideration the contents of the AASB DP in forming their views on financial reporting by charities.

Although the issues relating to statutory financial reporting requirements set out in the ACNC legislation and the applicable financial reporting framework are interlinked, we appreciate that the focus of this review is the ACNC legislation. Accordingly, we provide below our comments on how Division 60 of the ACNC Act and accompanying legislation could be improved to achieve sufficient transparency in the charities sector.

In addition to our below comments, we have also provided in Attachment 2 to this submission our comments in response to the AASB DP.

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<sup>3</sup> <http://www.aasb.gov.au/Research-Centre/AASB-Staff-Papers.aspx>

## **Uniform application of financial reporting requirements**

CPA Australia notes that the financial information lodged by some charities with the ACNC is withheld from the public register. We also note that the financial reporting requirements do not apply uniformly across the entire population of registered charities. This disparate application of the financial reporting requirements is detrimental to the ACNC Act's first object; "to maintain, protect and enhance public trust and confidence in the Australian not-for-profit sector".

CPA Australia suggests that the financial reporting requirements should apply uniformly to all charities registered with the ACNC. If charity financial reports are withheld or charities are exempt from financial reporting or other requirements, this should be supported by clear reasoning that demonstrates how public trust and confidence in the sector will continue in spite of any exemptions, as well as how the information needs of users are being met in the absence of publicly available financial reports or an Annual Information Statement (AIS).

## **Thresholds for tiered financial reporting**

The current requirement to prepare and lodge financial reports based on AAS by charities with revenue higher than \$250,000 places an unnecessary and excessive burden on charities, particularly at the lower end of the reporting spectrum.

The thresholds for financial reporting by companies limited by guarantee under the Corporations Act formed the basis for thresholds for financial reporting by charities. The consultations that informed the setting of thresholds for financial reporting by companies limited by guarantee mention the role of economic significance and public interest in the setting of thresholds, however no detailed analysis is readily identifiable on how the role of economic significance and public interest ultimately translated into the final thresholds that were determined at that time.

CPA Australia recommends the current thresholds for financial reporting by charities are reviewed and raised to a suitable level based on objective and clear criteria. The role of economic significance and public interest continue to remain relevant, and any new thresholds to be set for financial reporting should, whilst removing any unnecessary regulatory burden on charities, ensure they continue to remain transparent and publicly accountable. As stated above, the issue of which charities should prepare financial reports, and the applicable financial reporting framework, are interlinked.

A further modification that could be more readily achieved through this Review is the provision of an exemption to financial reporting by charities that move to a higher threshold in a particular year due to one-off or exceptional revenue through grants or donations. Currently, if a charity falls into a higher reporting tier in such circumstances, but wishes to remain in its previous reporting tier, they need to apply to the ACNC to obtain an exemption on the premise that its revenues will revert to the previous threshold in the following year. To ease the administrative burden on such charities, CPA Australia suggests the legislation be amended to allow charities to self-assess their eligibility for reporting under a particular tier over a two-year period, rather than every year. The ACNC could continue to monitor compliance with the requirements through the revenue information lodged by charities in their AIS.

The AASB DP proposes some options for consideration on how tiered financial reporting could be improved. Our comments in response to these proposals are included in Attachment 2 to this submission.

The sector could benefit from a more regular and periodic review of thresholds for financial reporting and to facilitate any changes to thresholds, we suggest the thresholds for financial reporting requirements are included in Regulations rather than in the ACNC Act.



The same or similar tiers for financial reporting by other NFP entities exist in Commonwealth legislation (companies limited by guarantee under the Corporations Act) and State legislation (incorporated associations under the respective laws of Victoria and Western Australia). It may be necessary to consider the impact on such other legislation when considering any changes to the current thresholds for financial reporting under the ACNC legislation.

### **Transitional provisions allowing the ACNC to accept reports provided to another Australian agency**

The ACNC legislation includes a temporary transitional provision, until the 2016-17 financial year, to allow the ACNC to accept financial reports given under an Australian law to an Australian government agency, as satisfying the financial reporting requirements of the ACNC legislation. This temporary measure was initially introduced in the ACNC legislation and subsequently extended, to reduce unnecessary red tape for charities, whilst the ACNC undertook various initiatives with other Commonwealth and State/ Territory government agencies to reduce financial reporting red tape.

Through its continued efforts, the ACNC has achieved a fair degree of success in reducing financial reporting red tape, however this remains a work in progress. To allow the ACNC to continue its efforts and successfully achieve its objective of red tape reduction, CPA Australia suggests the current temporary transitional provision is introduced as a permanent feature of the ACNC legislation. Including this provision in Regulations would enable easy withdrawal when the provision is no longer considered necessary.

### **Collective Reporting**

CPA Australia understands that collective reporting, a form of group reporting, available through Division 60 of the ACNC Act, subject to approval by the ACNC, has never been used by any charity or charity group to date. We are also unclear as to the benefits of reporting on this basis. We suggest the Review Panel consider the purpose behind this provision, and whether it is still necessary to be retained within the ACNC Act.

### **Audit and Review Requirements**

Currently audit and review of financial reports are required for large and medium charities respectively. CPA Australia considers that the current thresholds requiring an audit or review are too low and need to be adjusted based on an assessment of the cost of obtaining an audit or review, against the benefits to those who rely on these financial reports.

In addition to audits/ review for medium/ large charities, the financial reports of smaller or potentially all small charities could benefit from a compilation engagement, where a qualified accountant could assist charities to compile their financial report in accordance with the applicable reporting framework. A compilation is conducted under APES 315 *Compilation of Financial Information* and is an engagement which provides no assurance. Instead the qualified accountant applies their expertise in accounting and financial reporting to compile the financial report from the underlying data provided by the charity, but does not verify the accuracy or completeness of the information provided by the client. The preparation of the AIS could also be subject to a similar compilation engagement.

Review engagements are limited assurance engagements intended to reduce the cost burden on charities, whilst still providing limited assurance to stakeholders who place reliance on the financial information. However, information gathered by the ACNC indicates that there is a very low uptake of review engagements by medium charities. This is despite the presumption that reviews should be less onerous to undertake and provide, and therefore less expensive to charities obtaining them for their financial reports.

We acknowledge that there may be many unavoidable factors which influence the low uptake of reviews by medium charities, including contradictory state legislation, requirements from funding providers and restrictions imposed by some charities' rules or constitution. Improvements to the assurance framework applicable to review engagements could contribute to an increased uptake of such engagements where eligible. In addition, the subject matter of these engagements could be narrowed to make the review engagement more understandable and focus the scope of the engagement on users' needs. For example, the subject matter of the review could be limited to whether proper books and records have been maintained, the underlying accounting records agree to the financial report, expenditure has been made in accordance with the charitable purpose or other matters of key concern to users of the financial reports.

CPA Australia recommends that both the nature (such as audit, review or compilation) and subject matter (such as the financial report, books and records or charitable purpose) of the engagement which will meet stakeholder needs for each tier is evaluated and the requirements set out in the regulations rather than the ACNC Act itself. As with the reporting requirements, this would allow more flexibility and timeliness in responding to stakeholder needs.

It will be critical that any assurance engagements required by the ACNC Act or Regulations are engagements undertaken under the standards issued by AUASB. Likewise, if a compilation engagement is required or recommended for charities within a certain tier, such as small charities, those engagements would need to be conducted under the Accounting Professional and Ethical Standards Board (APESB) standard APES 315.

#### **Availability of Registered Company Auditors**

The number of Registered Company Auditors (RCAs) in Australia is declining. The reducing population of RCAs can make it both difficult and expensive for a charity to obtain the services of an RCA, particularly for those in rural or remote locations and for charities with limited financial resources.

In the instances where small or medium charities are obtaining an audit of their financial reports, given the lower risk associated with such charities, CPA Australia considers that a wider group of practitioners could be considered suitable to conduct such audits. Currently, all audits of charities, regardless of their size and complexity, are required to be conducted by an RCA, however reviews may be conducted by a broader group constituting members of a professional accounting body as specified in section 324BE(1) of the Corporations Act. CPA Australia recommends that audits conducted for small or medium charities should also be permitted to be conducted by those specified under section 324BE(1).

New Zealand adopts a two-tiered auditor registration model that includes licensed auditors who are the equivalent of Australian RCAs and qualified auditors, who can undertake certain statutory assurance engagements including charity audits. CPA Australia recommends that consideration be given to developing a similar two-tiered auditor registration model in Australia. This could lead to a new designation for auditors and reviewers of small and medium entities including charities, which requires suitable experience in auditing or reviewing such entities, but will not require the same experience as an RCA. This would broaden the pool of auditors available to conduct audits and reviews and improve access to such services for charities, particularly in rural and remote Australia.

#### **6. Have the risks of misconduct by charities and not-for-profits, or those that work with them, been appropriately addressed by the ACNC legislation and the establishment of the ACNC?**

Please see our responses to question 4.

**7. Are the powers of the ACNC Commissioner the right powers to address the risk of misconduct by charities and not-for-profits, or those that work with them, so as to maintain the public's trust and confidence? Is greater transparency required and would additional powers be appropriate?**

Treasury will be aware of the progress of Treasury Laws Amendment (Enhancing Whistleblower Protection) Bill 2017 which is currently being considered by the Senate Economics Legislation Committee. The Bill will introduce significant enhancement to whistleblower protection under the Corporation Act and introduces similar provision into taxation administration legislation. These reforms are part of government's Open Government National Action Plan which seeks to harmonise whistleblower protection across a number of areas of Commonwealth legislative responsibility. It may therefore be worth considering how these reforms might be adopted within the ACNC Act or whether coverage via amended Part 9.4AAA suffices for body corporates registered via that Act.

Auditors of charities should have an obligation to report to the ACNC significant non-compliance or suspected non-compliance with the ACNC Act or obstruction to their audit or review. CPA Australia recommends that auditors of charities should have reporting obligations to the ACNC equivalent to the auditor's requirements to report to ASIC under section 311 of the Corporations Act, which requires the reporting of significant contraventions or those which have not been or will not be adequately dealt with by commenting on it in the auditor's report or bringing it to the attention of the directors. The contraventions captured in that section are those which the auditor has reasonable grounds to suspect amount to a contravention of the Act, amount to an attempt, in relation to the audit, by any person to unduly influence, coerce, manipulate or mislead a person involved in the conduct of the audit or amount to an attempt, by any person, to otherwise interfere with the proper conduct of the audit. This would support the ACNC's existing investigatory and enforcement powers.

**8. Has the ACNC legislation been successful in reducing any duplicative reporting burden on charities? What opportunities exist to further reduce regulatory burden?**

As noted in the cover letter, the ACNC has successfully undertaken red tape reduction initiatives and continues to engage with Australian governments and agencies to further reduce unnecessary regulatory burden.

CPA Australia supports the ACNC's continuing advocacy initiatives undertaken on behalf of the charities sector, particularly with state/ territory regulators, to further reduce regulatory burden. We commend the ACNC for its efforts in successfully negotiating and achieving desired red tape reduction outcomes in Tasmania, South Australia and the Australian Capital Territory and note the ACNC is continuing its initiatives to achieve similar red tape reduction outcomes with other states and territories.

Significant advances have been made in red tape reduction with other Commonwealth agencies. However, we believe there remains one remaining area of red tape that needs to be addressed. Charities receiving grants from Commonwealth agencies continue to endure the unnecessary burden placed on them to provide multiple acquittals to different grant providers. Although a previous version of the Commonwealth Grant Guidelines (CGG) directed agencies to rely on financial information lodged with the ACNC as satisfying their own acquittal requirements in many cases, this direction is no longer present in the current version of the CGG. CPA Australia recommends reinstatement of this direction.

As part of the objective to reduce red tape reduction, simplification in financial reporting requirements has been achieved through differing means:

- Indigenous Corporations do not have to lodge financial reports with the ACNC as long as they comply with their financial reporting requirements with the Office of the Registrar of Indigenous Corporations.

- The financial reporting requirements for Companies Limited by Guarantee under the Corporations Act have been “turned off”, requiring these entities to only comply with the financial reporting requirements of the ACNC Act.
- Some states and territories have passed legislation that exempts certain regulated entities from financial reporting requirements, if they comply with the financial reporting requirements of the ACNC Act.
- Transitional financial reporting arrangements are in place for non-government schools, and the ACNC also has transitional powers to accept financial reports lodged under another Australian law as satisfying its own requirements.

Although we appreciate that the desired outcome of red-tape reduction is being achieved through the different means illustrated above, there is a risk that a change to the ACNC legislation or one of the other laws/ regulations that interact with the ACNC legislation to achieve red tape reduction, could undermine the red-tape reduction with unintended consequences. CPA Australia suggests a medium to long term objective should be to rationalise the different approaches and align the mechanisms employed to achieve consistent legislative outcomes.

**9. Has the ACNC legislation and efforts of the ACNC over the first five years struck the right balance between supporting charities to do the right thing and deterring or dealing with misconduct?**

Yes, CPA Australia believes the predominantly supportive role played by the ACNC, complimented by its intermittent regulatory intervention actions to address breaches of the law, achieves the right balance for the ACNC and the ACNC legislation. Going forward, CPA Australia recommends the same regulatory approach taken by the ACNC over the last five years.

## **Attachment 2**

### **CPA Australia's comments in response to the Australian Accounting Standards Board Discussion Paper – Improving Financial Reporting for Australian Charities (AASB DP)**

In our responses to question 5 under Attachment 1, we have provided our comments that more directly address the issues relating to the financial reporting requirements in Division 60 of the ACNC Act. However, it is our view that the issues relating to the financial reporting requirements in Division 60 of the ACNC Act and the applicable financial reporting framework are both interlinked. We therefore recommend the Review Panel take into consideration our comments in response to question 5 above in conjunction with the comments we have provided below that address the proposals in the AASB DP.

#### **Thresholds for tiered financial reporting**

As stated previously, it is our view that the current thresholds for tiers of financial reporting are too low and need to be reviewed and revised based on clear and objective criteria. The AASB DP considers four options for change to the current tiered approach to financial reporting by charities.

A three-tiered option (option 2 in the AASB DP) remains in our view the simplest and easiest option to administer, that allows for a reporting structure that gradates charity financial reporting based on their economic significance and public accountability. Our following comments focus on the proposed financial reporting structure and framework under Option 2.

Option 2 as currently proposed will require charities to assess their reporting tier based on their expenses for the year, rather than the current revenue-based criteria. We acknowledge that charity revenue can be subject to significant fluctuations year-on-year due to one-off grants or donations, and expenses may be a more consistent measure. However, as noted in the AASB DP, although it is less likely compared to revenue, expenses can also be subject to significant fluctuations. There is also a risk that some charities could manipulate expenses to achieve a pre-determined outcome for reporting within a particular tier. As an alternative, we suggest that both revenue and expenses be considered as combined criteria for determining which tier a charity should report under.

Charities that fall within tier 2 under the proposed Option 2 will be required to prepare and lodge financial statements applying the Australian Accounting Standards with Reduced Disclosure Requirements (AAS RDR). In our view, the full recognition and measurement requirements of AAS RDR is both excessive and onerous for charities with expenses exceeding \$270,000 per annum. A simplified accruals-based recognition and measurement solution for financial reporting is likely to be more appropriate for charities that fall within tier 2. Our suggestions on how a simplified accruals-based reporting framework could be developed is provided in the following section.

Charities that fall within tier 1 under the proposed Option 2 will be required to prepare and lodge financial statements applying the full Australian Accounting Standards framework. This will be an unjustified increase in financial reporting by larger charities that are currently eligible to apply AAS RDR in the preparation of financial statements. We suggest retaining AAS RDR for financial reporting by charities that fall within tier 3 under Option 2.

#### **The AASB financial reporting framework**

The AASB DP proposes two new tiers of GPFS; a cash-based framework and a simplified accruals-based framework. We have provided our comments below in respect of these two new proposed frameworks.

### ***Cash-based financial reporting framework***

Although some cash-based financial reporting is currently required by small charities (tier 1) through the AIS, the proposed cash-based framework will introduce a standard developed by the AASB that should foster consistency and comparability across charities that are eligible to adopt this form of reporting. It will also serve as a reference point to the ACNC when monitoring financial statements prepared under this framework.

We support the AASB developing and providing a cash-based financial reporting framework to be adopted by eligible charities. Rather than a framework that addresses only cash receipts and payments, we suggest the development of a modified accruals-based framework that also enables a simplified recognition of some assets and liabilities that can be readily identified and measured by smaller charities with limited resources. This will allow some assessment and understanding of not only a charity's cash-based financial performance but also a limited understanding of its financial position.

### ***Simplified accruals-based financial reporting framework***

The AASB DP states that a separate AASB staff paper will be prepared in due course to consider the proposals for a new tier of reporting and the AASB DP suggests that this may be modelled on an NFP version of the IFRS for SMEs standard. The IFRS for SMEs is a simplified version of IFRS developed by the International Accounting Standards Board (IASB) to serve the financial reporting needs of Small to Medium Enterprises.

Previously, CPA Australia has supported proposals to consider the adoption of IFRS for SMEs for financial reporting in Australia. We support proposals to develop a simplified accruals-based financial reporting framework based on a recognised international standard such as the IFRS for SMEs standard. Whilst we believe it remains appropriate to consider adopting and adapting IFRS for SMEs for reporting in Australia, we recommend the following points are taken into consideration in developing a new simplified accruals-based financial reporting framework:

- Any new simplified accruals-based financial reporting framework could be considered as a replacement for special purpose financial reporting in Australia, and this consideration is relevant not just for the charities sector, but across all sectors that currently use this form of reporting. A comprehensive project is necessary to consider the development of a potential new simplified accruals-based financial reporting framework, and this project should address financial reporting for all sectors in Australia, rather than for just the charities sector.
- Any new simplified financial reporting framework should not give rise to significant differences between entities with similar operations in the NFP and for-profit sectors. We provide below a couple of examples where differences in financial reporting could arise:
  - Under the Aged Care Act 1997 all providers of residential care services, regardless of whether they are NFP or for-profit entities, are required to prepare general purpose financial reports. A dedicated NFP simplified financial reporting framework in these circumstances could give rise to differences in financial reports prepared by tier 2 residential care providers, depending on whether they are classified as NFP entities or for-profit entities.
  - Social enterprises are a relatively new and growing sector where entities adopt both for-profit and NFP objectives. Differences in financial reporting may arise depending on whether a social enterprise is classified as a for-profit or NFP entity.
- Any changes to compliance requirements, particularly for smaller charities, needs to be viewed through a costs vs benefits filter. The AASB DP notes that a new framework may result in additional short-term costs during the transition period. We suggest quantification of such costs to the sector before proceeding further.

### **Differential reporting and the reporting entity concept**

The AASB research report *Application of the Reporting Entity Concept and Lodgement of Special Purpose Financial Statements*<sup>4</sup> points to evidence that the reporting entity concept is not being applied as intended, and that many entities that may be reporting entities that should prepare and lodge GPFS are incorrectly preparing and lodging SPFS. A view has also been expressed that if an entity is required to lodge financial statements on a public register which can be accessed by the general public, these should be GPFS.

A further challenge to the reporting entity concept is set to arise with the soon to be published Conceptual Framework from the International Accounting Standards Board (IASB). The IASB Conceptual Framework will be adopted in Australia soon after it is published, as Australia is committed to adopt International Financial Reporting Standards (IFRS) issued by the IASB, and the IASB Conceptual Framework underpins IFRS. The IASB Conceptual Framework includes a description of the Reporting Entity that significantly differs from the reporting entity concept that is currently employed for differential reporting in Australia. This forthcoming development will have an impact on financial reporting by all sectors in Australia, including the charities sector.

The AASB is set to consult on the impact of the IASB Conceptual Framework on the currently applied reporting entity concept. We suggest engaging with the AASB to explore options for addressing this matter, and solutions could include an IFRS for SMEs based simplified financial reporting framework as discussed above.

### **Performance reporting**

There is a view that information about a charity's performance in delivering against its mission and objectives is equally if not more important than its financial performance. There is no reporting framework at present that allows charities to provide information on non-financial performance indicators in a consistent and comparable manner.

The reporting framework for charities in New Zealand includes requirements and criteria for reporting on service performance. The AASB has previously worked with its counterpart in New Zealand to develop proposals on service performance reporting. We suggest the AASB continue to explore development of a framework for the reporting of service performance by charities and other entities that could benefit from such reporting.

In addition to service performance reporting, other information that may be considered useful by stakeholders include specific financial performance indicators such as fundraising costs and program delivery costs. We suggest the AASB considers such identified stakeholder needs for specific financial information in future developments for financial reporting by charities.

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<sup>4</sup> [http://www.aasb.gov.au/admin/file/content102/c3/AASB\\_RR-1\\_06-14\\_Reporting\\_Entities\\_and\\_SPFSs.pdf](http://www.aasb.gov.au/admin/file/content102/c3/AASB_RR-1_06-14_Reporting_Entities_and_SPFSs.pdf)