14 February 2013

Manager, Philanthropy and Exemptions Unit
Personal and Retirement Income Division
The Treasury
Langton Crescent
PARKES ACT 2601

By email: NFPReform@treasury.gov.au

Dear Sir

Not for Profit Accounting Specialists Submission on the draft Australian Charities and Not-for-profits Commission Regulation 2012

We welcome the opportunity to make a submission to Treasury on the Australian Charities and Not-for Profits Commission (ACNC) financial reporting regulations. We broadly support the regulations as drafted to set out the content requirements for financial reports lodged with the ACNC. However we have identified a number of issues and these are outlined in the attached appendix.

Our comments have been endorsed by the following CEOs of Not For Profit organisations;

- ***Sam Tolley, CEO, Women's and Children's Hospital Foundation Inc.***
- ***Kym Barnden, CEO, Common Equity Housing SA Ltd.***
- ***Carley Jones, Executive Officer Playgroup SA Inc.***
- ***Inta Rumpe, The Ethnic Schools Association of SA Inc.***

If you have any queries on our comments please contact Sue Raw, via email at sue@nfpas.com.au or phone on (08) 8215 0022.

Yours sincerely

Andrea Petersen
Director

Appendix One

Reporting Thresholds

As we have previously raised, we understand the basis upon which the reporting thresholds have been derived, however, we still believe that those thresholds, particularly for those entities classified as large and the associated requirements that accompany that threshold, will be onerous for many charities and not for profit organisations. We believe that $1m turnover is quite low and would result in many more obligations than presently in place for organisations of that size. These obligations will result in additional costs for those organisations that are already under cost pressure. As these are now embedded in the legislation, they will be difficult to amend; however, we recommend a review of these thresholds prior to the five year review of the rest of the legislation to ensure they are considered appropriate.

Responsible Entities

The reference to "responsible entity" and "responsible entities" in the regulations could result in a lack of understanding of the terminology as it is not commonly used or understood throughout the sector. We recommend the terminology be changed to something that is clearer and easier to understand.

Comparative information in the 30 June 2014 financial statements

By including the provision to allow registered entities to lodge financial statements without comparative information for the financial year beginning on 1 July 2013, charities who have not previously prepared general purposed financial statements and are now required to, will lodge financial statements that do not comply with accounting standards (i.e. with no comparative information).

This non-compliance will lead to qualification of the audit report. In order to present unqualified financial statements to their members, comparative information will need to be included and therefore, to ensure that these regulations commence from 1 July 2013, financial reports should not be required to be prepared for the ACNC for the 2014/15 financial year, to ensure that comparative information can be included as required by accounting standards.

Annual Information Statement

As at the date of this submission, the draft Annual Information Statement (AIS) has not been released. The explanatory material indicates that the information required in this statement will be proportional to the size of the entity. It is very important that these AIS's are proportional to the size of the entity, especially for small and medium not for profit organisations where resources are stretched and often voluntary (especially for those in the small category). These entities do not have the resources to capture additional information and prepare onerous information statements. It is very important that compliance costs are kept to a minimum, information should not be requested unless it is absolutely essential to achieving the required level of accountability.

Systems may not currently be in place to capture new information, e.g. volunteer hours. In these cases charities should be given the option of providing estimates and give time to put systems in place.

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The application of five key accounting standards

The draft material refers to the expected application of five key accounting standards for all financial statements, whether the entity is a reporting entity or a non-reporting entity. The justification given is that "these five standards are currently seen as necessary for any financial reports to give a true and fair view as required by the financial reporting regulations".

In our experience in dealing with charities in the small and medium tiers, the requirement to apply AASB 107 *Statement of Cash Flows* would be an onerous additional requirement as many of these organisations do not currently adopt this accounting standard. .

To appropriately prepare a Statement of Cash Flows, the preparer needs to have completed appropriate accounting studies to understand the complexities involved in the preparation of the statement and the associated reconciliations.

We would also suggest that the usefulness of the Statement of Cash Flows is limited to those who have a detailed understanding of the accounting treatments of the various items in the statement. The additional cost of preparation would outweigh the benefits to members and users of the statements.

Reduced Disclosure Reporting (RDR)

The explanatory material states that "Entities that choose to apply RDR will be subject to the same recognition and measurement requirements as entities reporting under the full set of accounting standards, but will have considerably fewer disclosures in the notes to their financial statements. This will significantly reduce the disclosure burden, and the reporting and auditing/reviewing costs for registered entities that are required to prepare a GPFR."

Whilst the RDR requirements do reduce the amount of disclosures required in the financial statements, the disclosures required still are reasonably onerous and quite significantly more than many small and medium entities have been producing in the past when preparing special purpose financial statements. For this reason, we believe the statement above from the explanatory material could be mis-leading.

Audit requirements

The legislation states in para 60-30 Audit or review, that;

(1) The audit or review must be undertaken by:
- (a) a registered company auditor (within the meaning of the *Corporations Act 2001*); or
- (b) a firm:
  - (i) that consents to be appointed, or is appointed, as auditor of a registered entity; and
  - (ii) at least one member of which is a registered company auditor (within the meaning of that Act) who is ordinarily resident in Australia; or
- (c) an authorised audit company (within the meaning of that Act); or
- (d) an entity prescribed by the regulations for the purposes of this paragraph."

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We are concerned that whilst this paragraph was inserted into the legislation, the regulations do not provide for auditors other than Registered Company Auditors to be permitted to provide audit services as no details have been included in the regulations around paragraph (d).

We again raise our concerns that in only allowing Registered Company Auditors (RCA's) to perform audits;

- The same auditing requirements imposed on listed companies are being imposed on organisations with a turnover as low as $250,001.
- There is a small pool of RCA's available, this will result in a higher demand for their services and possibly increased prices as a result. Finding a RCA willing and/or with the capacity to take on the work may be difficult.
- RCA's can charge a premium for their services, and rightly so – but this will result in increased costs for charities.
- Charities who are in the "medium" tier, but whose constitution requires an audit, will require the services of an RCA.
- An organisation with a turnover of $1,000,001 is classified as 'large' and is required to have an audit conducted by a RCA. We don't believe a turnover of $1,000,000 sufficiently high to define a charity as 'large' and hence have the same auditing requirements as large publicly listed entities. We believe a turnover of $3,000,000 is a more appropriate threshold.

We would have liked to see the regulations utilise paragraph 60-30 1(d) and widen the base of auditors allowed to perform audits for not for profit entities with turnover between $1,000,000 and $3,000,000 to include other qualified members of the professional accounting bodies in Australia. This will relieve the pressure on the small pool of RCA's in Australia, and more importantly, relieve the cost pressure on not for profit entities of having their annual audit conducted.

In addition, the provision that allows members of professional accounting bodies to perform reviews for those in the medium tier, without requiring those members to have a Certificate of Public Practice (CPP), could expose those members if they do not have the appropriate levels of professional indemnity insurance (such as that required by those holding a CPP). This could have broader implications for the members of the NFP being reviewed.

Public use of the published financial information

Regardless of how the reporting framework is ultimately defined, the ability to make effective comparisons about the cost efficiency of individual charities is at best limited and at worst substantially misleading. The capacity to incorporate explanatory narrative is a useful remedy to a certain extent however we are concerned that any statements by the ACNC should inform readers of the limitations of relying solely on the published information. This is of course somewhat counter intuitive to the rationale for better transparency that enables individual comparisons. Our point here is that readers need to be aware of the limitations of simplistic comparisons and the ACNC must avoid any presentations that encourage a "leader-board" style. Media presentations have already attempted such approaches with disastrous consequences for the charities involved with the relatively poor expense ratio that may in fact have a perfectly reasonable explanation that fails to reach the reader.

Appendix One

Prepared by Not for Profit Accounting Specialists, Andrea Petersen Director.
Endorsed by;
Sam Tolley, CEO, Women's and Children's Hospital Foundation Inc.
Kym Barnden, CEO, Common Equity Housing SA Ltd.
Carley Jones Executive Officer Playgroup SA Inc.
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For more information please contact Director Andrea Petersen or Sue Raw at NFPAS on 08 8215 0022