

15 February 2013

Manager
Philanthropy and Exemptions Unit
Indirect, Philanthropy and Resource Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

Email: NFPReform@treasury.gov.au

Dear Sir,

Consultation Paper: Australian Charities and Not-for-profits Commission – Financial Reporting Requirements

The Australian Institute of Company Directors (Company Directors) welcomes the opportunity to offer comment to Treasury on the Consultation Paper: Australian Charities and Not-for-profits Commission – Financial Reporting Requirements. Company Directors is the second largest member-based director association worldwide, with over 32,000 individual members from a wide range of corporations: publicly-listed companies, private companies, not-for-profit organisations (NFPs), and government and semi-government bodies. As the principal professional body representing a diverse membership of directors, our internationally-recognised services and we provide a broad-based director perspective to current director issues in policy debates.

The NFP sector is one of our core focus areas. Our activities include public and tailored educational services, events, published materials, research and facilitation of dialogue among members and other stakeholders on NFP issues. Additionally, we have participated in NFP policy reform discussions and lodged various submissions, which we have developed in consultation with our membership, including with our standing Policy Committees and NFP Steering Committee.

Company Directors broadly supports the proposed financial reporting requirements. We do, however, believe that some changes are required and importantly stress the need for further guidance and information to ensure the requirements are understood by the breadth of charities operating in the NFP sector. This is essential if the ACNC is to meet its intended objective to “promote the reduction of unnecessary obligations on the sector”.

In summary, specifically we believe:

- The terms “Responsible Entity” and “Responsible Entities” are confusing and should be replaced (see our Governance Standards submission for more detail on this issue);
- Greater clarification is required on the definition of revenue for a charity;
- The Reporting Tiers should be altered or, at a minimum, a formal review mechanism of these inserted into the standards;
- The exception regarding joint and collective reporting should be further explained; and
- Each charity should be able to vary their own accounting period to suit their requirements.

These points are discussed in more detail below.

Responsible entity definition

As has been raised by Company Directors and other stakeholders previously, the terms “Responsible Entity” and “Responsible Entities” should be replaced by “directors and officers”. The terms are confusing and inconsistent with drafting language in other jurisdictions.

Importantly, the term “responsible entity” has an entirely different definition in the *Corporations Act*.

The current terms “responsible entity” and “responsible entities” are not readily understood or commonly used and potentially will affect the understanding of readers. The suggested alternate term would be more appropriate as it well-used and one that most people understand or at least can comprehend on first reading.

We appreciate that “responsible entity” has been used throughout the *Australian Charities and Not-for-profits Commission Act* and as a result this Act will need to be changed retrospectively.

Definition of revenue

The draft standards refer to revenue as defined in accounting standard AASB118. While some may hold the view that the term revenue is easily understood and widely used, it is much more complicated when being determined by a charity.

The examples below highlight some of the issues around the definition and determination of what constitutes revenue for a charity.

- Grants are currently considered to be income for reporting purposes and this means that the Income Statement is likely to be inflated by income that is in fact provided for a capital purpose. Predominantly, such grants are “tied” in that they are provided for a specific purpose and, usually, cannot be applied, as general revenue can be applied, to operations.

- The recognition of assets can also be problematic for registered entities as they receive assets from funders (either via a grant or direct provision of the asset) which are administered but not controlled. Increasingly, funders of assets that are also funding service delivery (e.g. the HACC program) are retaining a significant interest in the assets that are purchased from grants.

This often means that an asset can be applied to the purpose for which it was bought (administered) but not sold or realised in any other way or applied to alternative uses without permission of the funder. Indeed, sometimes the funder requires the asset to be returned should it no longer be required by the grant recipient. At the very least, the recipient organisation must seek permission to change the use of the asset or to realise it.

Company Directors recommends that the ACNC provide guidance to enable charities to determine what constitutes “revenue” for the purposes of the Act. The determination of revenue for each charity is fundamental to all of the financial reporting that flows there on. It should also be clarified that charities need to make these determinations annually.

Without this guidance many registered entities will need to seek external advice which could impose unnecessary costs and divert funds away from their core mission. Failure to clarify revenue recognition may result in registered entities incorrectly determining their appropriate Reporting Tier and therefore imposing unnecessary reporting burdens on them.

We consider the ACNC can provide a useful educational role in this area, as well as a range of checklists, examples or guidelines to assist charities meet their responsibilities.

Reporting Tiers

We understand that the Reporting Tiers have been the subject of consultation, however Company Directors continue to maintain that they are inappropriately calibrated. This is a view endorsed by our members who have provided us with feedback on these standards.

In Company Directors’ view it would be more appropriate, for example, for the upper revenue threshold for a small registered entity to be \$500,000, and the upper revenue threshold for a medium registered entity to be \$2 million.

The current Tiers have been based upon a review of Companies Limited by Guarantee that report to ASIC and we believe this does not adequately represent the breadth of organisations operating in the sector.

If the Reporting Tiers are not changed at the outset, we strongly recommend that the standards expressly include a mechanism to review these Tiers after the first reporting year under the new framework. This post-implementation review will help to promote confidence within the sector that the standards do not place an unreasonable compliance burden on charities and that any unintended consequences will be rectified.

Joint and collective reporting

We recommend that the concept of joint and collective reporting and how this interacts with other obligations be further explained.

The ACNC should clearly explain the intent of including these reporting options within the standards and what accounting framework will be applied in the preparation of these financial statements.

Accounting period

As has been raised by Company Directors and other stakeholders previously, we believe that rather than providing the ACNC Commissioner with the discretion to allow a charity to vary its accounting period, each charity should be free to choose whatever annual reporting period suits their individual circumstances (e.g. some education-based charities may need to report on a calendar year basis to meet funding body requirements).

While we understand the benefits that flow from greater comparability of information, we suggest that forcing charities to have the same accounting period will do more harm than good. In our view such a requirement would impose unnecessary costs on many charities and make it more difficult and expensive for them to obtain accounting and auditing services given the concentration of demand for such services at the end of the 30 June standardised financial year. This is particularly relevant in light of the number of other entities in Australia that also have a 30 June year end.

We trust that our comments and recommendations on the proposed standards make a valuable contribution to the consultation process.

If you would like to discuss our submission in more detail, please contact Steve Burrell, General Manager Public Affairs and Communications, on 02 8248 6627 or at sburrell@companydirectors.com.au.

Yours sincerely,



John HC Colvin
CEO and Managing Director