



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

20 February 2013

Dear Sir/Madam,

RE: AusAID submission – Australian Charities and Not-for-profits Commission (ACNC) annual financial reporting requirements

AusAID welcomes the opportunity to comment on the draft regulations and explanatory Exposure Draft on the proposed Australian Charities and Not-for-profits Commission (ACNC) annual financial reporting framework. AusAID supports the Government in its commitment to minimise the compliance burden on entities registered with the ACNC and agrees that the burden on grant recipients should be reduced wherever possible.

AusAID endorses the general approach to annual financial reporting outlined in the Exposure Draft.

We also strongly believe that there are opportunities to gain additional benefits that have not, as yet, been explored fully. We believe that there is the potential for additional benefits by further alignment of the annual reporting requirements with the principle of 'report-once-use-often', grant management (particularly around acquittals), and the use of risk management to better focus reporting and accountability resources.

AusAID sees the draft requirements for annual financial reports under the ACNC framework as one component within the Government's response to streamlining accountability and compliance requirements for Civil Society Organisations (CSO)/Non-Government Organisations (NGO), particularly around grants. The newly released Commonwealth Grant Guidelines (CGG) applicable from July 2013, and the Commonwealth Financial Accountability Review (CFAR) Position Paper (*Sharpening the Focus*) also bear on the issues we raise in this submission.

AusAID has a close relationship with a large number of CSOs/NGOs who partner with us in delivering Australia's overseas aid program. As such we, and our partners, have experience in working in a wide variety of situations, including difficult and high risk situations, and also in meeting the community's accountability and outcome reporting expectations.

AusAID has extensive government financial management and financial statement reporting experience on our Audit Committee (including independent members Mr Oliver Winder; Mr Len Early; Ms Jenny Morison; Mr David Lawler). Committee members have indicated that they see both potential issues and additional opportunities relating to the newly proposed CSO/NGO accountability requirements. They are mindful of not losing some of the gains in transparency and accountability made over past years.

'Report-once-use-often' reporting framework: grant acquittals

Previous ACNC discussion papers, the new Commonwealth Grant Guidelines and the CFAR Position Paper all include the proposal that if an entity provides annual audited financial statements, then financial grant acquittals should not be required, unless the granting activity is high risk.

AusAID is concerned with some of the underlying logic of this proposal including the level of assurance that can realistically be obtained from the proposed annual financial reporting framework.

The following sections outline our concerns and also present what we believe are opportunities to resolve those issues and allow CSOs/NGOs to still “report once” but in a way that retains appropriate accountability.

Grant acquittals: “not required unless the granting activity is high risk”: is this the correct risk?

The implication of the statement that “if an entity provides annual audited financial statements, then financial grant acquittals should not be required, unless the granting activity is high risk” is that grant acquittals somehow address “grant activity” risk. The CGGs outline a number of risk categories that potentially exist relating to grants: these are (see CGG clauses 7.9 and 9.5):

- risks involved with the granting activity (or grant program)
- risks related to the grantee/recipient; and
- risks directly flowing from the project/task/services being funded

AusAID, in undertaking risk assessments, normally classify grant acquittals as addressing grantee risks rather than those related to the granting activity. It is difficult to see any substantive connection between grant acquittals and the mitigation of granting activity risks.

AusAID believes that to be logical, the statement “unless the granting activity is high risk” would need to be changed to “unless the grantee/recipient risks are high”. This change would also assist implementing agency’s understanding of the issues and decisions they need to make.

Grantee/recipient risks: do we face a catch 22 situation?

If it is accepted that grant acquittals are in reality a mechanism to address grantee/recipient risk our experience at AusAID indicates that grantor bodies will then face a common dilemma.

If in carrying out initial due diligence on an entity it is identified that project financial management capability is relatively weak, often the most appropriate response to this risk is to implement a grant acquittal and reporting regime. This will place some strain and compliance costs on the grantee but should ensure project financial management is strengthened.

On the other hand, if an entity is identified as being strong in project financial management, the need for grant acquittals is less; however as they are strong in this area the production of grant acquittal statements is not difficult and would impose little additional compliance costs on the agency with the exception of needing to have them separately audited.

AusAID therefore feels that one of the focuses in compliance reduction should be around reducing the complexity and costs of grant acquittal audits.

Audited annual financial statements and grant acquittals: is there currently any connection?

Annual financial statements generally do not disclose any financial information about individual grants or their appropriate management. Likewise, the auditing of annual financial statements does not normally include reviewing the specific financial management or recording of individual grant projects and therefore does not provide anything other than minimal assurance in relation to the internal controls, project financial management, or accounts and records relating to grant funds.

Audited annual financial statements, as they currently stand, do not address the same issues or risks that grant acquittals do.

This raises the question as to why the provision of audited financial statements in their current format (addressing one set of risks) would logically exempt an agency from having to prepare grant acquittals (addressing a different set of risks).

These points are relevant to grant administrators because they need to adopt an effective and robust risk management framework. Grant acquittals allow grantors to monitor if the funds are being spent correctly on a

particular project. Consistent with the *ANAO Grants Administration Better Practice Guide* (June 2010) grant acquittals are integral to the success of the grant funding process because they are used by grantors to manage the risks that directly affect grant programs. This includes the risks that funds are not used for their intended purpose and inefficient/ineffective grant implementation. Hence, acquittals are designed to complement annual reporting requirements from the perspective of grant administration.

AusAID believes, and recommends, that consideration be given to the inclusion of summary grant information in annual financial statements as an effective method of bringing together grant acquittals, annual financial statements and independent audit assurance. The inclusion would be optional for reporting CSOs/NGOs.

Core support grants are an exception. Where annual funding support is given to entities to support, or increase, their core activities and service delivery levels, annual financial statements become, in effect, the grant acquittal. The annual financial statements and their audit address risks directly associated with this type of grant. In these circumstances no separate grant acquittal should be required. This specific situation should be explicitly acknowledged in the various documents relating to grants management and CSO/NGO financial reporting frameworks.

The multiplicity of grant acquittals and audits

For those entities managing a portfolio of grants the main issue can be the need to prepare multiple acquittals, with differing formats and requirements depending on individual grantors, and have these separately audited. The ability to deliver summary grant acquittal information within the ACNC financial reporting framework would be a valuable option for CSOs/NGOs.

Limited scope of the current grant acquittal exemption: could the benefits be widened?

The ACNC proposed annual reporting framework only requires large entities (those with annual revenue above \$1 million) to have their annual financial statements audited. Thus the benefits of the current proposal to reduce grant acquittal requirements are limited to this group.

Medium registered entities can choose to have their annual financial statements reviewed rather than audited. AusAID considers that if summary grant acquittal information was included in the notes to the financial statements and those statements were reviewed rather than audited this would still provide sufficient assurance to grantors to meet the majority of grant acquittal needs.

Consideration could be given to widening this to cover small agencies that chose to prepare annual financial statements and have them reviewed (or audited). Small agencies could opt into preparing annual financial statements and having them reviewed (or audited).

Additional financial statement note disclosure proposed

The additional note disclosure proposed by AusAID would be relatively simple and is not considered an onerous obligation. The purpose of the additional note is to disclose supplementary information about specific grants or grant contributions from Government agencies, thereby providing assurance over the reporting entity's grant management capability and performance and eliminating the need for individual grant acquittals.

Please see **Attachment A** for an example of the proposed additional note disclosure.

The inclusion of this additional note would be at the discretion of the reporting entity if they determined that they had significant grant acquittal compliance costs across their total grant portfolio.

The level at which this information is aggregated in the note disclosure would need to be tailored for each reporting entity depending on the number of grants received from Government (or other) agencies. For example, the note disclosure could be at either the individual grant level or aggregated to grants provided at the agency level if the grantor agency indicated this was acceptable.

As this note/appendix would form part of the financial statements it would need to be audited as part of the annual financial statement audit thereby eliminating the need for separate reporting/auditing of individual grants. The cost of the annual audit would be marginally more expensive but be considerably less than separate audits of individual grants/acquittals.

It should be noted that any grant where the grantor does not require acquittal/audit would not need to be included in the table.

Ideally auditor guidance/standards would need to be developed on how and what needs to be audited/reviewed in relation to this disclosure (i.e. controls around project recording in the general ledger, tests regarding purpose of payments, etcetera) to ensure that the appropriate level of assurance is obtained.

Additional commentary

AusAID would also like to make the following general observations in relation to the ACNC financial reporting requirements.

- AusAID strongly supports the inclusion of the responsible entities declaration within the draft regulations. Further guidance regarding who should sign the declaration would be useful to ensure that only those officials with appropriate skills and knowledge make such a declaration.
- The draft regulations and explanatory material make reference to an annual information statement. Further guidance as to what information this statement would contain would be beneficial.

Conclusion

AusAID would once again like to thank you for the opportunity to comment on the content and application of the draft regulations and explanatory material. AusAID is supportive of the Government's red tape reduction agenda and believe the ACNC and the evolving reporting environment is vital to achieving this outcome. However, this approach must ensure that public accountability is maintained and that appropriate levels of assurance are still obtained for granting activities. The amendments to the annual financial reporting model proposed by AusAID are designed to strengthen the level of assurance gained from ACNC reporting entities whilst at the same time minimising any compliance burden, creating a win-win scenario.

In raising the issues we see around grant acquittals it should be noted that AusAID does not see these as necessarily impacting on AusAID's grants management. Payments of assistance for the purposes of Australia's international development assistance program are specifically excluded from the definition of grants for the purposes of the CGGs. Additionally, the majority of our aid projects are likely to fall within the definition of high risk given the inherently difficult situations in which we deliver aid.

Our aim in making this submission is to support the initiatives being undertaken, and suggest possible improvements or additional benefits that might be pursued. As well as wishing to assist with the initiatives currently underway we are also concerned at times with the need to ensure that the underlying logic of proposed initiatives and frameworks are clearly laid out to assist those responsible for future implementation.

Should you have any questions regarding this submission please do not hesitate in contacting me at simon.kidman@ausaid.gov.au or on (02) 6178 4542.

Yours sincerely



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Chief Auditor
AusAID



Paul Wood, FCCA
Chief Finance Officer
AusAID

Attachment A

Note XX: Grant Acquittal Summary (for those grant agreements requiring audited annual acquittals)

Cash based accounting:

	Opening Cash	Revenue	Expenses	Closing Cash
Project/Grant XXX (single funding source)				
Project/Grant YYY (single funding source)				
Project/Grant ZZZ AusAID: World Bank: NGO own funding: (multi funding sources)	\$xxx	\$aa \$bb \$cc \$total		\$xxx

Accrual based accounting:

	Opening Balance	Revenue	Expenses	Closing Balance	Accrued Expenses	Closing Cash
Grant 1 name						
Grant 2 name						

Note 1: projects with multiple funding sources will require careful consideration. Each funding source will be looking to see their funding amounts disclosed if they are to use the table as an acquittal mechanism. Expenditure on a jointly funded project is in reality on a single project total: allocating joint project expenditure to individual donors is artificial, resource intensive, potentially misleading, and in reality not necessary in acquitting a jointly funded project.

Note 2: asset purchases will be a complication requiring consideration. This could be resolved by adding two additional columns – annual asset purchases (after the expense column) and total grant assets balance (last column).