

EXPOSURE DRAFT

EXPLANATORY MATERIALS

Australian Charities and Not-for-profits Commission Act 2012

*Australian Charities and Not-for-profits Commission Amendment Regulations
(No. 2) 2018*

The *Australian Charities and Not-for-profits Commission Act 2012* (the Act) provides for the registration and regulation of charities by the Australian Charities and Not-for-profits Commission (ACNC).

Section 200-5 of the Act provides that the Governor-General may make regulations prescribing matters required or permitted by the Act to be prescribed, or necessary or convenient to be prescribed for carrying out or giving effect to the Act.

The purpose of the *Australian Charities and Not-for-profits Commission Amendment Regulations (No. 2) 2018* (the Regulations) is to prescribe external conduct standards for the purposes of Division 50 of the Act. The external conduct standards provide a minimum level of assurance that registered entities meet appropriate standards of governance and behaviour when operating outside Australia.

Registered entities will need to comply with these standards to be, and remain, registered with the ACNC. The external conduct standards set principles-based minimum standards for registered entities, rather than mandating detailed procedures and requirements.

The standards are intended to promote transparency and greater confidence in the not-for-profit sector across the community and general public that funds sent and services provided overseas by the registered entity are reaching legitimate beneficiaries and being used for legitimate purposes.

Introducing external conduct standards will assist in meeting Australia's international obligations including under the Financial Action Task Force Recommendations (FATF Recommendations). The FATF is an inter-governmental body established in 1989 to promote measures for combatting money laundering, terrorist financing and related threats to the integrity of the international financial system. As a member of FATF, Australia has agreed to comply with the FATF Recommendations.

Introducing the external conduct standards will also assist in Australia meeting its obligations under a number of other international treaties that it is a party to.

Further details of the Regulations are set out in Attachment A.

Subject to the Minister being satisfied that appropriate consultation has been undertaken before the Regulations are made, the Act does not specify any other

conditions that are required to be satisfied before the power to make the Regulations is exercised.

The Regulations are a legislative instrument for the purposes of the *Legislation Act 2003*.

The Regulations commence on the latter of 1 July 2019 and the end of the last day of the disallowance period.

Attachment A

Details of the Australian Charities and Not-for-profits Commission Amendment Regulations (No. 2) 2018

Section 1—Name of Regulations

This section provides that the title of the Regulations is the *Australian Charities and Not-for-profits Commission Amendment Regulations (No. 2) 2018*.

Section 2—Commencement

This section provides that the Regulations commence on the latter of 1 July 2019 and the commencement day referred to in section 50-20 of the *Australian Charities and Not-for-profits Commission Act 2012*. The commencement day referred to in that section is the end of the disallowance period that applies to the Regulations. As provided under section 42 of the *Legislation Act 2003*, the disallowance period is 15 sitting days of each House of Parliament.

Section 3—Authority

This section provides that the instrument is made under the *Australian Charities and Not-for-profits Commission Act 2012* (the Act).

Section 4—Schedules

Each instrument that is specified in a Schedule to this instrument is amended or repealed as set out in the applicable items in the Schedule concerned, and any other item in a Schedule to this instrument has effect according to its terms.

Schedule 1—Amendments

Overview of external conduct standards

The external conduct standards contain guide material to assist readers by providing a plain English explanation of the provisions.

There are four external conduct standards:

- a standard on the activities and control of resources (including funds);
- a standard on the annual review of overseas activities and record keeping;
- a standard on anti-fraud and anti-corruption; and
- a standard on the protection of vulnerable individuals.

Application of the external conduct standards

Each of the four external conduct standards apply to a registered entity if it operates outside Australia, or works with third parties that operate outside Australia.

A registered entity or third party operates outside Australia, if it operates outside Australia in whole or in part.

The external conduct standards are intended to apply to registered entities in relation to matters outside Australia and matters that are not outside Australia, but that are closely related to entities, things or matters outside Australia. For example, the management of overseas aid within Australia is closely related to matters outside Australia if the registered charity either operates or collaborates with a third party that is outside Australia.

A ‘third party’ is defined in relation to a registered entity to mean an entity that formally or informally collaborates with the registered entity for the purpose of advancing the registered entity’s purpose or purposes. A number of additional types of entity are included in the definition of ‘third party’, including:

- an entity with which the registered entity has some form of membership, association or alliance; and
- an entity that has an ‘arrangement’ with the registered entity.

An ‘arrangement’ means any arrangement, agreement understanding, promise or undertaking, whether express or implied, and whether or not enforceable (or intended to be enforceable) by legal proceedings. .

However, a registered entity does not operate outside Australia only because it carries out activities outside Australia that are merely incidental to the operation and pursuit of a registered entity’s purposes in Australia.

Example 1—Incidental to operations and purposes in Australia

A registered entity is set up in Australia to help Australians suffering from cancer. Part of the treatment it provides involves travel to Canada. This would be considered to be incidental when considered with reference to the entity’s operations and pursuit of purposes in Australia, and the entity would not have any obligations under the external conduct standards.

Example 2—Incidental to operations and purposes in Australia

A registered entity is set up in Australia to help homeless Australians. The entity acquires supplies, such as blankets, from overseas providers by mail order. This would be considered to be incidental when considered with reference to the entity’s operations and pursuit of its purposes in Australia, and the entity would not have any obligations under the external conduct standards.

Example 3—Incidental to operations and purposes in Australia

A registered entity that is a school arranges for students to go on a trip overseas to its sister school in Canada. The school’s overseas activities are incidental when considered with reference to the entity’s operations and pursuit of its purposes in Australia, and the entity would not have any obligations under the external conduct standards.

Compliance under the external conduct standards

A registered entity is responsible for assessing its compliance with the external conduct standards. Section 50-10 of the Act specifies that an entity must comply with the external conduct standards in order to become registered, or to remain entitled to be registered under this Act. Because compliance with the external conduct standards is a condition of registration, they are provisions that are ‘subject to monitoring’ under the Act.

Where a provision is ‘subject to monitoring’ the Commissioner of the Australian Charities and Not-for-profits Commission (the Commissioner) may use a range of powers under Chapter 4 of the Act in relation to the registered entity, such as requesting information, entering premises or securing evidence.

Section 35-10 of the Act also allows the Commissioner to revoke an entity’s registration after they have taken into account a range of factors, including the nature, significance and persistence of any non-compliance.

The Commissioner may use all the enforcement powers contained in Chapter 4 when the Commissioner reasonably believes that a registered entity has not complied with an external conduct standard or will likely not comply.

Standard 1—Activities and control of resources (including funds)

The object of this external conduct standard is to give the public trust and confidence that a registered entity is managed in a way that:

- ensures that the registered entity remains solvent;
- minimises risks to the registered entity’s assets;
- ensures that the registered entity, and its resources, are furthering the registered entity’s purposes; and
- ensures that the registered entity is operating in a way that is consistent with its purpose and character as a not-for-profit entity.

The term ‘public’ takes on its ordinary meaning and includes members, donors, employees, volunteers and benefit recipients of a registered entity to which the standard applies.

The standard’s objects are not just about ensuring or safeguarding the activities undertaken by the registered entity while operating overseas, but also preventing registered entities from being used by other parties in a way that is not consistent with its status as an Australian not-for-profit entity. This promotes transparency and confidence across the sector and the public that the registered entity’s activities, funds and services are applied for legitimate purposes.

This standard also assists in meeting Australia’s obligations under FATF Recommendation 8. In particular, the Interpretive Note to the Recommendation sets out measures that countries should adopt, including that not-for-profits are to have appropriate controls in place to ensure that all funds are fully accounted for and are spent in a manner that is consistent with the purpose and objectives of the organisation.

Under the standard, a registered entity is required to have in place reasonable procedures and take reasonable steps to manage the risks associated with its own operations and activities. The standard also requires that reasonable controls are in place with respect to resources given to third parties.

In relation to its own operations and activities, a registered entity must:

- take reasonable steps to ensure that its activities outside Australia are carried out in a way that is consistent with its purpose and its character as a not-for-profit entity; and
- maintain reasonable internal control procedures to ensure that resources (including funds) are used in a way that is consistent with its purpose and character as a not-for-profit entity.

In relation to resources the registered entity provides to third parties, it must take reasonable steps to ensure that the resources (including funds) given to third parties outside Australia (or within Australia for use outside Australia) are applied:

- in accordance with the entity's purpose and character as a not-for-profit entity; and
- with reasonable controls and risk management processes in place.

The requirement that the registered entity must act consistently or in accordance with its character as a not-for-profit entity ensures that while operating overseas the entity acts in accordance with the purpose for which the entity was created and how it is run in Australia. This means acting consistently with the legal requirements of being a charity and not knowingly operating in a way that is inconsistent with those laws.

Because the standards are based around taking 'reasonable steps' or having in place 'reasonable procedures', what is reasonable depends on the circumstances. For example, where there is a higher risk of resources given to third parties not being applied in accordance with the entity's purpose and character as a not-for-profit entity, more controls and risk management processes may need. If funds are being sent to an area with a high terrorism financing risk, greater controls and risk management processes would be needed to address or mitigate the risks.

What is reasonable will depend on the size of the registered entity and the scale of its operations inside and outside Australia and the location and nature of the operations. For larger registered entities or entities with significant resources overseas, having training manuals, staff that ensure compliance and routine audits may be appropriate, whereas this may be beyond what is reasonable for a smaller registered entity if there is less risk of funds being misapplied.

In addition to these requirements, a registered entity must comply with, and maintain reasonable internal control procedures to ensure compliance with, the following laws which also apply to Australians, both in Australia and whilst operating outside Australia:

- money laundering;
- the financing of terrorism;
- sexual offences against children;

- slavery and slavery-like conditions;
- trafficking in individuals and debt bondage;
- people smuggling;
- international sanctions;
- taxation; and
- bribery.

Standard 2—Annual review of overseas activities and record-keeping

The object of this external conduct standard is to ensure that registered entities are transparent and accountable to the Australian public in relation to its activities carried-on outside Australia.

The standard assists in meeting Australia’s obligations under FATF Recommendation 8, in particular, for not-for-profit entities to issue financial statements that provide detailed breakdowns of incomes and expenditures, and have the capacity to provide timely information on its activities, size and other relevant features.

The standard requires that a registered entity must obtain and keep records necessary to prepare a summary of its operations and activities outside Australia on a country-by-country basis for each financial year during which it:

- operated outside Australia; or
- gave resources (including funds) to third parties outside Australia (or within Australia for use outside Australia), other than resources provided to another registered entity.

The purpose of requiring records to be obtained and kept assists an entity to review their overseas activities and to complete an ‘overseas activity statement’, which will form part of the entity’s annual information statement that is required to be provided to the Commissioner. All registered entities are currently required to give an annual information statement to the Commissioner in the approved form no later than 31 December in the following financial year, or such later time as the Commissioner allows. If a registered entity has a substituted accounting period, the Act allows that entity to apply to the Commissioner to submit the report within six months of the end of that period.

Obtaining and keeping records and producing a summary is not intended to be an onerous requirement. Many registered entities with robust internal processes would already be obtaining and keeping records for internal purposes, or may also be subject to existing reporting requirements. For example, the *Private Ancillary Fund Guidelines 2009* has a similar reporting requirement.

The records that must be obtained and kept must enable a ‘summary’ to be produced. A ‘summary’ generally refers to a brief and comprehensive presentation of key facts or statements about particular matters, so records must be obtained and kept to enable a complete and accurate summary to be prepared.

Generally, it is expected that to enable the preparation of a ‘summary’ records must be obtained and kept of the following information:

- the kinds of operations and activities that the registered entity conducted outside Australia, on a country-by-country basis;
- details of how the registered entity’s operations and activities outside Australia enabled it to pursue and achieve its purpose, on a country-by-country basis;
- details of all expenditure relating to its operations and activities outside Australia (on a country-by-country basis);
- details of any procedures and processes that the registered entity used to monitor its overseas operations and activities;
- a list of the third parties that the registered entity worked with outside Australia; and
- details of any documented claims of inappropriate behaviour by the registered entity’s employees or responsible entities outside Australia, and subsequent actions taken by the registered entity as a result.

It is expected that the ACNC will release guidance on the records that should be obtained and kept prior to this standard commencing.

Standard 3—Anti-fraud and anti-corruption

The object of this external conduct standard is to give the public trust and confidence that the registered entity is managed in a way that:

- ensures that the registered entity remains solvent;
- minimises the risks to the registered entity’s assets;
- ensures that the registered entity, and its resources, are furthering the registered entity’s purposes; and
- ensures that the registered entity is operating in a way that is consistent with its purpose and character as a not-for-profit entity.

The term ‘public’ takes on its ordinary meaning and includes members, donors, employees, volunteers and benefit recipients of a registered entity to which the standard applies.

The external conduct standard is intended to promote trust and confidence that the resources of Australian registered entities are being used to further their not-for-profit purposes and are not being misused for illicit or improper purposes.

The standard also assists in meeting Australia’s obligations under FATF Recommendation 8, in particular, for not-for-profits to have appropriate controls in place to ensure that all funds are fully accounted for and are spent in a manner that is consistent with the purpose and objectives of the entity.

Under this standard, the registered entity must take reasonable steps:

- to minimise any risk of corruption, fraud, bribery or other financial impropriety by its responsible entities, employees, volunteers and third parties outside Australia; and
- to identify and document any perceived or actual material conflicts of interest for their employees, volunteers, third parties and responsible entities outside Australia.

Because the standard is based on the registered entity taking ‘reasonable steps’, the steps that are required to be taken depend on the circumstances. For example, a small registered entity may have basic systems and documentation outlining its approach to legal compliance, integrity and ethical conduct. For a large registered entity, reasonable steps may include having greater documentation including a purpose and values statement, detailed operational manuals, extensive training programs, detailed monitoring and reporting systems and a robust, multi-faceted complaints and whistle-blowing system. If the entity operates in a region or environment where there is a higher risk of corruption, it must take greater steps to ensure compliance and mitigate the higher risks.

Standard 4—Protection of vulnerable individuals

The object of this external conduct standard is to ensure that when a registered entity operates outside Australia, it operates in a manner that minimises the risk of abuse to vulnerable individuals.

This external conduct standard is intended to promote trust and confidence that while operating overseas, registered entities work to protect vulnerable individuals from abuse, as this would be consistent with community expectations of how registered entities should operate.

This standard also assists in meeting Australia’s obligations under the Convention on the Rights of the Child (CRC), the UN Guidelines for the Alternative Care of Children and the Convention on the Rights of Persons with Disabilities (CRPD). In particular, Article 3 of the CRC, which requires the protection of children as is necessary to ensure their well-being through appropriate legislative and administrative measures. Similarly, Article 16 of the CRPD requires the protection of individuals with disabilities from all forms of exploitation, violence and abuse through appropriate legislative and administrative measures.

The external conduct standard requires a registered entity to take reasonable steps to ensure the safety of vulnerable individuals outside Australia when the registered entity or a third party in collaboration with the registered entity provides or makes available to the individual services or benefits.

Similarly, if a registered entity or a third party in collaboration with the registered entity employs or engages vulnerable individuals to provide services or benefits on behalf of the registered entity while operating overseas, they also must take reasonable steps to ensure the safety of those individuals in that context.

A vulnerable individual is defined to mean a child or other individual who is or may be unable to take care of themselves, or is unable to protect themselves, for any reason, against harm or exploitation. For example, an individual may be unable to take care of themselves because of their age, an illness, trauma, disability, or some

other disadvantage. A ‘child’ is defined to mean an individual who is under the age of 18 years of age.

Because the standard is based on the entity taking ‘reasonable steps’, the steps that are required to be taken will depend on the circumstances. For example, reasonable steps for a larger registered entity may involve having policy documents and specific training for employees and volunteers on how to minimise the risk of abuse to vulnerable individuals. Similarly, larger registered entities may be required to put in place procedures for handling complaints made about employees or volunteers to ensure that individuals in vulnerable circumstances are not put at risk by the employee or volunteer’s presence. However, reasonable steps for a smaller charity may only involve appropriately investigating and dealing with complaints on an ad hoc basis to ensure that individuals in vulnerable circumstances are protected.

What is reasonable also depends on the risks posed to the vulnerable individuals. Where the risk is greater, more steps may be required to be taken. For example, if there is some risk of abuse to children, it may be necessary to take greater steps to reduce or eliminate that risk.