



27 January 2012

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

Consultation Paper: Review of not-for-profit governance arrangements

The Institute of Chartered Accountants in Australia (The Institute) welcomes the opportunity to make a submission to the Treasury to assist with its consultations on governance arrangements faced by the not for profit (NFP) sector.

The Institute is the professional body for Chartered Accountants in Australia and members operating throughout the world. Established by Royal Charter in 1928, we have a long tradition of leading the Australian Chartered Accounting profession.

Our members serve the public interest through their obligation to uphold high standards of service within many facets of the economy; in public practice and commerce, and sectors including government, not-for-profit and academia. Many of our members are involved in the NFP sector as directors, treasurers, accountants or auditors (in either paid or voluntary capacities) and are therefore passionately interested in the topic. Over the past few years we have regularly made submissions to both Commonwealth and State governments and at times presented evidence to inquiries on NFP issues.

The Institute has a pivotal role in promoting financial integrity in society. We do this through our leadership and our advocacy work on influencing policy and regulatory frameworks in Australia, and in relevant international settings.

We represent up to 70,000 current and future business leaders, with more than 57,000 members, and around 13,000 talented graduates working and undertaking the Chartered Accountants Program.

Through the Global Accounting Alliance, Institute members are also part of an 800,000-strong network of professionals and leaders worldwide.

We strongly support the government in its commitment to strengthening the NFP sector, including the establishment of the Australian Charities and Not-for -profits Commission (ACNC). However, given the main problems identified below we consider the implementation date of 1 July 2012 is too soon to enable full consideration of all the relevant issues. We would recommend the ACNC is still established on 1 July 2012, in a separate Act dealing with the establishment and powers of the ACNC only. Any legislation actually establishing duties and responsibilities of the NFP sector should be debated further, and thereby should not become operational until 1 July 2013 at the earliest. This should give the ACNC time to consult with the various other NFP sector regulators and the sector itself in order to achieve its objective of streamlining and reducing the bureaucratic and administrative burden faced by the sector. It would give time to refine the legislation before its release and give the NFP sector adequate time to develop processes to deal with the changes. We further recommend that the Commonwealth accelerate the harmonisation of legislation, so that State based associations legislation can mirror the changes to that required for the ACNC. This will address the confusion that currently exists as to how the Commonwealth, States and Territories will work together on the NFP sector reform.

Customer Service Centre
1300 137 322

NSW

33 Erskine Street
Sydney NSW 2000
GPO Box 9985
Sydney NSW 2001

Phone 61 2 9290 1344
Fax 61 2 9262 1512

ACT

L10, 60 Marcus Clarke Street
Canberra ACT 2601
GPO Box 9985
Canberra ACT 2601

Phone 61 2 6122 6100
Fax 61 2 6122 6122

Qld

L32, 345 Queen Street,
Brisbane Qld 4000
GPO Box 9985
Brisbane Qld 4001

Phone 61 7 3233 6500
Fax 61 7 3233 6555

SA / NT

L11, 1 King William Street
Adelaide SA 5000
GPO Box 9985
Adelaide SA 5001

Phone 61 8 8113 5500
Fax 61 8 8231 1982

Vic / Tas

L3, 600 Bourke Street
Melbourne Vic 3000
GPO Box 9985
Melbourne Vic 3001

Phone 61 3 9641 7400
Fax 61 3 9670 3143

WA

Ground, 28 The Esplanade
Perth WA 6000
GPO Box 9985
Perth WA 6848

Phone 61 8 9420 0400
Fax 61 8 9321 5141



NFP reform elements released on 8 and 9 December 2011

The following comments relate to the package of NFP reforms released on 8 and 9 December 2011. Comments relating specifically to governance arrangements will follow.

The relevant consultation documents are:

1. Consultation paper for review of not-for profit governance arrangements;
2. Exposure draft legislation to establish the ACNC; and
3. Consultation paper on the implementation design

General Comments

We consider the consultation period for the three elements of reform referred to above to be inadequate for an inquiry as far reaching as this one considering the current diversity of legal regimes. Further such consultation precedes parallel reforms in fundraising and companies limited by guarantee, which will have a direct impact upon this review. We appreciate the extension of the deadline to 27 January 2012 for the first two items. However, with the consultation period predominantly over the traditional Australian holiday season, we have found it difficult obtaining appropriate member comment in order to meet the submission deadline. It is vital for NFPs to be given the opportunity to respond to these proposals. We do understand that Treasury's intention for the new legislation to be in place by 1 July 2012 in order for the ACNC to become operational. We also understand that passing any legislation through parliament is a lengthy process, but our concern is that there will be very little input from those that the legislation is meant to assist. Therefore the opportunity for a collaborative process so necessary for successful implementation of such wide ranging significant reforms will be lost.

We are also concerned with the regulatory burden attached to such proposals. One of the core purposes of the reforms is to streamline and reduce the bureaucratic and administrative burden for NFPs. However, the paper fails to address the question of how the proposed regime will co-exist with parallel existing legislation. Many NFPs have multiple reporting requirements, particularly those grantee organisations that must provide acquittal reports to fund providers. The consultation papers do not show enough action to allow progression to a truly 'one-stop-reporting shop'. Again the opportunity to engage NFPs fully in this reform process is lost as there does not seem to be any real reduction in the reporting burden imposed on the NFP sector by multiple layers of reporting requirements. Presumably, at least at the outset, incorporated associations and other entities will be required to fulfill the requirements of at least two sets of regimes, with different regulators. It is possible that these regimes may be in conflict and at the very least increased regulatory burden will result in the need to ensure compliance with both regimes. Therefore we consider that there are still many detailed negotiations between agencies/regulators to be concluded on, before the ACNC can be operational. Only then will the sector become more confident that the requirements are not duplicative, burdensome or unclear.

Our last general point that we make in relation to all three consultation documents is that it is unclear how they interrelate. We understand the proposed legislation in respect of the governance framework is not contained in the current ACNC exposure draft. We presume this is because the outcome of the governance consultation paper will inform the proposed legislation. However, given our comments on the consultation paper below, we strongly suggest that the outcome of this review is exposed for consultation prior to forming legislation in this area. Further, there appears to be some crossover between Division 55 of the exposure draft which covers reporting and the ACNC reporting framework section of the implementation design consultation paper. It would therefore appear to be necessary to review the implementation design consultation paper in order to provide comments on the exposure draft. However, the deadlines for comment are one month apart. The relationship between these three documents needs to be clarified and any crossover or inconsistencies highlighted and explained to all stakeholders so they can comment in an informed manner.



Governance arrangements Consultation document

We support the intent of the governance review to centralise and simplify the governance arrangements in order to reduce red tape and minimise compliance burdens for the NFP sector. We support the approach set out in the consultation paper of high level principles -based rules with supporting non-mandatory guidance. However, whilst the paper refers to a principles-based approach many of the questions in the paper deals with prescriptive matters. We suggest that many of these matters raised in the questions be left to the governing bodies of individual organisations, rather than form part of the legislative framework.

Comments addressing your specific consultation questions follow in appendix 1.

If you have any queries on our comments please contact Ms Kerry Hicks, the Institute's Head of Reporting via email at kerry.hicks@charteredaccountants.com.au

Yours faithfully,

Lee White
Chief Executive Officer

Appendix: Detailed Answers to Consultation Questions

1. Should it be clear in the legislation who responsible individuals must consider when exercising their duties, and to whom they owe duties to?

The legislation should not attempt to define classes of the community relevant to an organisation. The legislation should refer to stakeholders in the broadest terms. Each responsible individual should then be responsible to those stakeholders particular to their organisation. The organisation and the responsible individuals should determine who they must consider when exercising their duties and to whom they owe duties.

2. Who do the responsible individuals of NFPs need to consider when exercising their duties? Donors? Beneficiaries? The public? The entity, or mission and purpose of the entity?

Consistent with our response on Question 1, in our view responsible individuals need to consider the mission or purpose of the entity when exercising their duties.

Each NFP organisation has a different mission or purpose so may have different stakeholders in each case. The law may then wish to require the company/entity to identify their duties to others.

Determining what is in the best interests of the NFP will require the responsible individuals to assess the interests of a range of stakeholders of the organisation, dependent on the circumstances.

3. What should the duties of responsible individuals be and what core duties should be outlined in the ACNC legislation?

We believe that the duties of responsible individuals in the ACNC legislation should be principles-based and similar to the duties of company officers, contained in the Corporations Act, and certainly no more arduous. We support the duties as set out in clause 91 of the consultation paper, being:

- a duty of care and diligence;
- a duty to act in good faith in the best interests of the entity;
- a duty to not misuse their position;
- a duty to not misuse information; and
- a duty to disclose material personal interests.

We consider that the duties above encapsulate all the tried and tested concepts relating to fiduciary and other duties imposed by law where one is acting for the benefit of those acting mainly for the benefit of others.

However we note that the definition of responsible individual seems to include concepts of director and officer as defined under the Corporations Act 2001. We would prefer consistency with the Corporations Act and thereby request that these concepts and associated duties are identified separately. Different statutory duties should be legislated for different categories of responsible individuals, for example similar to directors and officers under the Corporations Act.

4. What should be the minimum standard of care required to comply with any duties? Should the standard of care be higher for paid employees than volunteers? For professionals than lay persons?

In our view the minimum standard of care should be that of a 'reasonable person'.

We do not believe there should be any different levels of responsibilities for individuals because of their employment status. If a person is in a position of responsibility, then they need to accept the responsibilities of that position no matter what their qualifications or employment status is. In having

Appendix: Detailed Answers to Consultation Questions

this view we are mindful to mirror the responsibilities of company directors– their responsibilities are consistent and independent of their employment or qualifications.

We strongly support the ACNC having a ‘best practice’ encouragement role and therefore are of the view that the ACNC should have publicly available principles-based governance models. This should be supported by suitable training and advice programs.

5. Should responsible individuals be required to hold particular qualifications or have particular experience or skills (tiered depending on size of the NFP entity or amount of funding it administers)?

We do not support requirements for responsible individuals holding particular qualifications, experience or skills. This would impose a higher standard than what currently exists for company directors. Introducing more stringent requirements for the NFP sector would be difficult in relation to staff and board recruitment, particularly in rural or remote Australia where qualified persons are often scarce and generally over-committed.

6. Should these minimum standards be only applied to a portion of the responsible individuals of a registered entity?

No, we believe this will introduce distortions and have unintended adverse consequences. See response to Question 5.

7. Are there any issues with standardising the duties required of responsible individuals across all entity structures and sectors registered with the ACNC?

A principles approach should be pursued, allowing for organisations to develop the most appropriate specific duties to achieve the purpose or mission of the organisation. We support the principles outlined in paragraph 91 of the paper as the set of duties required, and we consider it would be beneficial using the Corporations Act as a model for these duties. Very specific mandated duties will detract from good governance and impose additional burdens often unnecessary for those with existing effective governance arrangements.

8. Are there any other responsible individuals’ obligations or considerations or other issues (for example, should there be requirements on volunteers?) that need to be covered which are specific to NFPs?

Significantly diverged requirements between the for-profit and not-for-profit sectors in respect of directors’ duties would not be desirable as it would reduce the flow of cross-sector governance experience and expertise at board level.

We do not consider that there should be additional requirements on volunteers who are not responsible individuals. This would be counterproductive to legislative changes that have been made to encourage volunteering.

9. Are there higher risk NFP cases where a higher standard of care should be applied or where higher minimum standards should be applied?

We support a principles-based approach and thus the standard of care and diligence expected of a responsible individual would depend on the entity size, amount of public monies involved, the individual’s qualifications and the risk of the entity’s activities. Further, a ‘higher risk NFP’ is a vague concept and will be difficult to define.

Appendix: Detailed Answers to Consultation Questions

10. Is there a preference for the core duties to be based on the Corporations Act, CATSI Act, the office holder requirements applying to incorporated associations, the requirements applying to trustees of charitable trusts, or another model?

We believe the core duties should be based on the Corporations Act, which appears to be more readily considered by the Courts and therefore has a higher base of common law.

11. What information should registered entities be required to disclose to ensure good governance procedures are in place?

This section of the Consultation Paper is somewhat confusing. It appears to refer to disclosure of financial information, internal governance rules, remuneration and conflicts of interest. These are all discrete topics involving different considerations.

The disclosure of financial information is under consideration in parallel consultations concerning the reporting framework. Therefore, we do not deal with this here.

Mandatory information to be disclosed in respect of corporate governance should be no more than what is required by the Corporations Act directors report for limited by guarantee companies. We consider this is principles based and contains basic governance information applicable to most NFP entities.

We would encourage the ACNC to provide education material and guidance to assist those smaller NFPs to complete such information.

12. Should the remuneration (if any) of responsible individuals be required to be disclosed?

We do not support the disclosure of individual remuneration details for individual responsible individuals. Such disclosure would be akin to that of listed entities, which we consider excessive in the NFP context.

Aggregate remuneration disclosures are adequately addressed in the Australian accounting standards, and we would not recommend anything more in the legislation. Accounting Standard AASB 124 *Related Party Disclosures* requires 'general purpose financial statements' for non-disclosing entities (this will include private non-for-profits) to disclose the aggregate remuneration paid to 'key management personnel'. Key management personnel is a term used in accounting standards to refer to 'those persons having authority and responsibility for planning, directing and controlling the activities of the entity, either directly or indirectly, including any director of that entity.'

Those entities that do not produce general purpose financial statements (i.e. they produce special purpose financial statements) are not mandatorily required to make any remuneration disclosures (or related party disclosures). We are unclear in the legislation as to whether special purpose financial statements will continue to be allowed for NFPs registered with the ACNC, and we explore this issue further in our submission on the Exposure Draft.

13. Are the suggested criteria in relation to conflicts of interest appropriate? If not, why not?

We believe that there should be governance requirements for conflict of interest and that the Corporations Act requirements should be adopted. Any additions to this list are unnecessary as it would impose a higher standard on NFPs than on for-profits.

14. Are specific conflict of interest requirements required for entities where the beneficiaries and responsible individuals may be related (for example, a NFP entity set up by a native title group)?

The general conflict of interest principles should apply unchanged to all organisations.

Appendix: Detailed Answers to Consultation Questions

15. Should ACNC governance obligations stipulate the types of conflict of interest that responsible individuals in NFPs should disclose and manage? Or should it be based on the Corporations Act understanding of 'material personal interest'?

It should be based on the existing Corporations Act criteria. This has the benefit of being familiar for experienced directors, and for having existing training and information material available. Additionally, the listing of conflict of interest types is likely to be incomplete and not relevant to every situation therefore it will be a flawed model that is referred to by managers and directors.

16. Given that NFPs control funds from the public, what additional risk management requirements should be required of NFPs?

It is important to acknowledge that not all NFPs control funds from the public or solicit donations.

Risk management of public funds should be overseen (as it is already) by the funding organisation and not added into legislation. Listed companies do not have legislated risk management obligations and they also control funds from the public. Therefore we consider it would be incongruous for this to be applicable to NFPs.

As part of the funding process, funders should be undertaking their due diligence regarding risk associated with potential recipients and should also establish requirements regarding ongoing management of risk by the funded organisation.

17. Should particular requirements (for example, an investment strategy) be mandated, or broad requirements for NFPs to ensure they have adequate procedures in place?

NFPs should not be subject to such additional requirements. Prudent financial management is a core and key role for directors of all organisations and part of their general obligations to apply a duty of care and act in the best interests of the organisation. Therefore there is no need for particular requirements to be mandated. See response to Question 16.

18. Is it appropriate to mandate minimum insurance requirements to cover NFP entities in the event of unforeseen circumstances?

The Institute opposes mandating minimum insurance requirements to cover NFP entities in the event of unforeseen circumstances. Further, we note that it may not be possible for NFPs to be issued with such insurance requirements or it could be so costly as to seriously damage the ability of the entity to service the community. See response to Question 16.

19. Should responsible individuals generally be required to have indemnity insurance?

The Institute opposes mandating indemnity insurance for responsible individuals. Further, we note that it may not be possible for responsible individuals of NFP organisations to be issued with such indemnity insurance or it could be so costly as to seriously damage the ability of the entity to service the community. See response to Question 16.

20. What internal review procedures should be mandated?

Whilst review processes should be encouraged, the nature and extent of such review will depend on the size and nature of the organisation. Hence we would oppose mandating such a requirement for NFPs and only include reference when a similar requirement is included for all entities. See response to Question 16.

Appendix: Detailed Answers to Consultation Questions

21. What are the core minimum requirements that registered entities should be required to include in their governing rules?

This should not be greater than the minimum requirements in existing NFP governance legislation. In practice we support the Corporations Act approach of 'setting minimum rules' and having 'replaceable rules'.

The ACNC should issue model constitutions with the minimum rules and replaceable rules that NFPs can modify according to the needs of their organisation. This will ensure that smaller NFP organisations can easily develop governing documents without recourse to costly legal advice.

22. Should the ACNC have a role in mandating requirements of the governing rules, to protect the mission of the entity and the interests of the public?

The rules should allow the organisation's stakeholders to take action (such as requiring a general meeting) to ensure its aims are being pursued.

We do recommend that all NFP entities be required to lodge a copy of the constitution with the ACNC to be made available to the public through its public portal. However, we would not want to see duplicative lodging requirements for those organisations that already lodge under current Commonwealth or State legislation. Therefore we would expect the ACNC to enter into memorandum of understanding arrangements with existing regulators for this information, to ensure the NFP sector is not burdened with an additional lodging requirement.

23. Who should be able to enforce the rules?

This depends on the type of organisation. In the case of a membership organisation, the rules/constitution comprises a civil contract between the members and the association. Hence it should be a requisite number of members who are able to enforce an organisation's governing rules.

When a dispute occurs in an organisation, perhaps an affordable tribunal can be set up to deal with such matters.

It should be noted that currently the power to make laws with respect to incorporated associations rests with the states. The Commonwealth cannot interfere with the legislative power unless the States agree to this by a formal referral of power. Hence this is a constitutional issue that must be resolved before being able to conclude on this matter.

Further, it is unlikely the ACNC will have the resources or experience to be involved in any significant enforcement activities, in contrast to existing regulators.

24. Should the ACNC have a role in the enforcement and alteration of governing rules, such as on wind-up or deregistration?

See answer to Question 23 above. Further it is likely that any winding up or deregistration would be done in accordance with the legislation under which the entity was incorporated.

25. Should model rules be used?

Yes, as mentioned in Question 21 we support the provision of a 'model' constitution, which can be taken as a base and adapted for use by individual NFPs. However, this area should not be considered while there are existing parallel legal regimes.

Appendix: Detailed Answers to Consultation Questions

26. What governance rules should be mandated relating to an entity's relationship with its members?

We support the provision of a 'model' constitution which, for a membership organisation, should set out its relationship with members. However, we consider that entity legislation and model rules already prescribe rules relating to members in some details. Hence we do not consider additional rules necessary or desirable at this stage.

27. Do any of the requirements for relationships with members need to apply to non-membership based entities?

Relationships with members' requirements are not applicable to non-membership based entities.

28. Is it appropriate to have compulsory meeting requirements for all (membership based) entities registered with the ACNC?

At least one general meeting should be required per annum, which should be particularly useful for member-based entities. However, this should not be introduced while existing parallel legal regimes exist which in most cases will already require such a meeting to occur.

29. Are there any types of NFPs where specific governance arrangements or additional support would assist to achieve in better governance outcomes for NFPs?

We believe that this support is best provided by the ACNC's education and guidance roles rather than legislation. It is hoped that the ACNC will develop guidance statements and provide training as key areas of weakness are identified over time.

Whilst some types of organisations may require assistance to achieve positive governance outcomes, we consider that a principles based approach at the outset will likely ensure that good governance outcomes can be achieved for all organisations.

We note that some regulators, for example ASIC, currently provide extensive information to office holders. We recommend that the ACNC should continue to extend such support to those entities and individuals in the NFP sector.

30. How can we ensure that these standardised principles-based governance requirements being administered by the one-stop shop regulator will lead to a reduction in red tape for NFPs?

The greatest risks to reduction in red tape is that:

- the ACNC goes over and above that required by the Corporations Act; and
- the ACNC's rules and reporting is not accepted by other Government agencies.

While there are non-Government funders, we believe that adoption by the Government funders will provide a model for others.

The development of the ACNC will not achieve the Government's aim if an agency requires additional and alternative reporting. The ACNC needs to become a 'common denominator' and its reporting recognised in regulation, operational guidelines, and contracts. As such, we would prefer to see the ACNC negotiate with state and commonwealth agencies to ensure governance requirements are uniform before developing an ACNC model.

Currently, any requirements developed by the ACNC will result in more administrative burden not less.

Appendix: Detailed Answers to Consultation Questions

31. What principles should be included in legislation or regulations, or covered by guidance materials to be produced by the ACNC?

High-level principles should only be enshrined in statute with any detailed guidance included in extraneous material. Such high-level principles could include, (as long as these are not seen as duplicating that already existing in Commonwealth and/or State legislation):

- duties of responsible individuals
- requirement for a constitution enshrining the entities purpose or objective
- general meeting requirement for at least one meeting per year
- basic governance reporting information, such as that currently included in the directors' report required for limited by guarantee companies

32. Are there any particular governance requirements which would be useful for Indigenous NFP entities?

No comment

33. Do you have any recommendations for NFP governance reform that have not been covered through previous questions that you would like the Government to consider?

Please refer to our opening comments contained in our letter to The Treasury.