



Response to the Treasury Australian
Charities and NFP Commission exposure
draft and Governance Arrangements
Consultation Paper
Joint COSS Submission

ACOSS Paper 182

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This submission is made on behalf of the national COSS network

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The COSSes are the peak bodies representing the needs and interests of service providers and their clients in the non-profit social service sector in Australia. Our members comprise community service providers, professional associations and advocacy organisations.

We provide independent and informed policy development, advice, advocacy and representation about issues facing the community services sector; a voice for all Australians affected by poverty and inequality; and a key coordinating and leadership role for non-profit social services across the country.

We work with our members, clients and service users, the non-profit sector, governments, departments and other relevant agencies on current, emerging and ongoing social, systemic and operational issues.

Executive Summary

This submission is in response to the exposure legislation on the establishment of the Australian Charities and Not-for-profits Commission and the consultation paper on Governance Arrangements in the sector, both released by the Treasury in 2011. We set out particular concerns with respect to:

- i. The over-reaching scope of the enabling legislation for the Commission;
- ii. The lack of clarity about the independence of the Commission; and
- iii. The prescriptive tenor of the governance arrangements proposed.

Beyond this detail of the exposure legislation as drafted, we are concerned by the absence of elements of the legislation that will eventually be included in the exposure draft, for example on governance. Most significantly, we are concerned that the sector's hitherto support for the establishment of a national regulator is being undermined by the rapid process of drafting with key points of departure from the blueprint for a national NFP regulator set down by the Productivity Commission (2010); and by the inadequate amount of time provided for consultation on these changes, notably at a time when many organisations are closed or unable to consult with their members and boards on these important reforms. We conclude by addressing two areas that remain unclear in terms of the legislative framework to enable the ACNC and its commencement.

- i. How can the ACNC's Objects best capture responsibilities to the sector and its clients or stakeholders, beyond those of public accountability?
- ii. How will the extent of the ACNC's powers and its expectations of the sector take account of existing or other responsibilities by charities and NFPs?

Introduction

The establishment of a national, independent regulator for charities and community services has long been championed by ACOSS. We welcomed the Federal Government's announcement in May 2011 to establish the Australian Charities and Not-for-profits Commission and have continued to work with our members, Government and the ACNC implementation taskforce towards realising this objective.

This submission is in response to the exposure legislation on the establishment of the Australian Charities and Not-for-profits Commission and the consultation paper on Governance Arrangements in the sector, both released by the Treasury in 2011. In this submission we set out our key concerns with the exposure draft and consultation paper. We do not seek to propose amendments to their drafting. Rather, we advocate the principles that will ensure the effectiveness of the ACNC and a supportive and engaged sector to work with it. These principles have been developed with our members over several years, including through consultation on and submissions to the Productivity Commission's study into the contribution of the not-for-profit sector (2010), the most recent in a line of processes that have concluded that a national, independent regulator for charities and not-for-profit organisations would be of great benefit.

The tenor and detail of aspects of the exposure draft and governance arrangements paper leave us with grave concerns about the following issues:

- i. The over-reaching scope of the enabling legislation for the Commission;
- ii. The lack of clarity about the independence of the Commission; and
- iii. The prescriptive tenor of the governance arrangements proposed.

Our concerns about the exposure draft are heightened by the absence of elements of the legislation that will eventually be included in the exposure draft, for example on governance. Most significantly, we are concerned that the sector's hitherto support for the establishment of a national regulator is being undermined by the rapid process of drafting with key points of departure from the blueprint for a national NFP regulator set down by the Productivity Commission (2010); and by the inadequate amount of time provided for consultation on these changes, notably at a time when many organisations are closed or unable to consult with their members and boards on these important reforms.

1. Concerns about the exposure draft and governance consultation paper

i. The over-reaching scope of the enabling legislation

The exposure draft proceeds from an assumption that it should be as expansive and comprehensive as possible, capturing the full extent of the powers that the Australian Charities and Not-for-profits Commission is expected to have over all not-for-profit organisations *eventually*. This means that the legislation has significant areas of over-reach, and is unnecessarily heavy-handed with a focus on compliance, when the intention is for a light-touch, principles-based approach to regulation. As a piece of enabling legislation, the exposure draft needs to provide at minimum for the far smaller range of powers and functions that will be required for the ACNC's commencement. But the legislation must strike the right balance between ensuring the ACNC has the full extent of powers necessary

to carry out its intended functions while also supporting the intention ‘light-touch’ regulation by examples of best practice and support to adopt them, rather than punitive compliance approaches. Key examples which demonstrate unnecessary over-reach and a failure to develop a legislative model that is fit for purpose include:

- a. The failure to recognise the reality of operating for many charities and not-for-profit organisations, leading to unnecessarily strict grounds for revocation (on the basis of insolvency); the prohibition to register organisations that have previously registered; and the automatic winding up of organisations if they are de-registered.
- b. The failure of the compliance powers to enable graduated responses and the exercise of the ACNC’s discretion.
- c. The *allocated penalty units*, which are out of sync with the requirements that are already in place in other jurisdictions, meaning that there are harsher/lesser penalties depending on where the ‘paperwork’ is submitted. It is important that the scale of penalty points be aligned across jurisdictions prior to the finalisation of the ACNC Act.

For more detail here, we commend the discussion and recommendations in the submission by the University of Melbourne *Not-for-profit Project*, particularly in terms of how to address the over-reach in the current legislation while establishing the appropriate mechanisms for *enabling* the powers and functions of the ACNC.

ii. The lack of clarity about the independence of the regulator

The sector has long-championed an independent national regulator. In its definitive discussion of this issue, the Productivity Commission (PC) recommended that,

The Australian Government should establish a one-stop-shop for Commonwealth regulation by consolidating various regulatory functions into a new national Registrar for Community and Charitable Purpose Organisations. While ultimately the Registrar could be an *independent statutory body*, initially it should be established as a statutory body corporate or organ in the Australian Securities and Investment Commission (emphasis added).¹

When the Government announced the establishment of the Australian Charities and Not-for-profits Commission during the Federal Budget 2011, it endorsed the importance of this independence by committing that, ‘a commissioner will be appointed to drive all the changes, who will be fully independent and report directly to Parliament via the Assistant Treasurer.’²

Notwithstanding this commitment to independence, the Government determined that the ACNC should share ‘back office functions’ with the Australian Taxation Office (ATO) and not with ASIC. This was unfortunate, given the relevance of ASIC’s regulatory functions to the establishment of the ACNC. More problematic for our members was the perception of a deeply negative culture at the ATO through which the administration of tax concessions for charities and NFPs has operated, particularly where the ATO is unable to recognise the range

¹ Productivity Commission (2010) *Contribution of the Not-for-profit sector*, Recommendation 6.5.

² ‘Making it easier for charities to help those who need it’, joint media release from the Assistant Treasurer and the Minister for Human Services and Social Inclusion, 10 May 2011.

and diversity of activities that constitute legitimate charitable purpose. For that reason, our members have maintained deep opposition to the regulator being situated within the ATO and significant caution about how any shared functions would proceed. While we recognise the pragmatic reasoning for seeking to leverage existing infrastructure while establishing the ACNC, the mechanism for this relationship must serve the Commission's independence.

Nothing in the exposure draft sets out how the independence of the regulator will be asserted or maintained through the ACNC enabling legislation. While this is of particular concern regarding its relationship with the ATO, it is equally relevant for the Commission's relationship with other agencies such as existing regulators.

Of greater concern, there are elements of the exposure draft that indicate a clear lack of independence in core areas such as staffing, as evidenced by the following clause in section 163-5: 'The staff assisting the Commissioner are to be persons engaged under the *Public Service Act 1999* and made available for the purpose by the Commissioner of Taxation.'

This implies that the Commission will not have sole authority over the recruitment and allocation of its staffing, which would be an unacceptable incursion on its independence. As the PC recommended, the statutory independence of the ACNC is critical to its success and to the sector's support for it. The independence of the Commission must be clearly and specifically set out in both its enabling legislation and in any other arrangements that govern its operation.

Key principles necessary to ensure the ACNC's independence

- An independent statutory framework establishing the ACNC's existence and function.
- A dedicated Commissioner appointed to oversee the ACNC. The Commissioner should be appointed by the Executive, not by the public service, maintaining their independence from existing and alternative structures. The legitimacy of this appointment will be strengthened by an open recruitment through advertising.
- An independent advisory body, appointed by the Executive to provide input on sector specific issues. The Productivity Commission recommended that this body be 'drawn from the sector' and 'support cultural change' within other institutions such as the ATO.
- A direct line of report to Parliament, not to a particular Minister. (This does not preclude portfolio responsibilities sitting within a Ministerial office.)
- Adequate funding through the administration of its own Budget, independent of bureaucratic and alternative institutional structures.

iii. A single, prescriptive model of governance

The exposure draft and governance arrangements consultation paper assume the regulation of governance by the ACNC will best be achieved by pursuing a singular, prescriptive model of governance. The structure clearly favoured by the draft and consultation paper is that of a company limited by guarantee. Yet as outlined in the *Final Report on the Scoping Study for a National Not-For-Profit Regulator*, 'organisational governance rules should be proportional to the size of the entities, risk factors and receipt of public and government assistance'. Charities and not-for-profit organisations in Australia is a vibrant, diverse and generally well-governed sector. As outlined by the Australian Institute of Company Directors, 'it would be

wrong to assume that a uniform approach to all sectors would deliver optimal outcomes'.³ It is inappropriate and unacceptable that the regulatory functions relating to governance should presume a single model that best suits all charities and not-for-profits.

Moreover, the function of regulation in respect to governance should be informed first and foremost by the extensive work already undertaken by the sector itself, which has led to the development of best practice models and innovative ways of educating sector organisations on these practices. At the same time we note, while model rules are generally perceived as helpful across the sector, their impact can vary significantly, for example from organisations that have worked extensively on their governance processes to new organisations just starting out.⁴

A set of core principles, applied through a non-onerous approach supported by minimum legislative requirements – as currently applicable to ASX listed companies - provides for a robust framework for establishing a governance model for the not-for-profit sector. The principles developed by the Charities Commission of England and Wales, similar to the Corporate Governance Principles developed by ASX, provide a high level framework adaptable to support local not-for-profit governance. If the Government and the ACNC proceed with developing such high level principles, further consultation should be undertaken to determine what principles should be in place to enable the current mix of not-for-profits to continue working in the community.

It should be noted the current ASX principles and recommendations are 'not prescriptions, they are guidelines, designed to produce an outcome that is effective.'⁵ Also, 'nothing in the Principles and Recommendations precludes a company from following an alternative practice... provided it explains the approach.'⁶ There would be little benefit in subjecting the diverse range of not-for-profit entities in Australia to more onerous requirements than those required for the large companies listed on the Australian Stock Exchange.

However, the questions in the governance arrangements consultation paper hint at the possibility of subjecting the not-for-profit sector to burdensome governance requirements, to a greater extent than applicable to the sector currently and to for-profit companies. For example, question 5 seeks opinion on whether responsible individuals should be required to hold particular qualifications or have prescribed experience. Currently individuals holding specific roles with ASX listed companies, companies limited by guarantee and incorporated associations must at a minimum be adults, and not be precluded from holding such a role by the courts, or other impairment (such as bankruptcy). The not-for-profit sector is wide and diverse, and requiring responsible individuals to hold particular qualifications may well exclude a significant proportion of the population from being involved in the governance of such organisations. At a time when the Government is encouraging diversity in decision making for for-profit entities, we do not recommend placing such constraints on the sector.

³ Stephen Cole, AICD Board member quoted in *Company Director – Volume 27, Issue 07* p.34

⁴ If, as discussed in the consultation paper, Victoria is to be used as an example of model rules on governance, it is important to be mindful that Victoria is currently reviewing the *Associations Incorporated Act* and the model rules may change as a result.

⁵ ASX Corporate Governance Council *Corporate Governance Principles and recommendations with 2010 Amendments (2nd Edition)* p. 5

⁶ ASX Corporate Governance Council *Corporate Governance Principles and recommendations with 2010 Amendments (2nd Edition)* p.6

It is clear, however, responsible individuals should be undertaking their work in the best interest of the organisation (commonly known as fiduciary duty). Current changes proposed to the Victorian *Associations Incorporation Act 1981* look to codify such duties in legislation. As outlined by PilchConnect there is benefit of codification of already accepted common law principles.

PilchConnect supports the introduction of a duty to pursue the purpose of the incorporated association, and the inclusion of duties of care and diligence, good faith and proper purpose, and the duty to prevent insolvent trading. It is generally accepted that these duties already apply to Committees of Management members of incorporated associations by virtue of the common law. PilchConnect provide governance training to incorporated associations based on this approach. However, the codification of the duties in the Act will remove all doubt.⁷

Questions 16-19 seek input regarding the level of insurance and risk management procedures. We seek assurance the requirements for risk management and insurances, including but not limited to governance arrangements, will not be more onerous than for other reporting organisations, as articulated in the governance principles of the Australian Stock Exchange. As outlined by the ASX, 'Each company will need to determine the "material business risks" it faces.'⁸ It is accepted that governments and philanthropic donors may require agencies they work with to have certain levels of insurance in place and to meet certain standards regarding service delivery standards. However this should remain an issue for the funder and organisations, and not regulated for all not-for-profits through the ACNC. For example, our experience is that some level of insurance is highly recommended, in particular public liability and indemnity insurance for governing Boards. However we do not accept that this is an area to which mandatory requirements should be attached, particularly not through the ACNC's enabling legislation. Setting standards around risk management falls appropriately within the function of a principles-led regulator, working in consultation with the sector itself.

At its heart, the governance arrangements discussion paper appears to confuse the role of governance requirements. Governance is the structures and processes by which an organisation sets goals, monitors performance, maintains viability and ensures compliance with legal requirements and ethical standards. Organisations should be able to operate in the best way that suits their values, members and/or clients while meeting basic requirements. If they then wish to deliver certain services and/or enter into contractual relations with government or other bodies, the requirements of such obligations, such as insurance, investment strategies, and internal review processes, should be established as required.

The role of the ACNC, as already carried out by Registrars-General and ASIC, should be oversight and good-practice guidance for the establishment and governance maintenance of not-for-profits. Organisations such as the Councils of Social Service, PilchConnect, the Australian Institute of Company Directors, and Management Support Online (to name just a few working in the community sector) already provide significant support and resource in developing good-practice governance procedures for not-for-profits. Equally important are

⁷ PilchConnect *Submission to Consumer Affairs Victoria on the Associations Incorporation Amendment Bill 2010* p.7

⁸ ASX Corporate Governance Council *Corporate Governance Principles and recommendations with 2010 Amendments (2nd Edition)* p.33

established standards such as the Good Governance Principles (AS 800-2003) as part of quality accreditation requirements and it is important that these are incorporated by the ACNC within its governance standards. This is neither mentioned in the governance arrangements paper nor foreshadowed in the exposure legislation.

2. Outstanding questions about the enabling legislation for the ACNC

Beyond the concerns outlined above, some key questions about the establishment of the ACNC remain unclear from the materials released to date.

i. How can the ACNC's Objects best capture responsibilities to the sector and its clients or stakeholders, beyond those of public accountability?

The widely recognised value of the sector socially and economically, and the support for the regulator as a mechanism to assist the sector further, are clearly absent in the tenor of the legislation as drafted. The Objects illustrates this best, containing a tension between the objectives of maintaining and improving public trust and confidence in the sector; supporting the sector by redressing overly burdensome and ineffective regulation; and establishing a satellite institution to support ATO and Treasury efforts to constrain tax concessions in the interests of revenue. There is the strong potential for disharmony between these purposes, and we question the merit in presenting them as equal priorities.

While the preservation of public trust and confidence in the charity and NFP sectors is an important policy objective, the current drafting sidelines the history of advocacy for the regulator *by the sector* in the interests of supporting and promoting the sector's performance. The fact sheets that have been developed alongside the exposure draft detail the education and support to the sector that will be the largest functions of the ACNC, yet nowhere is this apparent in the exposure draft and the legislation provides no guarantee that this will be the case. Unless these functions are made explicit in the purpose and principles in the Act, the sector will continue to harbour concerns that the ACNC is simply a punitive mechanism for compliance.

The Object of the exposure draft is defined narrowly in the following way in section 2-5:

The object of this Act is to promote public trust and confidence in not-for-profit entities that provide public benefits.

We recognise that the matter of public confidence is central to the Commission's purpose; albeit not the priority matter for which our members have expressed their support for the Commission. We are concerned at the narrow way in which this object is conceived and the implication that the way the sector currently conducts itself is not worthy of the public's trust and confidence.

The exposure draft sets out the following to further its object:

(i) promote the good governance, accountability (to donors, to governments and to the public generally) and transparency of such entities (including through the provision of educational information to them and the provision of information to the public about them);

- (ii) minimise regulatory duplication and simplify such entities' interactions with governments; and
- (b) this Act establishes a process for registering and regulating such entities.

As important as good governance is for accountability to funders and the public generally, it is equally important for the interests of those that charities and NFPs seek to serve. For example in community services, these are the clients and communities in which services are operating. The promotion of good governance and accountability should be in the interests of the clients or beneficiaries or users of charities and NFPs, as much as the funders and public generally.

ii. How will the extent of the ACNC's powers and its expectations of the sector take account of existing or other responsibilities by charities and NFPs?

One of the drivers of the sector's support for the establishment of the ACNC has been the intention to reduce the duplicative, ineffective and overly burdensome regulation organisations currently face. ACOSS has supported the National Roundtable of Nonprofit Organisations' call on this point, outlining the key objective being *not necessarily less but better regulation of the sector*. We understand that the initial establishment of the ACNC will not necessarily lead to reduced duplication in the first instance and may in fact add to the regulatory burden as other regulatory bodies await the process of nationalising regulation, particularly in the states and territories. An adequate transition/harmonisation timeline needs to be developed and communicated and it is vital that this includes transitional provisions.

For those organisations that may be regulated by their own states and territories (such as Incorporated Associations or co-operatives), who are also receiving tax concessions there appears to be a lack of clarity regarding if they are subject to registration by the ACNC. The default position should not be that these organisations lose their tax concessions if they do not become registered. Government needs to provide clarity on this matter, in conjunction with the States and Territories – otherwise there will be a significant duplication regulatory burden for a significant number of organisations. Yet there is currently no binding commitment from states and territories to hand over regulatory powers to the ACNC and the sector is understandably concerned to ensure that any 'transition' period through this phase does not continue indefinitely. Further clarity regarding the process and timeframes to address this, such as a formal agreement through COAG, will be key in this regard.

The sector seeks further clarification about how the burden of unnecessary and ineffective reporting or acquittal requirements will be reduced through the establishment of the ACNC. How will the burden of reporting be reduced, given responsibilities to other organisations such as funders and to members; and in the context of standards and accreditation processes? What will be the relationship between the governance rules administered by the ACNC and the common law (for example directors' responsibilities following the Centro case), or an organisation's constitution?