



29 August 2008

Mr John Hawkins
Committee Secretary
Senate Economics Committee
Department of the Senate
PO Box 6100
Parliament House
CANBERRA ACT 2600

Dear John

Enquiry into the disclosure regimes for charities and not for profit organisations

The Institute of Chartered Accountants in Australia welcomes the opportunity to make a submission to the Senate Economics Committee on disclosure regimes for charities and not for profit organisations (NFPs).

We represent approximately 46,000 Chartered Accountants and 12,000 graduate students enrolled in our CA Program. Many of our members are involved in the not for profit sector in a paid capacity or as volunteers and are passionately interested in the topic from the perspective of both preparers and users of the financial and other reports prepared by these NFPs, if the responses we receive whenever we seek feedback on not for profit issues are a guide.

Very little has changed over the past decade in the NFP regulatory and reporting environment, despite numerous recommendations from the Institute as well as others with interest in this sector that action be taken to simplify a complex environment. Our detailed submission, which follows, expresses our view that there are indeed significant problems with the current disclosure regime for NFPs and that a single national regime would enable many of these problems to be effectively addressed. Our submission also makes suggestions as to how such a national regime might be achieved.

If you require further information on our submission please contact Ms Kerry Hicks at the Institute on 02 9290 5703 or at kerry.hicks@charteredaccountants.com.au.

We would be pleased to elaborate our views in a hearing before the Committee.

Yours sincerely

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Summary of recommendations

1. A single national disclosure and regulatory regime for not for profit organisations (NFPs) should be introduced.
2. The issue of a single disclosure and regulatory regime should be referred to the Minister for Superannuation and Corporate Law for development in the context of the Green Paper on financial services issued on 3 June 2008.
3. The regulatory regime should operate under a tiered system on the basis of revenue thresholds.
4. There ought to be a single, separate accounting standard for NFPs, with appropriate recognition for small, non-complex NFPs.



ENQUIRY INTO THE DISCLOSURE REGIMES FOR CHARITIES AND NOT FOR PROFIT ORGANISATIONS

Introduction

The Institute and its members have a long association with the not for profit sector. Many of our members are active in either a paid or voluntary capacity as treasurers, directors or auditors of these types of entities and regularly struggle with the disparity of requirements and obligations that are imposed on them by the various disclosure frameworks under which these entities operate. An additional complication is the difficulty of reconciling how these frameworks could or should compare with the disclosure regimes imposed on the 'for profit' sector. Our members want to ensure that the material they produce for their relevant NFP complies with their professional standards as members of our Institute and represents 'best practice' financial reporting and governance. However this goal is hard to achieve.

These difficulties were exacerbated by the decision of the Financial Reporting Council (FRC) to move to international harmonisation of accounting standards in 2002, along with the decision by the Australian Accounting Standards Board (AASB) to continue with sector neutral accounting standards. This necessitated the need for the introduction of NFP specific requirements into the 'for profit' international accounting standards to ensure the 'capital markets' based requirements of international standards did not seriously impact on this sector. This has provoked significant professional debate about the definition of NFPs and the appropriate accounting treatments and disclosures for these entities. A NFP project providing guidance on the definition is currently on the work programme of the AASB, although there are currently no moves in the development of a separate accounting standard applicable to NFPs.

The difficulties our members were facing in this area led the Institute to commence a research project in 2005 which sought to provide assistance to the not for profit sector in applying NFP reporting requirements. The results of this report were published in 2006 as [*Not for profit sector reporting: a research project*](#), a copy of which is attached.

In 2007, we published a further report titled [*Enhancing not for profit annual and financial reporting*](#). These two reports provide extensive guidance on NFP reporting and contain summaries of the relevant requirements that were designed to assist NFPs in fulfilling their reporting requirements. The reports include a set of specimen accounts and commentary on the application of accounting standards to these types of entities.

In the last twelve months we have observed that, in addition to the AASB, other regulators have begun addressing the needs of the 'not for profit' sector. As a result we have made submissions on the following proposals:

- The AASB's ITC 14 *Proposed Definition and Guidance for Not for profit Entities*
- The NSW Government's draft *Associations Incorporation Bill 2008* - a project to update the out dated requirements of this legislation
- The Commonwealth Treasury paper *Financial Reporting by Unlisted Public Companies*
- The Tasmanian Department of Justice proposals on *Tasmanian Associations Incorporation Act 1964 – Proposal to Exempt Small Incorporated Bodies from Auditing Requirements* – a proposal to exempt small associations from an audit requirement
- The Victorian State Services Authority's *Review of Not for Profit Regulation*
- The review of the Victorian *Associations Incorporations Regulations 1998*

The papers we produced as part of these projects are also attached.

Internationally there is a concurrent debate within the accounting profession on the disclosure regime that is appropriate to small and medium enterprises that operate in the 'private' sector. The International Accounting Standards Board (IASB) is attempting to provide a simpler international standard for small and medium sized entities, recognising that the current suite of international standards is designed for large 'profit based' entities in the world's capital markets. Therefore the current suite of international standards (which Australia adopts for all reporting entities) can impose significant costs, without associated benefits, on smaller entities.



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The Institute has been extensively involved in this project, originally called IFRS for SMEs and now called IFRS for Private Entities. We organised a roundtable discussion of interested parties, participated in AASB roundtable discussions and participated in the field testing process. We made a submission to the IASB and a further submission to respond to the AASB on ITC 12 *Request for Comment on a Proposed Revised Differential Reporting Regime for Australia* and IASB Exposure Draft of a Proposed *IFRS for Small and Medium-sized Entities*. Preparation of the Australian submission necessitated us to seek and consider feedback on appropriate NFP financial reporting requirements, since the Australian proposal was to make this international standard applicable to both 'for profit' and 'not for profit' entities.

It is clear that there are already a number of interrelated proposals for reform on the table at present. While we are keen to encourage reform in this area, it is vital that the State and Federal governments and the Accounting and Auditing standard setting boards work together in this area, monitoring and providing input to each others' proposals so that the resulting regime is consistent and easy to apply. Any financial reporting or auditing requirements imposed by government must be workable within the constraints of the accounting, auditing and professional/ethical standards that our members are bound by. The Institute believes that it is only within this context that real reforms will be achievable, enabling NFPs to provide their services in a suitably robust framework of governance and reporting.



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Relevance and appropriateness of current disclosure regime

Our primary criticism of the current regime is that it is too complex and fragmented.

The variety of legislation that applies to NFPs contributes to this complexity and fragmentation. Charitable NFPs are subject to corporate and fundraising legislation that varies from jurisdiction to jurisdiction. Sporting NFPs and other NFPs (such as membership services organisations) are subject to the same variety of corporate legislation.

Not for profits may be, inter alia, companies limited by guarantee, statutory bodies set up under their own legislation or charter (such as our Institute), trusts, co-operatives and incorporated associations. Statutory bodies may fall under the Corporations Act or under their own legislation. Companies limited by guarantee are governed by the Corporations Act. Associations are regulated by state offices of fair trading or consumer affairs under state-based legislation.

Appendix 1 presents a table of the most common different reporting requirements that may apply to not for profits, i.e. those affecting associations and companies limited by guarantee. Please note that this table only covers financial reporting and auditing regulation. There are also State laws on fundraising or gaming and racing that have to be complied with where the 'not for profit' runs raffles and other events to raise money. The decision diagrams attached behind Appendix 1 illustrate the difficulty of a NFP entity in determining their reporting obligations.

Our secondary criticism relates to the inconsistency of legislation and the currency the legislation.

Firstly, the legislation governing these various structures is both inconsistent between the types of legal structures and inconsistent within the structures. For example Incorporated Associations are controlled by individual state legislation, much of which is inconsistent when compared state to state. NFPs using this incorporated association structure now increasingly find themselves operating across state boundaries and therefore their managers and advisers need to be familiar with a number of differing regulatory regimes. In fact the results can be so complex that some advisers in fact recommend a 'company limited by guarantee' structure (regulated by ASIC as part of the *Corporations Act*) in preference so that the NFP only needs to worry about one piece of national legislation. However NFP's obligations under the *Corporations Act* are significantly different and in many cases more onerous than under associations legislation. And these additional costs may be to the detriment of the NFP's activities.

Secondly, the legislation that governs not for profits is often out of date, having not kept pace with developments in accounting practice and corporate governance. These issues are less of a problem when dealing with NFPs regulated under the *Corporations Act*, as the *Act* is regularly updated, but entities under this structure struggle with the opposite problem of having requirements imposed on them that are not really appropriate to their circumstances (the *Act* being essentially designed for corporate profit making entities).

The growth of the 'company limited by guarantee' structure as a vehicle for NFP activity is evidenced by the information contained in the 2007 Commonwealth Treasury paper *Financial Reporting by Unlisted Public Companies*, extracts of which we reproduce below. The Treasury paper includes a breakdown of companies limited by guarantee by size.

'There are approximately 11,000 companies limited by guarantee registered under the *Corporations Act 2001*. This figure has been growing at 6 per cent per annum in recent years. Companies limited by guarantee do not have the power to issue shares to members. Rather, each member agrees to pay an amount specified in the company's constitution in the event that the company goes into liquidation. In most cases, the amount of this guarantee is nominal. As indicated in Table 1, the size of these organisations is predominately small with close to 70 per cent having operating revenue of less than \$1,000,000.



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Table 1: Size of companies limited by guarantee¹

	Revenue (%)	Cumulative Total: Revenue (%)	Assets (%)	Cumulative Total: Assets (%)
Less than \$200,000	41	41	35	35
Between \$200,001 and \$500,000	13	54	10	45
Between \$500,001 and \$1,000,000	14	68	18	63
Between \$1,000,000 and \$12,500,000	28	96	30	93
Between \$12,500,001 and \$25,000,000	2	98	2	95
Greater than \$25,000,000	2	100	5	100

These results are consistent with the findings of a survey of companies limited by guarantee in 2002 by The University of Melbourne² which found that 64 per cent had revenue of less than \$1,000,000. This survey also found that almost all companies limited by guarantee have a not for profit motive.³ They included sports and recreation related organisations (21 per cent), community service organisations (19 per cent), education related institutions (15 per cent) and religious organisations (10 per cent).¹

It should be noted that some companies limited by guarantee are quite small, and some associations have grown to the extent that they are larger than some companies limited by guarantee and have interstate branches.

It is also worth noting that the above statistics only represent 11,000 of the estimated 700,000 NFPs that are believed to exist in Australia. Therefore the work that Treasury is doing in this area on unlisted public companies as part of the *Improving Corporate Reporting and Accountability* project will have a significant impact on entities under the *Corporations Act*, but certainly not on the entire NFP sector.

The paper published by Treasury in 2007 specifically asked respondents a question 'Do you consider there is a need to harmonise the financial reporting requirements of companies limited by guarantee and incorporated associations to provide a consistent reporting framework for not for profit entities in Australia?'. The submissions that are publicly available overwhelmingly support harmonisation. However it seems that the Treasury recommendations derived from the discussion paper, which are expected to be issued in September this year, will not be addressing this area. This is extremely disappointing to the majority of those involved in the NFP sector.

¹ Based on sample data provided by ASIC on 3 November 2006.

² Woodward and Marshall, A Better Framework: Reforming Not for profit Regulation, The University of Melbourne (available at: <http://ccisr.law.unimelb.edu.au/index.cfm?objectId=017B1CA1-B0D0-AB80-E29B8B41F029F841>)

³ A small number of companies limited by guarantee reported having a profit motive in the survey; however, the authors of the survey attribute these results to companies misinterpreting the question.



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Suggestions for change

In our view, the private not for profit sector needs to be seen as a continuum rather than analysed by its individual structures as is currently being done.

Given all the complexities that exist, we do not consider that it is appropriate to use the underlying structure of the entity as the determinant for how the NFP entity reports. Instead we propose a system that is more aligned with the needs of the users of the reports, those managing the entity, its members and those who donate money to the entity, i.e. a system which is based on the accountability of the NFP to its stakeholders.

A single regulatory regime

We therefore suggest that there should be a single regulatory regime covering all NFPs, however constituted, and based on size thresholds. The Institute has already made this recommendation in various papers and submissions that are attached including the 2007 submission to Commonwealth Treasury referred to above.

We believe this regime should be overseen by a single national regulator and ASIC is the obvious candidate. However if this task is given to ASIC, a separate division catering solely to the needs of NFPs should be created as ASIC's resources are already stretched supervising the larger companies in the 'for profit' sector and the needs of NFPs are sufficiently different. This separate division should not have to compete for funding with ASIC's 'for profit' activities.

While we advocate the creation of a separate division within ASIC for NFPs, we suggest that the AISC database continue to be used as the official register for all types of entities, as the hardware and software is already in place. If there is only one database, individuals with directorships in both the 'for profit' and not for profit sectors will be able to be cross referenced.

In making this recommendation, the Institute acknowledges that there would be significant implementation and transitional issues to be resolved if a single harmonised regime were to be adopted. This is inevitable given the current plethora of arrangements. However, our experience and expertise tell us that this would be the most effective and sustainable solution.

We suggest that the issue be referred in the first instance to the Minister for Superannuation and Corporate Law, and be considered in the context of the full transfer of responsibility for financial services from the States to the Commonwealth, as set out in the Green Paper released on 3 June 2008.

In establishing a new disclosure regime a primary consideration must be that it be applicable to both the smaller not for profits who are staffed by volunteers who are not necessarily financially experienced as well as to the larger ones who have full time directors and financial staff. This is particularly important in country areas where financially experienced volunteers are likely to be harder to find than in the cities (as evidenced by the difficulty of rural and regional Australia to find registered company auditors). A regime that is not cost beneficial will have a substantial negative impact on this sector.

In our submission to Treasury we suggested that regulation for the smaller end of the spectrum should focus on ensuring that not for profits have adequate governance structures in place, and those in a management role understand their responsibilities. We repeat these comments for the purpose of this submission.

While any disclosure regime covering smaller not for profits must be simple enough for volunteers to follow, we do consider that some level of oversight by a regulator is vital. The community at large has expectations of a high level of accountability on the part of those handling funds donated by members or supporters for specific purposes. There is also a need to ensure that NFPs report consistently to enable the users of these reports to be able to make informed decisions.

Again, compliance obligations on not for profits should be kept as cost-effective as possible to ensure that these entities spend their funds on their objectives rather than on regulatory compliance.



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As we see it, three main models are possible:

1. All NFPs could be brought within the scope of the *Corporations Act*
2. NFPs should be excluded from the *Corporations Act* and operate under specific legislation, that would cover associations and other NFPs however constituted. We suggest that this could be achieved in one of two ways:
 - a. By the States enabling legislation that mirrors a Commonwealth law (as was done with the Companies Code that applied from 1981 to 1989.)
 - b. By the States ceding responsibility for regulation of NFPs to the Commonwealth, enabling them to be regulated by one piece of Commonwealth legislation in the manner of the *Corporations Act*
3. Companies limited by guarantee could remain under the jurisdiction of the *Corporations Act*, while associations and other NFPs would be regulated by state bodies using a nationally agreed consistent framework (as in 2a above). Thresholds would be consistent between the *Corporations Act* and state associations legislation to ensure that arbitrage opportunities do not arise between legal structures.

Our preference is for either 2a or 2b.

In our view Option 1 is undesirable for several reasons. The *Corporations Act* contains many requirements more relevant to a 'for profit' organisation that would be seen as onerous for a NFP.

Option 3 would require maintaining two related regimes governed by both State and Commonwealth legislation and would be cumbersome, much like the current systems that we are seeking to reform.

Specific legislation applicable to NFPs, as described in 2, regulated by a specialised unit within ASIC, who could acquire expertise in the area and could also take on functions such as education would be seen as preferable.

This specific legislation would replace the plethora of State based associations and fundraising laws, not simply add another tier of regulation.



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Tiered regulatory structure for reporting, lodgement and audit

In our submission to Treasury made in August 2007 (attached) we suggested a possible tiered regulatory structure, with the smallest entities only required to lodge basic financial information as long as an adequate corporate governance structure is in place. This suggestion could be extended to embrace all not for profits, however constituted.

We also suggested that not for profits below a certain threshold should be subject to an enhanced governance regime designed to ensure that those charged with governance are in a position to sign a solvency resolution similar to that required by small proprietary companies under S347A of the *Corporations Act*. There is precedent for a governance based approach in the criteria ASIC uses in granting relief from the requirement to have an audit under RG 115 *Audit Relief for Proprietary Companies*. Before granting relief, ASIC expects to see that the company is well run and in a sound financial condition.

We suggest that the NFP sector be divided into three tiers to determine the extent of their reporting and audit obligations. The tiers we suggest in this submission are lower than those we suggested to Treasury in 2007 as a result of further consultation with members and other professional bodies.

1. Entities with >\$2,000,000 revenue – these should apply Australian Accounting Standards and have an audit by a registered company auditor.
2. Entities with revenue >\$500,000 but less than \$2,000,000 – these should apply Australian Accounting Standards and could choose to have either a full audit or a review
3. Entities with revenue < \$500,000 – these would lodge simplified unaudited financial information as described in our submission on *Financial Reporting by Unlisted Public Companies* (attached) but be subject to an enhanced governance regime.

We have chosen revenue as the critical factor. In the NFP sector, staff numbers may not be reliable because of the sector's reliance on volunteers. Similarly, total assets may not provide a meaningful cut-off figure as assets are often held at very old historic costs where the NFP does not see the necessity of commissioning an up to date valuation.

In combining the various NFPs under one regulator, we would strenuously argue against mandating a single reporting date as happens with companies. As we noted in our submission on the NSW Government's draft *Associations Incorporation Bill 200*, such a requirement would place unnecessary pressure on NFPs and their advisers.



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Other measures that can be taken by government

Much has been written about the inadequacy of financial reporting by NFPs, in particular that donors to charities are unable to discern the proportion of their donation that goes to charitable objectives and the proportion that goes to administration. It is clear from the results of the Choice Survey *Charities' accounting can disguise true costs*⁴ that donors want to know about the proportion of a charity's resources that are devoted to its different activities and be confident that the funds they donate are being used for charitable purposes.

One accounting standard

The Australian Accounting Standards relevant for not for profits currently are the 'for profit' standards with additional Australian paragraphs inserted for NFPs. We do not agree with this approach. Adding additional Australian paragraphs to the International Financial Reporting Standards is confusing to the international community (who see this as amending IFRS standards) and imposes additional burden and requirements on the NFP sector. NFPs need to be familiar with the full suite of IFRS standards so they can determine their applicability or not.

The AASB is looking to review the requirements, although they are bound by the Financial Reporting Council direction of sector neutrality. They are currently proposing NFPs to have the option of complying with:

- full IFRS
- IFRS for private entities
- Full IFRS recognition and measurement with reduced disclosures

These standards will be 'for profit' standards with additional 'Australian' paragraphs that are deemed to be particularly relevant for NFPs.

To remove confusion and complexity associated with the continuation of the current approach, (for profit standards with additional paragraphs), a separate NFP conceptual framework along with a separate NFP standard is needed. Member feedback that we have received repeatedly requests a specific NFP accounting standard, responding to the particular needs of the sector.

The need for such a framework has been the subject of discussion for some time. It is now more than ten years since the Industry Commission⁵ recommended:

'The Commonwealth Government should provide funds to the Australian Accounting Standards Board and Public Sector Accounting Standards Board to develop within two years suitable accounting standards for Community Social Welfare Organisations (CSWO).

The development of specific accounting standards for the sector would improve accountability of CSWOs. It would help donors and the public generally to compare the performance of CSWOs; governments to assess the effectiveness of CSWOs in providing services for which they are funded; and CSWOs to minimise the costs of accounting and reporting.'

In our view, the development of this NFP specific approach to stakeholder reporting would overcome the financial reporting complexity resulting from the combination of the *Corporations Act*, incorporated associations and fundraising legislation, and sector neutral Accounting Standards.

⁴ www.choice.com.au

⁵ Charitable Organisations in Australia, Industry Commission Report No. 45 16 June 1995, page xiii



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We consider that many of the issues raised by Choice could be addressed by consistent disclosure requirements in a tailor-made accounting standard for NFPs. The Institute's publication *Enhancing Not for Profit Annual and Financial Reporting*⁶ gives examples of how NFPs can use reporting, beyond that which is required under current accounting standards, to communicate effectively with their stakeholders, and has been well received. An accounting standard, developed specifically for this sector would, however, be more effective in ensuring good financial communication in this sector.

Such an accounting standard could also include specific reporting requirements relating to government grants. These requirements would have been agreed to by all government departments – federal and state – so that the financial report would be able to be used to satisfy the needs of all stakeholders. Currently significant burdens exist on NFPs who need to meet different expectations from different government departments when reporting on the acquittal of grants received.

Examples of other reporting issues that are not addressed by current NFP requirements in accounting standards include:

- operating statement disclosures (for example, the amount spent on fundraising and administration)
- segment reporting for NFPs
- reporting by management on the extent to which the entity has met its objectives
- governance

The International Accounting Standards Board's (IASB) proposed IFRS for Private Entities may turn out to be a suitable product for our Australian Accounting Standards Board to adapt for the NFP sector. However, we will not see the final version of this document until the first half of 2009.

In line with our previous proposals, we would advocate the use of a NFP standard for those entities with assets/revenue >\$500,000. In the interests of cutting red tape, we suggest that small NFPs should be allowed to provide something much simpler on an unaudited basis similar to the old Key Financial Data on the Annual Return. However, if such a model were to be introduced for all NFPs, we consider it is imperative that there remains an option for a specific percentage of members or the regulator to request an audited financial report prepared in accordance with Australian Accounting Standards (similar to the requirements imposed on small proprietary companies under s293 and s294 of the Corporations Act).

⁶ <http://www.charteredaccountants.com.au/A118424100>



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Answers to Specific Questions Asked in the Committee's Background Paper

Concerns about the NFP sector

- i. **Are current disclosure regimes for not for profit organisation adequate?**
- > **If so, why (taking into account concerns such as those expressed by *Choice*)?**
 - > **If not, why not?**

In our view the current regime is inadequate. The complexity of the reporting and compliance regime for NFPs results in a waste of all forms of scarce NFP resources – funds raised by donation or received as grants, volunteer time, and management time – and might act as a deterrent to individuals who wish to volunteer their time to assist NFPs. If the NFP sector is to continue to make a valuable contribution to the Australian economy, its regulatory and reporting environment needs to be simplified.

The Choice article and the Institute reports make recommendations for improvements in disclosure by NFPs.

Feedback from our members in recent times indicates that the sector would like national legislation containing consistent reporting and assurance obligations as well as its own accounting standard in order to achieve consistency of accounting and reporting across the sector and so improve accountability. Further we recommend that the AASB be assigned the task of developing a 'private sector NFP' specific financial reporting framework drawing on similar frameworks in UK and US.

- ii. **What would be the potential advantages and disadvantages for not for profit organisations of moving towards a single national disclosure regime? How might any disadvantages be minimised?**

The main advantage for NFP organisations would be simplicity and consistency for entities and practitioners working across State boundaries. Any disadvantage for small NFPs by having standardised requirements that might be more complex than the reports they are currently providing can be mitigated by use of thresholds as we have described in the section above entitled *Suggestions for Change*. This improved regime would also have the significant advantage of providing substantial communication benefits to the contributors to these organisations.

- iii. **Would a standardised disclosure regime assist not for profit organisations who undertake fundraising activities, and who operate nationally, to reduce their compliance costs if it meant that they would only have to report on fundraising to a single entity (rather than reporting to each state and territory)?**

Our understanding is that having one disclosure regime would assist NFPs that operate across state boundaries and their advisers. The impact on compliance costs would be dependent of the requirements under current State legislation. In some cases, depending on the size of the entity, compliance costs may increase and in others compliance costs may reduce.

- iv. **If there was to be a nationally consistent disclosure regime, should it apply across all not for profit organisations or should different regimes apply to different parts of the sector? For example, should charities be treated differently than other not for profit entities?**

We were present at the Roundtables held by the Australian Accounting Standards Board to discuss ITC 14 *Proposed Definition and Guidance for Not for Profit Entities* at which it became very clear that the NFP sector is diverse and difficult to define.

At this stage we recommend segregating the NFP sector by size. See our section entitled *Suggestions for Change* for indicative size thresholds.



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While subdivisions of the NFP sector are difficult to define, the main distinction would be those that currently fall within state charitable legislation, which may require additional legislation and accounting disclosure requirements in the annual accounts. These state-based requirements relating to charitable fundraising etc should be included within the new national legislative framework, rather than exist in separate requirements of the Law.

The new legislation should include a clause requiring a review of its effectiveness after say three years of operation and the regime may be fine tuned at that time.

- v. **If different regimes were to apply to different parts of the sector, how would this be determined and why? For example, would it be based on classifications, i.e., as a charity or deductible gift recipient, or would different regimes apply to different organisations based on their annual financial turnover or staffing levels (or some other proxy for size and/or capacity)?**

See above.

Calls for regulatory reform

- i. **Does there need to be regulatory reform of the not for profit sector?**
If not:
- > **Why not?**
 - > **Are there alternative (non regulatory) measures that might be taken by government and the not for profit sector to address some of the concerns raised by groups such as *Choice* about the governance, standards, accountability and transparency of not for profit organisations who use public and/or government funds?**
 - > **Who should be responsible for progressing and/or funding these measures?**
 - > **How might the uptake of any such measures be monitored?**

We strongly support legislative reform of this sector. We consider that Treasury would be best placed to propose regulatory reform in this sector, given the extent of intelligence they have already gained through the submissions received in relation to their 2007 consultation process.

In order to prevent duplication of resources, we consider that ASIC is best placed to regulate the sector, as mentioned in the section *Suggestions for Change*. Although we note that they currently have little expertise in this area. Therefore we would recommend a specialist unit be set up within ASIC to deal with the special needs of NFPs.

This unit could be funded in a variety of ways. Firstly, the fees received by state governments through the operation of the current state legislation could be charged by ASIC. For an example of State charges in NSW, see Appendix 2. However this is unlikely to meet the costs of regulating this sector and to impose additional costs on this sector would be untenable. Other measures could include reduction of state government assistance, given that the states would not be bearing the costs of regulating this sector and investigation into the use of one of the Commonwealth funds such as the Financial Industry Development Account of the ASX National Guarantee Fund.

If so:

- > **What should be the objectives of reform?**

As we described above under the section *Relevance and appropriateness of current disclosure regime* we believe that the current requirements are too fragmented and complex.



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The main objective should be simplification to achieve a consistent national regulatory framework for NFPs which allows these entities to clearly and consistently demonstrate their accountability to their stakeholders through high quality disclosure frameworks.

- > **Are there minimum requirements that must be met in order for a national regulatory system to be worthwhile?**
- > **Should regulatory reform apply to the whole not for profit sector, or only to segments of the sector? For example, to charities; to bodies receiving public funds, whether through grants or tax concessions; to bodies with a financial turnover about a specified threshold etc?**

In our experience many NFPs receive government assistance in some form and those that do not still need to display a high level of accountability as they may be soliciting donations and sponsorship from the public.

We suggest that regulatory reform should apply to the whole sector but that financial thresholds should be used to segregate the sector, so that small NFPs that are properly managed are subject to less onerous requirements.

- > **Where should the impetus for reform come from? Who should drive reform?**

As we support a nationwide consistent framework in our view the impetus should come from the Commonwealth. The Treasury is currently driving the push to reform unlisted public companies and in our view this should be part of a comprehensive reform of the NFP sector.

We suggest that the issue be referred in the first instance to the Minister for Superannuation and Corporate Law, and be considered in the context of the full transfer of responsibility for financial services from the States to the Commonwealth, as set out in the Green Paper released on 3 June 2008.

In the financial reporting area, the impetus should come from the Financial Reporting Council (FRC) which has strategic oversight of the activities of the Australian Accounting Standards Board (AASB) who would develop any future accounting standard for NFPs.

- > **What sort of consultation should be conducted on the nature of any regulatory reform? How could input be facilitated from across the broad range of organisations that comprise the not for profit sector?**

Eliciting feedback on reform proposals from affected parties is always difficult. However there are a number of umbrella bodies with significant interests in this sector who should be able to coordinate feedback. Our Institute, for example, can publicise proposals to our members who in turn are involved in a large number of NFPs as employees, auditors and volunteers. Similarly in the sporting field, the AFL, ARU, etc are likely to have a mechanism in place to communicate with their clubs at grass roots level.

- > **Are there particular models of regulation and/or legislative forms that would be useful, in the Australian context, in improving governance and management of charities and not for profit organisations and in catering for emerging social enterprises? What are the perceived advantages and/or disadvantages of these models?**

We understand that there is support for a regulatory system such as that in place for charities in New Zealand and the UK.



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ii. Should there be a single national regulator for the not for profit sector?

In our view, there should be such a regulator.

If not,

- > **Why not? What would be the disadvantages in having a single national regulator?**

If so:

- > **Should a national regulator be responsible for the entire not for profit sector or only the charitable sector?**

In our consideration of ITC 14 it became clear that a common thread within the NFP sector was being focussed on a service objective rather than generating a return for shareholders, although in some cases the distinction is blurred. For example, a charity op shop is run to make a profit, but the reason it exists is to provide funds for certain charitable activities. Within the sector, it is clear that there are a vast number of different organisations and activities.

Consequently we suggest that the national regulator be responsible for the entire sector as we anticipate definitional complexities if the regulator covers some NFPs and not others. For example, if the term “charity” is used, what types of entities constitute a charity and do organisations that do charitable work, e.g. churches or sporting clubs, get included even when only part of their activities involve charitable acts to the wider community?.

- > **Should the regulator be independent of government?**

In our view the regulator should be an independent division within the Australian Securities and Investments Commission (ASIC) accountable to government, in the same way as the AASB.

ASIC’s database should be used to register NFPs to avoid duplication of systems. We also recommend that electronic reporting of data, such as the *Standard Business Reporting* initiative that is being implemented by Treasury at the moment, be used to facilitate efficient and effective reporting of information by NFPs.

- > **Where would the regulator be best located? For example, as a stand alone agency or located within an existing institution, such as the Australian Securities and Investment Commission.**

See above response.

- > **What would be the role of a national regulator? For example, should it have an:**
 - **educative/advisory role?**
 - **enforcement role?**
 - **mediation/dispute resolution role?**

Its role could embrace all these aspects. However, we see its primary function as being educative and advisory as we aim to achieve consistency across the sector to improve the sector’s accountability.

- > **Should a national regulator be responsible for making decisions about charitable status?**

While we see no reason why this role should not be moved from the ATO to a new regulator in due course, we consider that further review should be undertaken with the respective departments before any such change is made.

- > **How should any national regulator be funded? For example, by the federal government, by federal, state and territory governments, on a cost recovery basis?**



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See responses above. However we wish to emphasise that a full cost recovery basis should not be considered as the NFP sector conducts numerous activities and provides many services that benefit society as a whole.

iii. **Should there be a single, specialist, legal structure for the not for profit sector?**

We are not qualified to comment on this aspect, but we do not reject the idea if it contributes to simplification of the regulatory requirements for the NFP sector.

Our concerns in this area would be the ability of the structure to cover the diverse types of NFP operations that currently exist and the fact that there would be costs involved in NFPs having to change their existing constitutions to adopt their new structure. On this basis any new structure would have to have demonstrable benefits to outweigh these difficulties.

If not,

- > **Why not? What would be the disadvantages in having a single, specialist, legal structure for the not for profit sector?**

If so, would this be best achieved through:

- > **A national legislation scheme, whereby current national and state and territory laws relating to the not for profit sector are harmonised into uniform law?; or**
- > **The referral of powers from the states and territories to the Commonwealth, allowing for incorporation of current laws relating to the regulation of the not for profit sector, for example, incorporations Acts and fundraising Acts, into Commonwealth legislation?**
- > **What should be the minimum features of any legal structure?**

The Institute does not see why a single national regulatory system cannot be set up for the NFP sector now without having to devise a new kind of entity.

However we believe that consideration should be given to the cost imposition on individual NFPs on such changes, such that changes required to constitutions, etc are minimal.

Our suggestions for how such a system might work are earlier in this submission under the section *Suggestions for change*.



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APPENDIX 1: SUMMARY OF FINANCIAL REPORTING REQUIREMENTS FOR UNLISTED PUBLIC COMPANIES AND INCORPORATED ASSOCIATIONS

Extracted from June 2007 Treasury Paper and updated by the Institute in July 2008... Note that some states are in the process of reviewing their associations' legislation.

	Legislation	Maintain financial records	Lodgement of financial information	Presented to Members	Audit	Accounting/Auditing Standards
Cwth	<i>Corporations Act 2001</i>	Yes — Section 286	Yes with ASIC — Section 319(1). Must lodge a directors' report and declaration, balance sheet, profit and loss statement, cash flow statement, statement of changes in equity and the notes to the financial statements.	Yes — accounts must be distributed to members by the earlier of 21 days before the AGM or 4 months after the end of the financial year — section 315.	Yes — Section 301. Audit must be completed by a 'registered company auditor'.	The accounts must be prepared in accordance with applicable accounting standards — Section 296. The audit must be conducted in accordance with auditing standards — Section 307A.
ACT	<i>Associations Incorporations Act 1991</i>	Yes — Section 71	Yes with Register-General — Section 79. Accounts must give a true and fair view of income and expenditure, assets and liabilities and any mortgages/charges on property — Section 72.	Yes at AGM — Section 73.	Yes, but not required to be completed by an accountant — Section 74. Audit by a registered company auditor or a member of the ICAA, NIA or CPAA only required if assets or revenue greater than \$150,000 or more than 1000 members or hold a liquor licence — Section 74 and Regulation 12. If the association has revenue exceeding \$500,000, the audit must be conducted by a registered company auditor — Section 76 and Regulation 13.	Audit opinion of an association with more than \$500,000 in revenue must state whether accounting standards have been complied with and, if not, whether this means they are not true and fair — Section 76.

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	Legislation	Maintain financial records	Lodgement of financial information	Presented to Members	Audit	Accounting/Auditing Standards
NT	<i>Associations Act 2003</i>	Yes — Section 41	Yes with Commissioner — Section 45. Accounts must not be misleading and must give a true and fair view of income and expenditure, assets and liabilities, any mortgages/charges on property and the activities of any trusts controlled by the entity — Section 42. Must also be presented with a statement by the management committee — Section 43 and Schedule 4 of Regulations.	Yes at AGM — Section 43. Associations are also required to make members aware of the accounts at least 14 days before the AGM — Section 44.	Yes, but varies on the size of the association. If the association has less than \$25,000 in revenue and less than \$50,000 in assets, it can be audited by a non-associated lay person. Associations with up to \$250,000 in revenue or \$500,000 in assets can be audited by an accountant or a person holding a prescribed class of qualifications and associations over these amounts must be audited by a member of an accounting body holding a public practice certificate or a person approved by the Commissioner— Sections 46, 47 and 48.	All audit opinions must state whether Australian Accounting Standards have been complied with. Schedule 4, Regulations. Audit opinion of an association with more than \$250,000 in revenue or \$500,000 in assets must state whether accounting standards have been complied with and, if not, whether this means they are not true and fair — Section 48. Audits of associations with more than \$25,000 in revenue or \$50,000 in assets must be conducted in accordance with applicable auditing standards — Regulation 11



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	Legislation	Maintain financial records	Lodgement of financial information	Presented to Members	Audit	Accounting/Auditing Standards
NSW⁸	<i>Associations Incorporation Act 1984</i>	Yes — Section 28(1)	Yes with Director-General — Section 27. Accounts must not be misleading and must give a true and fair view of income and expenditure, assets and liabilities, any mortgages/charges on property and the activities of any trusts controlled by the entity — Section 26.	Yes at AGM — Section 26(6).	No requirement for the accounts to be audited.	No requirement for the accounts to be prepared in accordance with accounting standards.

⁸ Legislation currently under review

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	Legislation	Maintain financial records	Lodgement of financial information	Presented to Members	Audit	Accounting/Auditing Standards
QLD	<i>Associations Incorporation Act 1981 as amended by the Associations Incorporation and Other Legislation Amendment Act 2007</i>	Yes — Regulation 9	Yes with Chief Executive — Section 59, 59A and 59B. Associations are required to lodge a financial statement that outlines the association's income and expenditure, assets and liability and details about mortgages, charges and securities affecting the association's property — Sections 2 and 59.	Yes at AGM — Sections 59, 59A and 59B.	Yes, but varies on the size of the association. If the association has less than \$20,000 in revenue and \$20,000 in current assets, the accounts only need to be accompanied by a statement from the entity's Treasurer or President that the association's books are kept in an appropriate manner. Associations with up to \$100,000 in revenue or \$100,000 in current assets must be accompanied by a statement by a member of the ICAA, NIA or CPAA that the association has bookkeeping processes in place to adequately record the association's income and expenditure and dealings with its assets and liabilities. Associations above these thresholds (or how are required to have their accounts audited under other legislation) must have their accounts audited by a registered company auditor — Sections 59, 59A and 59B.	No requirement for the accounts to be prepared in accordance with accounting standards.



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	Legislation	Maintain financial records	Lodgement of financial information	Presented to Members	Audit	Accounting/Auditing Standards
SA	<i>Associations Incorporation Act 1985</i>	Yes — Sections 35 and 39C	Yes but only if required to prepare accounts. An entity is required to prepare accounts if it has revenue greater than \$200,000 — section 35. Accounts must be lodged with the Corporate Affairs Commission. The accounts must fairly present the results of the operations of the association and its financial position — section 35.	Yes at AGM but only if required to prepare — Section 35.	Yes (if required to prepare) by a registered company auditor or just a member of the ICAA, NIA or CPAA, a person the Commissioner considers has appropriate qualifications — Section 35.	No express requirement to use accounting standards, but the auditor must attest that the accounts 'present fairly' the results and financial position of the association — Section 37
TAS^h	<i>Associations Incorporation Act 1964</i>	Yes — Section 23A	Yes with the Commissioner (if not exempt by the Commissioner) — Section 24B. Accounts must be adequate to explain the financial transactions and financial position of the association — Section 24B.	No requirement to present accounts to members.	Yes (if not exempt by the Commissioner) — Section 24. The person must be a registered company auditor or another person approved by the Commissioner — Section 24.	No requirement for the accounts to be prepared in accordance with accounting standards.

^h Legislation currently under review



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	Legislation	Maintain financial records	Lodgement of financial information	Presented to Members	Audit	Accounting/Auditing Standards
VIC	<i>Associations Incorporation Act 1981 as amended by the Fair Trading and Consumer Acts Further Amendments Act 2008</i>	Yes — Section 30A	Yes — Section 30. Accounts must be lodged with the Registrar. Accounts must contain particulars of income and expenditure, assets and liabilities, any mortgages/charges on property and the activities of any trusts controlled by the entity — Section 30.	Yes at AGM — Section 30.	Yes but only if revenue over \$200,000 or assets over \$500,000. Auditor must be a registered company auditor, a member of the ICAA or CPAA or a person otherwise approved by the Registrar — Section 30B.	Accounts must be prepared in accordance with AAS 4, AAS 5, AAS 6, AAS 8, AAS 15, AAS 17, AAS 28, AAS 36, AASB 1018 and AASB 1041 — Regulation 7.
WA⁽ⁱ⁾	<i>Associations Incorporation Act 1987</i>	Yes — Section 25	No requirement to lodge accounts.	Yes at AGM — Section 26. Must present accounts showing the financial position of the association.	No requirement for an audit.	No requirement for the accounts to be prepared in accordance with accounting standards.

ⁱ It is noted that WA is in the process of amending the reporting requirements for incorporated associations through the *Associations Incorporation Bill 2006*. This table does not include an outline of the measures proposed in this Bill

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Appendix 2

Example of charges levied on NFPs by the NSW Office of Fair Trading

Incorporated Associations

Set up fees for an Incorporated Association are:

Application for Reservation of Name (Form 3) \$40
Application for Incorporation (Form 1) \$105

Both forms and fees are required.

Lodgement of Annual Statement (Form 12) Fees:

Within 1 month of AGM \$45
If lodged more than 1 month after AGM \$66
If lodged more than 2 months after AGM \$72

There are also a number of other fees for Incorporated Associations and these are listed on the Fair Trading website at:

[http://www.fairtrading.nsw.gov.au/About us/What the Office of Fair Trading does/Fees/Associations fees.html](http://www.fairtrading.nsw.gov.au/About%20us/What%20the%20Office%20of%20Fair%20Trading%20does/Fees/Associations%20fees.html)

Co-operatives

Application for incorporation for a non-trading (not for profit) Co-operative \$129

Lodgement of Annual Report:

With 28 days of AGM \$Nil
Later than 28 days but not later than 2 months \$96
More than 2 months late \$196

The plethora of fees for co-operatives is on the Fair Trading website at:

[http://www.fairtrading.nsw.gov.au/About us/What the Office of Fair Trading does/Fees/Cooperatives fees.html](http://www.fairtrading.nsw.gov.au/About%20us/What%20the%20Office%20of%20Fair%20Trading%20does/Fees/Cooperatives%20fees.html)