

Submission to Productivity Commission's study into Australia's not-for-profit sector

PilchConnect: *a specialist legal service for community organisations*

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JUNE 2009

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SUMMARY OF PILCHCONNECT RECOMMENDATIONS

- a. That an improved specialist NFP legal structure is developed which allows an organisation to operate across all states and territories, with a sliding scale of reporting obligations, fees and penalties based on the size of the group. As corporate law experience shows, this is best achieved via a referral of state powers.
- b. That a new, independent, national, specialist NFP regulator is established, as endorsed by the 2008 Senate Inquiry at Recommendation 3 of its final report.
- c. That the expenses involved in establishing and financing a new independent NFP regulator can be minimised by:
 - exploring the use of ASIC's online data collection, storage and searching practices, possibly with a sector-managed resource such as Guidestar (UK)
 - cost sharing with the States because of savings achieved by no longer needing separate regulators in each State and Territory
 - cost savings achieved by fewer staff required in the ATO (whose role will be to apply revenue laws rather than determine eligibility), and
 - cost saving to the NFP sector by a reduction in red tape and, therefore, greater capacity and efficiencies in delivery by NFPs of publicly funded services.
- d. That a new independent NFP regulator will:
 - serve as the lynchpin for the introduction of any national regulatory reforms, including fundraising, incorporation, data collection and reporting
 - handle more difficult and contentious issues such as charitable status for tax concessions
 - bring Australia more into line with other jurisdictions and, by being a broader model than just a 'charity commission', will show leadership to English, Scottish and NZ counterparts.
- e. That a minimum standard of disclosure that is simplified and tailored to the NFP situation should be required of all NFPs.
- f. That a tiered regime of reporting obligations based on size should be introduced, with full auditing only being required from larger NFPs. Those NFPs with annual revenue of, say, less than \$500,000, should only be required to report in accordance with a standard that is simplified and tailored to the needs of NFP stakeholders. Filing fees should be modest and again, a sliding scale based on size should be introduced. More work needs to be done to test what are the most appropriate thresholds in the light of the size of those organisations currently on the ASIC and state-based incorporated associations' registers.
- g. That the work of the CPNS Standard Chart of Accounts should continue to be rolled out via COAG but that a NFP-specific accounting standard is still required. Such a standard would underpin greater accountability and transparency and should be a combination of existing industry standards and narrative accounts of how organisations are achieving stated objectives.
- h. That a national NFP regulatory framework must include fundraising laws. These laws need to be overseen by an independent national NFP regulator. Without this legislative consistency and related regulatory oversight, the accountability and transparency that governments and the public are calling for will not be achieved.
- i. That the Productivity Commission works with the Henry Review to endorse a simplified approach to taxation of NFPs with the aim of reducing the confusion and compliance costs that currently exist within the sector.

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- j. That any taxation reform should be underpinned by a rational basis for charity and NFP taxation exemption and other fiscal initiatives. The current system no longer has this underpinning.
 - k. That the Productivity Commission gives support to the modernisation of the charity categories to include, for example, organisations that focus on preventative measures and the protection of human rights. Any changes should be consistent with Recommendation 13 of the 2001 Charity Definition Inquiry, and the approach taken by in overseas models such as the United Kingdom and Ireland.
 - l. That more government funding be made available for sector-based support services to assist NFPs in understanding and implementing sound governance and accountability practices, allowing these organisations to more efficiently meet their compliance obligations and have greater time to focus on core objectives.
 - m. That all incorporated NFPs be required to lodge annual data (both numeric and narrative) to an independent, NFP national regulator. This data, combined with ABS survey data, should be freely available and used to inform the regulator, government and other stakeholders of trends within the NFP sector and provide an evidence base for future policy development.
 - n. That State and Federal Governments work to ensure consistent accountability and reporting requirements in relation to publicly funded service delivery.

1. **SCOPE OF SUBMISSION**

- 1.1. PilchConnect welcomes the opportunity to contribute to the Productivity Commission's study into Australia's not-for-profit (**NFP**) sector.
- 1.2. While there have been many inquiries into the sector dating from the earlier Industry Commission Review in 1995¹, we believe this 2009 study is well placed to draw together the insights and recommendations from previous state and federal reviews, as well as identifying matters needing prompt implementation.
- 1.3. In particular, by identifying impediments to the efficient and effective operation of NFPs and considering implications for the implementation of law reform, this study is an opportunity to provide state and territory governments with a roadmap to reform so that NFPs can enjoy a better regulatory environment that is free from the current complexities, duplication and inconsistencies.
- 1.4. In this submission we draw on:
 - (i) the significant body of existing work undertaken by a range of academic, government and other inquiries into the NFP sector;
 - (ii) our experience in delivering legal information, advice and training to NFPs, in particular brokering pro bono legal assistance and providing low cost training for Victorian NFPs on a range regulatory and governance issues; and
 - (iii) our submissions to the 2008 Senate Standing Committee on Economics 'Inquiry into disclosure regimes for charities and NFP organisations' (**2008 Senate Inquiry**) and the ongoing 'Inquiry into Australia's future tax system' (**Henry Inquiry**). These submissions are attached as Appendix A and Appendix B respectively. For a full list of our submissions to Victorian and Federal Government reviews see Appendix C.
- 1.5. Rather than repeating in full what we have already put to previous inquiries, we refer to and highlight material contained in our earlier submissions where relevant to the Productivity Commission's study (and where they remain the views of PilchConnect). We have also included additional reflections on certain issues.
- 1.6. This submission focuses on the following three areas raised by the Productivity Commission in its Issues Paper released in April 2009:

Enhancing the efficiency and effectiveness of the NFP sector

The primary focus of our submission is the need for significant regulatory reform. We also call for greater access to free and low cost training, information and support services for small to medium NFPs.

Measuring the contribution of the NFP sector

We focus in this section on the need for better qualitative and quantitative measurement of the sector with a view to ensuring this information is used to drive effective policy formation.

Service delivery

We make general comments under this heading, highlighting the need for improved funding arrangements between government (state and federal) and the NFP sector. This includes consistent quality standards and aligned accountability requirements.

¹ See: www.pc.gov.au/ic/inquiry/45charit

2. **ABOUT PILCHCONNECT**

- 2.1. PilchConnect is a specialist NFP community legal centre based in Victoria and one of the six services operating under the umbrella of the Public Interest Law Clearing House Inc. (**PILCH**). PILCH was established in 1994 and is Australia's largest provider of pro bono services.² Since its inception, PILCH has brokered pro bono assistance for NFPs as part of its work of promoting law in the public interest and its commitment to access to justice.
- 2.2. PilchConnect was formally launched as a separate PILCH service in November 2007. PilchConnect provides free or low cost legal information, advice and training to NFP community organisations across Victoria, and conducts policy and law reform work on issues of importance to the NFP sector. Our service is unique within Australia and can be contrasted with local community legal centres which focus on assistance for individuals.³
- 2.3. By developing as a sector-based hub of NFP legal expertise, PilchConnect is working to achieve excellent standards of governance and regulatory compliance by NFP community organisations so their economic and social contribution to Victoria and Australia is maximised.
- 2.4. In effect, we are 'helping the helpers' by supporting the establishment and the effective running of well-governed community organisations. In turn, these NFPs provide crucial support and assistance to the local communities in which they operate, including services to clients and members, promoting volunteering and community well being.
- 2.5. PilchConnect works in partnership with the Australian Centre for Philanthropy and NonProfit Studies at Queensland University of Technology (**CPNS**) and with peak bodies such as Volunteering Victoria, Volunteering Australia and VCOSS. The service is presently in a three year pilot phase. Our services include:
 - (i) **referrals to law firms for pro bono work** - matching eligible, public interest NFPs, who have complex legal issues with PILCH member law firms to provide free legal assistance;
 - (ii) **telephone advice service** – staffed by in-house lawyers to address 'quick' common queries raised by NFPs (pilot to commence July 2009);
 - (iii) **legal information** - a specialist NFP web portal that maps and links existing free legal information and resources, as well as providing a new plain-English fact sheets, FAQs, case studies, guides etc under the framework of the 'lifecycle' of an organisation⁴;
 - (iv) **legal training** - a monthly seminar program for NFPs on relevant legal issues (e.g., incorporation, governance, volunteers, tax concessions, fundraising laws, regulatory compliance) and piloting outer metro and regional training; and
 - (v) **law reform and policy work** - significant work on regulatory reform issues of importance to the NFP sector has already been undertaken by PilchConnect (eg, submissions to 2008 Senate Inquiry, Henry Inquiry, 2007 Federal Treasury Inquiry on Unlisted Companies, and the 2007 Victorian State Services Authority Review).⁵
- 2.6. In this submission we have drawn on the work of previous inquiries and our submissions to them. We are pleased that the Productivity Commission's study expressly states that it will be doing the same.

² See <http://www.pilch.org.au/about/>

³ Note The Arts Law Centre of Australia provides advice, information and training to individual artist and also NFP arts organisations: see <http://www.artslaw.com.au/>

⁴ See www.pilch.org.au/legal_info/

⁵ See [Appendix C](#) for full details of all PilchConnect submissions

3. **ENHANCING EFFICIENCY AND EFFECTIVENESS OF THE NFP SECTOR**

This section is divided into two parts, each with significant importance to the creation of a more efficient and effective NFP sector. Part A examines the need for regulatory reform within the sector and Part B looks at the need for accessible training and support for small-to-medium NFPs.

Part A: Regulatory Reform

3.1. In this part of our submission we consider a range of measures that would reform the regulatory environment for NFPs with the goal of creating a more streamlined, consistent regulatory underpinning for Australia's NFP sector. This part is structured as follows:

- Overview
- An improved national NFP legal structure
- An independent, national NFP regulator
- Tiered reporting based on size and uniform accounting standards
- Nationally consistent fundraising laws
- Simplifying tax concessions

Overview

3.2. Red tape abounds in the NFP sector. The Australian NFP sector is subject to an estimated 178 state and federal statutes; the sector reports to 19 different government organisations and 74 other entities.⁶ The complexity of these legal obligations and reporting requirements is a significant barrier to efficiency.

3.3. If this unnecessary complexity and duplication existed in the business sector it would not be tolerated. Corporate law reform over the last decade demonstrates this. Pressure from business on similar issues was the impetus for:

- the Corporate Law Simplification Taskforce (1993 – 1997) which initiated a wave of significant reforms⁷ including the introduction of the plain language 'Small Business Guide';⁸
- the Corporate Law Economic Reform Program (1997 – 2004) which also saw significant reform to the corporations legislation⁹ as well as the formation of the 'Business Regulation Advisory Group';
- the establishment in 1998 of the Australian Securities Commission (now ASIC) as an independent national regulator; and
- a referral of State powers so that a truly national scheme with could be established.

3.4. The NFP sector itself is calling for reforms to the regulatory approach, and has done so for quite some time. In its first statement released in March 2004, the National Roundtable of Nonprofit Organisations identified the reform of the legal and regulatory environment of NFP organisations as its number one priority.¹⁰

⁶ See submission by National Roundtable of Nonprofit Organisations to 2008 Senate Inquiry, dated 27 November 2008

⁷ For example *First Corporate Law Simplification Act 1995* (Cth)

⁸ See s 111J *Corporations Act 2001* (Cth)

⁹ For example, *Corporate Law Economic Reform Program (CLERP) Act 1999* (Cth) and *Corporate Law Economic Reform Program (Audit reform and Corporate Disclosure) Act 2004 (CLERP 9) 1999* (Cth)

¹⁰ See full statement at:

www.nonprofitroundtable.org.au/Content/NavigationMenu2/PolicyRegulatoryReform/documents2/Reg_Reform-Statement.pdf

- 3.5. We refer to Heading 5 of our submission to the 2008 Senate Inquiry (pages 14–21, [Appendix A](#)) where we outline our views on the unsatisfactory nature of the current regulatory regime and the need for a national framework.
- 3.6. In particular we draw your attention to the two case studies we provided (paras 5.18 and 5.19, pages 19–20, [Appendix A](#)). These case studies are typical of many of the of inquiries we receive at PilchConnect, and we highlight that:
- in addition to NFP-specific laws (eg, fundraising and taxation concessions), NFPs have to be familiar with the laws that apply to all enterprises such as employment and occupational health and safety, however it is often difficult to work out how these laws apply in the context of volunteers and community activities (eg, volunteers visiting people in their homes and driving their own cars);¹¹ and
 - the overlapping nature of the regulatory obligations for NFPs are not well understood within the sector and too often laws are amended with unintended consequences for NFPs.¹²
- 3.7. For small-to-medium NFPs, the *impacts* of the above issues are even greater given their scarce financial resources and limited access to relevant legal expertise. For some, it is often the case that ignorance (or even a 'blind eye') is bliss.
- 3.8. Without reform to the current regulatory environment incorporating a more efficient approach to regulation by removing unnecessary red tape (whilst maintaining acceptable standards of accountability), the vital contribution of the NFP sector will be hampered and Australia will continue to fall behind the standards of comparable countries.¹³
- 3.9. We acknowledge that implementation of some of our recommendations will require a net increase in government funding (eg, the establishment of an independent national regulator)¹⁴, however we submit that this economic trade off is justified. Drawing to a fairly small extent on extra (but of course, finite) government funding to establish proper regulatory underpinning for the overall Australian NFP sector is, we believe, entirely appropriate. All Australians (particularly those most disadvantaged and marginalised) will benefit in both economic and social terms if the NFP sector is supported in a way that allows it to grow, innovate and use its limited resources more efficiently.

An improved national NFP legal structure

- 3.10. We reiterate the views expressed under Heading 8 of our submission to the 2008 Senate Inquiry (pages 28–32, [Appendix A](#)), which endorses the need for an improved national, specialist NFP legal structure.

Why?

- 3.11. The choice of existing legal structures for NFPs can be extremely confusing and none of the available entities can be said to be entirely satisfactory. The National Roundtable of Nonprofit Organisations notes that there are at least 20 different ways to incorporate as a NFP in Australia through a combination of state and federal regulation which creates 'unnecessary complexity and duplication on both the sector and on governments'.¹⁵
- 3.12. What legal structure is appropriate for a particular group is the second most common legal inquiry that we receive from the NFP sector (behind taxation queries). As well as being an issue at the time

¹¹ See Case Study One, page 19, PilchConnect Senate Inquiry Submission, [Appendix A](#)

¹² See Case Study Two, page 20, PilchConnect Senate Inquiry Submission, [Appendix A](#)

¹³ See Modernising Charity Law 2009 Conference papers, available at <https://wiki.gut.edu.au/display/CPNS/Modernising+Charity+Law+Conference+Papers>

¹⁴ See page 12–13 of this Submission

¹⁵ See National Reform Agenda: Initial Statement (2004), at www.nonprofitroundtable.org.au

of incorporation, it often remains an ongoing issue for an organisation: for example, if it expands operations across state and territory borders, or if it wishes to amalgamate with another group.

- 3.13. From those that we speak to, it is clear that many incorporated associations are arguable 'carrying on business' outside their home state but are completely unaware that they should register under the Corporations Act. Further, it is hard to provide clear advice when there is no guidance from ASIC or from case law on what this 'business' term means in the NFP context.
- 3.14. The lack of a better national legal structure can also cause unnecessary complexity for federated organisations which typically have incorporated associations in each state and territory, however where the national body (though very small) is incorporated as a company limited by guarantee.¹⁶
- 3.15. There are few legal practitioners who have detailed knowledge/experience of the range of NFP structures including incorporated associations, co-operatives and indigenous corporations. Many recommend a company limited by guarantee structure even when audit costs¹⁷ place a significant burden on the group's financial resources and there is limited confidence or expertise within the group to manage ongoing compliance.
- 3.16. Recent amendments to the Victorian incorporation associations legislation have meant that significant 'chunks' of the Corporations Act have been incorporated by reference into the state associations regime. For example, Part VIIAC of the recently enacted *Associations Incorporation Amendment Act 2009 (Vic)* applies the voluntary administration provisions of the Federal Corporations Law. While this remedy is a useful one, and the application of consistent legal provisions is entirely sensible, it highlights the growing convergence of the two legal structures. It also means that committee members of incorporated associations (and their advisors) are required to be familiar with two separate governing Acts.
- 3.17. For case studies that highlight some of the problems flagged above, we refer the Commission to:
- Case Study Four of our submission to the 2008 Senate Inquiry,¹⁸ and
 - the submission of the Human Rights Arts and Film Festival Inc (HRAFF) submission to the 2008 Senate Inquiry.¹⁹
- 3.18. Choice of legal structure often requires a detailed legal response. Accordingly, PilchConnect has developed a number of freely available fact sheets for NFP groups to draw upon when considering whether or not to incorporate, including information on which of the several legal structures is the most appropriate in their circumstances. These fact sheets incorporate the diverse views of several legal practitioners, affirming the complexity of this process for NFPs, particularly when compared with the for-profit sector where a company is the only real (incorporated) option.
- 3.19. Currently in Victoria, NFPs should consider the following factors before deciding on a legal structure (noting that some factors will vary from state to state):
- Where will the group operate or carry out its objects or activities?
 - Does the group have access to expertise for ongoing compliance with relevant laws?
 - Will the group have money to pay initial and ongoing fees, plus meet compliance costs?
 - If the group is not a 'charity' (within the technical legal definition), will the group undertake substantial 'trading activities' with the public (rather than just with its members)?
 - What flexibility is needed in the rules or constitution?
 - What duties and penalties will be imposed on the directors / committee members and officers?

¹⁶ See Woodward & Marshall, *A Better Framework: Reforming Not-for-Profit Regulation* (2004), Ch. 3

¹⁷ When auditing by a registered company auditor is not otherwise required of the group under, say, a funding contract.

¹⁸ See page 31, [Appendix A](#)

¹⁹ See http://www.aph.gov.au/senate/committee/economics_ctte/charities_08/submissions/sub133_pub.pdf

- How many members are required?
- How quickly is the legal structure required?
- Voting rights at meetings – do they want non-member proxies to be allowed?
- Is there any requirement under other legislation/ funding agreement to have a particular structure?
- What information are directors / committee members happy to have on a publicly available register?
- What flexibility might be needed in the future to change our structure eg, to amalgamate?

The PilchConnect fact sheet (*'Incorporated association or company limited by guarantee'*)²⁰ attempts to address many of the above questions, however many of these issues require a legal advisor to speak directly with an organisation. There will be other considerations when broadening the consideration to other possible structures such as a co-operative or indigenous corporation.²¹

What?

- 3.20. The sector desperately needs a *better* NFP legal structure that allows an organisation to operate nationally, with a sliding scale of reporting requirements, fees and penalties based on size.
- 3.21. At the very least, this new structure could combine the best elements of the 'incorporated association' structure and the 'company limited by guarantee' to form a new, national NFP specific legal entity that is sufficiently flexible to cater for NFP organisations of varying types and sizes.
- 3.22. Currently, there are desirable attributes in both the 'incorporated association' and 'company limited by guarantee' models. For example, the Victorian provisions in relation to the amalgamation of an association with another organisation have no equivalent under the Corporations Law, and conversely there are provisions under the Corporations Law such as the voluntary administration provisions which are desirable for the state-based association regimes.
- 3.23. There is also considerable confusion about the respective duties of directors (of NFPs incorporated as companies limited by guarantee) and duties of committee of management members (of NFPs incorporated as associations). We believe the better view is that the duties, are for all practical purposes, the same – for example, best practice for a committee of management of an incorporated association should include avoiding trading while insolvent even though (in Victoria) there is no statutory provision. However, the current variation between the statutory provisions of the Corporations Law and the eight different incorporated associations Acts causes much uncertainty and makes training and advice more difficult.
- 3.24. It is also absurd that the penalty for a breach could vary enormously depending on the legal structure of the group, rather than the severity or impact if the breach. For example, a committee member of Victorian incorporated association that allowed the association to trade while insolvent could (if sued by the association) be liable to compensate the association for a breach of the common law duty of reasonable care and diligence. This is to be contrasted with civil and criminal penalties (fine or imprisonment) that the director of a NFP operating under the *Corporations Law* could be liable for (in an action bought by ASIC) in similar circumstances.

²⁰ Available at www.pilch.org.au/legalstructure/#2

²¹ See also PilchConnect fact sheet *'Which legal structure should we choose?', available at: www.pilch.org.au/legalstructure/#1*

How?

- 3.25. At paragraph [8.4] of our submission to the 2008 Senate Inquiry,²² we discuss how legislative reform which implements a new, national NFP legal structure could be achieved. We remain firmly of the view that the preferable method is a referral of powers to the Commonwealth enabling the introduction of a new, commonwealth NFP-specific Act (covering legal structure and fundraising) in conjunction with another Commonwealth Act establishing a new *independent* national regulator. That is, we are advocating the NFP sector have the benefit of the national model that business has enjoyed since 2001.
- 3.26. We appreciate the political cooperation required to achieve a referral of powers. As an interim step or 'fall back' position (that is, one that is at least significantly better than continuation of the current position) we suggest the option of an additional chapter in the existing Corporations Law to deal specifically with NFPs. This should include a plain English guide for NFPs, and the fees and penalties should be lower and based on a sliding scale according to size. We see no reason why this new part of the Corporations Act could not be administered by a new independent regulator, maybe co-located with ASIC and drawing on their data collection systems.
- 3.27. As outlined in the evidence provided by Ms Susan Woodward to the 2008 Senate Inquiry²³, it is on balance, our view that existing **incorporated associations** should migrate, and that there should be a deeming provision to provide for their automatic transfer to any new national regime.
- 3.28. For those NFPs incorporated as **companies limited by guarantee**, our view is that the best approach would be to have an 'opt-out' scheme so that they would be deemed to be transferred to the new NFP structure unless they could, in effect, show some reason why the new regime would not suit their particular type of organisation. An opt-out option may not even be necessary if the new legal structure legislation is contained as a separate part of the Corporations Law – that is, as is currently the case, a company can (subject to member or shareholder approval) change between most other types of companies quite easily.
- 3.29. The following table summarises some of the points for and against mandatory migration of existing incorporated associations to the suggested new national legal structure.

<i>Arguments FOR mandatory migration of incorporated associations</i>	<i>Arguments AGAINST mandatory migration of incorporated associations</i>
If given a choice, many (especially small) organisations are likely to avoid changing to their structure – they will be unaware of what action is required, confused about what to do and/or just think it is all too difficult.	Get better 'buy in' if voluntarily adopt the change. ²⁴
More choice of legal structure will exacerbate current problem of multiple structures and varying regulation.	May be perceived by some in the NFP sector as more regulation and 'red tape'.
Choice of structure would allow for 'forum shopping'.	
This would put significant pressure on the limited resources of PilchConnect, peak bodies and other sector support services as 135,000 associations ²⁵ will need help to decide if they should migrate or not, and to understand new compliance obligations.	

²² See pages 28–30, PilchConnect Senate Inquiry Submission, [Appendix A](#)

²³ See Hansard from 11 November 2008: <http://www.aph.gov.au/hansard/senate/commtee/S11532.pdf>

²⁴ See comments from Professor Myles McGregor-Lowndes p 89, 29 October, 2008, Senate Committee on Economics, Hansard available at <http://www.aph.gov.au/hansard/senate/commtee/S11330.pdf>

²⁵ Federal Treasury estimates for 2008 financial year.

- 3.30. We do not think all existing NFPs should be forced to adopt a single legal structure. Rather it is about improving and simplifying the most common structure while not increasing the burden in the transitional phase.

PilchConnect recommends:

- a. That an improved specialist NFP legal structure is developed which allows an organisation to operate across all states and territories, with a sliding scale of reporting obligations, fees and penalties based on the size of the group. As corporate law experience shows, this is best achieved via a referral of state powers.

An independent, national NFP regulator

- 3.31. The current mix of regulators and interplay between state, territory and commonwealth legislation applicable to the NFP sector is unsatisfactory. State-based regulation of incorporated associations and various fundraising practices gives rise to inconsistencies across jurisdictions, creating issues for many NFPs who are, with new technologies, increasingly more likely to want to operate across state borders.
- 3.32. In its submission to the 2008 Senate Inquiry, the ATO noted that the wide variety of legal structures and inconsistent disclosure obligations '*make the non-profit sector challenging to administer and challenging for the public to understand.*'
- 3.33. Federal bodies such as the ATO and ASIC are not in the best position to regulate the sector and nor do they want to. Currently the ATO has de facto responsibility for the regulation of the sector given its role in determining charity status amongst NFPs, and assessing their eligibility for tax concessions. While the latter function is one that falls within the ATO's mandate of protecting Australia's revenue base, we submit that the initial classification of charity status should be performed by a body that is independent from the ATO.
- 3.34. ASIC finds itself in a position where, again by default, it is required to oversee the relatively small proportion of NFPs that are incorporated as companies limited by guarantee. ASIC is not an ideal regulator for the NFP sector given its primary focus is on the for-profit sector which poses very different challenges to the regulation of community-based NFP organisations. The result is that many NFPs find ASIC to be inaccessible to non-business people and an inappropriate regulator for the NFP sector.²⁶
- 3.35. An independent national regulator which has a public education and training support function in addition to its regulatory responsibilities will go far to reduce the level of confusion currently within the sector. This proposition is not a new suggestion, and was recommended to presiding governments in both 2001 and 2008.²⁷
- 3.36. There is clearly a demand from within the NFP sector for an independent body with sole responsibility for the administration and regulation of the NFP sector.²⁸
- 3.37. Under this model, there would still be a significant role for the states and territories, particularly in working with state-funded NFPs. All governments and the public would have access to better data about NFPs including (at least minimal) financial, size and activity information. This support role already occurs in relation to NFPs registered with ASIC. We are unaware that, at least in Victoria,

²⁶ See Woodward & Marshall, *A Better Framework: Reforming Not-for-Profit Regulation* (2004), p.81

²⁷ See 2001 Charity Definition Inquiry (Rec 25) and 2008 Senate Inquiry (Rec 3, 4 and 5)

²⁸ The vast majority of sector-based submissions to 2008 Senate Inquiry were in favour of new independent regulator

the government provides more (or less) support to community based and/or state-funded NFPs depending on their particular legal structure.

- 3.38. Indeed, if director/committee member duties and compliance obligations are more consistent across NFPs then this should support training that, for example, a state government might want to provide as part of the capacity building of community organisations or a sub-set of the sector that delivers state funded services. Further, the states would be freed from a registration and compliance role that is not revenue earning.

PilchConnect recommends:

- b. That a new, independent, national, specialist NFP regulator is established, as endorsed by the 2008 Senate Inquiry at Recommendation 3 of its final report.

PilchConnect recommends:

- c. That the expenses involved in establishing and financing a new independent NFP regulator can be minimised by:
- exploring the use of ASIC's online data collection, storage and searching practices, possibly with a sector-managed resource such as Guidestar (UK)
 - cost sharing with the States because of savings achieved by no longer needing separate regulators in each State and Territory
 - cost savings achieved by fewer staff required in the ATO (whose role will be to apply revenue laws rather than determine eligibility)
 - cost saving to the NFP sector by a reduction in red tape and, therefore, greater capacity and efficiencies in delivery by NFPs of publicly funded services.

PilchConnect recommends:

- d. That a new independent NFP regulator will:
- serve as the lynchpin for the introduction of any national regulatory reforms, including fundraising, incorporation, data collection and reporting
 - handle more difficult and contentious issues such as charitable status for tax concessions
 - bring Australia more into line with other jurisdictions and, by being a broader model than just a 'charity commission', will show leadership to English, Scottish and NZ counterparts.

Tiered reporting based on size and uniform accounting standards

- 3.39. The current reporting requirements that are imposed on NFPs are inconsistent and inappropriate. In some cases the requirements are too little and in others, they are excessive and overly burdensome.
- 3.40. For most NFPs, they must adhere to a disclosure regime which has little practical relevance for their stakeholders (eg, donors, volunteers, clients and members). In this regard we agree with Recommendation 13 of the 2008 Senate Inquiry which suggests that any new disclosure regime should contain elements of narrative and numeric reporting as well as financial, in acknowledgement of the differences between NFP stakeholders and those in the for-profit sector.²⁹
- 3.41. While adequate disclosure is essential to transparency and the integrity of the sector, reporting should be limited to relevant information and should occur on a 'sliding scale' to ensure that small NFPs (particularly the 'micro' groups) are not required to meet as complex reporting regimes as larger organisations with significant turnover.
- 3.42. We reiterate Section 9 of our submission to the 2008 Senate Inquiry (pages 33–9, Appendix A), and submit that the Productivity Commission should endorse the views of the Senate Committee contained in Recommendations 10 to 13 of that Inquiry, relating to the need for tiered reporting obligations.
- 3.43. Since the 2008 Senate Inquiry Report was released, PilchConnect notes the COAG commitment to the adoption of the (CPNS) Standard Chart of Accounts for the NFP sector.³⁰ This work should be used as an impetus for the development of an AASB NFP-specific accounting standard. A requirement by regulators and grant makers (government and other) for reports based on such a standard would provide much-needed consistency to the reporting process and, assuming the standard was again scaled according to organisational size, it would also reduce the compliance burden for many NFPs.

PilchConnect recommends:

- e. That a minimum standard of disclosure that is simplified and tailored to the NFP situation should be required of all NFPs.

PilchConnect recommends:

- f. That a tiered regime of reporting obligations based on size should be introduced with full auditing only being required from larger NFPs. Those NFPs with annual revenue of, say, less than \$500,000, should only be required to report in accordance with a standard that is simplified and tailored to the needs of NFP stakeholders. Filing fees should be modest and again, a sliding scale based on size should be introduced. More work needs to be done to test what are the most appropriate thresholds in the light of the size of those organisations currently on the ASIC and state-based incorporated associations' registers.

²⁹ This recommendation is in line with PilchConnect's submission to the 2008 Senate Inquiry.

³⁰ See decision of COAG's Business Regulation and Competition Working Group (BRCWG) dated 13 March 2009 (Media release at www.deewr.gov.au/Ministers/Stephens/Media/Releases/Pages/Article_090313_163210.aspx)

PilchConnect recommends:

- g. That the work of the CPNS Standard Chart of Accounts should continue to be rolled out via COAG, but that a NFP-specific accounting standard is still required. Such a standard would underpin greater accountability and transparency and should be a combination of existing industry standards and narrative accounts of how organisations are achieving stated objectives.

Nationally consistent fundraising laws

- 3.44. The current mix of state and federal fundraising regulation generates inconsistencies within the NFP sector, and creates administrative burdens on many organisations who wish to engage in fundraising activities. This unnecessary red tape continues to hinder NFPs in the delivery of their services and has a real impact on the effectiveness of the sector as a whole, particularly as more NFPs engage in cross-border fundraising through the use of new technologies.
- 3.45. We reiterate the observations made under Section 7 of our submission to the 2008 Senate Inquiry (pages 26–7, [Appendix A](#)), and submit that the Productivity Commission should endorse the views of the Senate Committee contained in Recommendation 9 of that Inquiry.
- 3.46. We note that since the 2008 Senate Inquiry, COAG has announced its intention to 'scope' the potential for fundraising harmonisation. While this development is welcome, we must ensure that this scoping exercise leads to positive action. In this regard, policy makers should ensure that any harmonisation of fundraising laws takes into account the emergence of new technologies and sound policy principles are developed that will be 'technologically neutral' and able to address to future fundraising techniques.

PilchConnect recommends:

- h. That a national NFP regulatory framework must include fundraising laws. These laws need to be overseen by an independent national NFP regulator. Without this legislative consistency and related regulatory oversight, the accountability and transparency that governments and the public are calling for will not be achieved.

Simplifying Tax Concessions

- 3.47. Taxation continues to be a major source of confusion for NFP organisations given its heavy reliance on self-assessment and proper interpretation of taxation categories.
- 3.48. We draw the Productivity Commission's attention to our submission to the ongoing Henry Inquiry, and reiterate our recommendations to that Inquiry as they relate to the taxation of NFPs. Our full submission to the Henry Inquiry is attached at [Appendix B](#).
- 3.49. In the above submission we note that the procedures for charitable endorsement are far too complex for many small to medium NFP organisations. Categories of entities entitled for tax concession are still derived from the nineteenth century proclamation of the 'four heads of charity', despite calls for a codification in the 2001 Charities Definition Inquiry. Such development has created two fundamental concerns:
 - charitable law has become out of step with contemporary opinion; and

- characterisation of valid charitable purposes has become so complex that it is difficult for lay people to make application for endorsement without the assistance of an expert lawyer.
- 3.50. Current classifications and categories of charitable purpose have evolved from case-based jurisprudence developed over four hundred years. In our experience, many NFPs that would be considered charitable entities in today's society are not able to receive the benefit of being considered a charity for taxation purposes.
- 3.51. This approach means emerging organisations that are charitable in nature, however focus on 'prevention' as opposed to 'direct relief' are denied charitable status, while certain groups who retain DGR status for historical purposes retain that status even when they are engaged in commercial activities.
- 3.52. Three examples of organisations that may not meet the charitable definition despite providing services that are in the 'public good' include:
- neighbourhood houses and learning centres which provide a range of services to their local communities many of which clearly help prevent social isolation;
 - human rights advocacy groups whose work contributes to the public benefit through advocating on behalf of marginalised and disadvantaged groups; and
 - local housing associations who continue to suffer variable treatment at the hands of the ATO despite providing valuable preventative 'homeless' solutions.
- 3.53. In this regard we endorse the submissions made by the Human Rights Law Resource Centre and the Association of Neighbourhood Houses and Learning Centres (ANHLC) to the Henry Inquiry.³¹ We also endorse ANHLC's submission to the current study.
- 3.54. Confusion about the taxation of NFPs is also a major contributor to inefficiencies in the sector. Even NFPs which do fall within the legal definitions of charity still find current charitable concessions applications so complex and confusing that they need to seek legal assistance. For example, the highly technical distinction between the definition of the 'health promotion' and 'harm prevention' DGR categories in the current regulations are difficult for many lay applicants to understand and apply to their NFPs circumstances.
- 3.55. At PilchConnect, approximately half of the requests we receive for legal assistance from NFPs relate to tax concession eligibility, and the process for obtaining tax concessions – in particular, DGR status. Nearly all applicants are confused about the terminology and the categories that exist. Some within the same 'group' of organisations have different successes in obtaining DGR or TCC status depending on which ATO office they have applied to.
- 3.56. The Australian NFP sector requires one overall simplified tax exemption scheme that is underpinned by a rational basis for the determination of charitable entities. Taxation exemptions should provide support to Australia's NFP sector rather than create a barrier by continuing to institute a complex and inconsistent regulatory framework.

PilchConnect recommends:

- i. That the Productivity Commission works with the Henry Review to endorse a simplified approach to taxation of NFPs with the aim of reducing the confusion and compliance costs that currently exist within the sector.

³¹ See www.hrlrc.org.au/files/henry-review-submission.pdf

PilchConnect recommends:

- k. That any taxation reform should be underpinned by a rational basis for charity and NFP taxation exemption and other fiscal initiatives. The current system no longer has this

PilchConnect recommends:

- j. That the Productivity Commission gives support to the modernisation of the charity categories to include, for example, organisations that focus on preventative measures and the protection of human rights. Any changes should be consistent with Recommendation 13 of the 2001 Charity Definition Inquiry, and the approach taken by in overseas models such as the United Kingdom and Ireland.

Part B: Access to free or low cost training and support for NFPs

- 3.57. The efficiency and effectiveness of the NFP sector will be enhanced if those who volunteer and work for NFPs better understand their regulatory compliance obligations. PilchConnect is a sector-based service with expertise in providing free and low cost assistance in relation to legal and legally related compliance issues.³²
- 3.58. Our experience is that many NFPs are often small, locally based, rely heavily on volunteers, they have limited resources and are unable to access or pay for legal assistance when facing legal problems. Such difficulties are heightened during times of economic crisis, when resources are necessarily prioritised for core service delivery.
- 3.59. The 2008 Senate Inquiry (supported by a considerable body of evidence from earlier inquiries), recognised that the regulatory environment for NFPs is even more complex than for small business. The range of legal issues they face are diverse – from the types of issues all organisations face (eg. employment, intellectual property), to NFP-specific issues (eg. eligibility for concessional taxation status, fundraising requirements, legal issues arising in relation to volunteers) and client-related issues.
- 3.60. The peak bodies we work with bear testimony to the demand for legal services by NFPs, receiving hundreds of calls each year from organisations about legal issues. Such bodies find it difficult to deal with legal queries (they do not employ lawyers) and their efforts are frustrated by the lack of low cost resources tailored to meet the needs of NFPs. Meanwhile, the lack of clear information about legal liability and other legal and regulatory issues acts as an impediment to people (especially volunteers) becoming involved NFPs.
- 3.61. While legal aid and community legal sector funding is available for disadvantaged individuals (primarily in the areas of criminal and family law), there is no equivalent funding for NFPs to access legal advice despite the positive role many NFPs play in preventing social exclusion and family breakdown.
- 3.62. In 2007, PILCH conducted a research project examining the need for, and feasibility of, a specialist NFP legal service. The research project included a legal needs survey, focus groups from the NFP sector and drew upon existing literature. The report concluded that access to legal information was an important concern for NFPs, having regard to the complex regulatory environment in which NFPs operate, the lack of existing and affordable legal services, and the need to prioritise limited financial resources for core service delivery. It found that NFPs required a comprehensive legal information resource, supported by other 'direct contact' services like a telephone helpline to answer quick, basic legal queries and to point NFPs in the right direction.
- 3.63. The report recommended the establishment of PilchConnect, which to date has assisted many community organisations through legal assistance, education and policy work.³³

PilchConnect recommends:

- k. That more government funding be made available for sector-based support services to assist NFPs in understanding and implementing sound governance and accountability practices, allowing these organisations to more efficiently meet their compliance obligations and have greater time to focus on core objectives.

³² 'Legally related' in this context includes understanding financial reporting obligations

³³ For the full Report see: www.pilch.org.au/pc_reports/

4. **MEASURING THE CONTRIBUTION OF THE NFP SECTOR**

- 4.1. Regular, accurate qualitative and quantitative measurement of the NFP sector is necessary to drive policy development and regulatory reform to better underpin and support the sector
- 4.2. We note that the ABS have previously provided useful quantitative data in its 2006-07 survey into the NFP sector, together with its earlier Non-Profit Institutions Satellite Account (cat no. 5256.0) in respect of the 1999-2000 financial year.
- 4.3. While these ABS statistics take into account the estimated value of volunteer contribution, there is very little qualitative data available which provides a measurement for the less tangible aspects of the NFP sector, particularly the flow-on benefits that arise from community engagement activities. We further note that the latest ABS statistics are based solely on NFPs with Australian Business Numbers, thereby missing the vast majority of NFP groups and organisations. As was noted in the 2008 Senate Inquiry:

... figures describing volunteering hours may not be precise, since the value of volunteering to micro organisations cannot be effectively captured, and there remains an acknowledgement that the available data is both 'incomplete and fractured'.³⁴
- 4.4. The announcement that the ABS will be updating its NFP statistics in September 2009 is most welcome. However it is critical that there remains a process in place to allow for the continued annual collection of this data to ensure trends are tracked and monitored over time, and feed into international data such as the John Hopkins Nonprofit Economic Data Project.³⁵
- 4.5. PilchConnect agrees with the Senate Committee's views on the unreliability of current NFP data, and submits that in order to maximise the effectiveness of government policy in relation to social inclusion it is first essential to gain an accurate picture of the NFP sector in Australia through improved data collection.
- 4.6. Annual data that includes the number of NFPs, their size and legal structure (if any), the number of volunteers and paid employees, the cost and value of services provided by (including by volunteers), the sectors of the community they support and their funding would be of immense value to inform government policy and regulatory reform.
- 4.7. We note in late 2008 the UK Office of the Third Sector undertook the extensive National Survey of Third Sector Organisations³⁶, purporting to be the largest survey of the third sector and has a particular emphasis on qualitative research on the effectiveness of NFPs. The UK survey is an attempt to establish objective criteria to measure the success in 'creating an environment for a thriving third sector'. A similar survey in Australia would provide clear direction for government in how to best support the sector, and act as a foundation for policy development.
- 4.8. The conceptual framework put forward by the Productivity Commission at page 21 of its Issues Paper is useful and highlights the difficulties in measuring the multi-layered benefits that community organisations provide.
- 4.9. While the first 'layer' of NFP contribution in the Productivity Commission's framework (financial donations, employee numbers and government funding) has been fairly well documented by the ABS, it is the indirect, qualitative benefits generated by sector where an identified gap in reliable data exists. While we understand these qualitative measures are less precise, it is these less-tangible aspects of the NFP sector that sets it apart from its for-profit counterparts, and it is the flow-on benefits to communities that continue to make this sector such a valuable resource.

³⁴ At page 23

³⁵ See www.ccss.jhu.edu/index.php?section=content&view=9&sub=10

³⁶ See <http://www.nstso.com/>

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- 4.10. The Issues Paper asks to what extent existing measures of the sector have been used to inform policy development. It is a regrettable trend within successive governments to largely ignore calls for policy development from within the NFP sector, and previous parliamentary committee recommendations for reform have been rarely implemented.³⁷

PilchConnect recommends:

- m. That all incorporated NFPs be required to lodge annual data (both numeric and narrative) to an independent, NFP national regulator. This data, combined with ABS survey data, should be freely available and used to inform the regulator, government and other stakeholders of trends within the NFP sector and provide an evidence base for future policy development.

³⁷ For example, see previous recommendations arising from the Charitable Organisations in Australia Report (1995) and Charity Definition Inquiry (2001).

5. **SERVICE DELIVERY**

- 5.1. The Productivity Commission has sought insight on how government-funded services by NFP community organisations can be delivered with greater efficiency and effectiveness.
- 5.2. PilchConnect receives a large number of enquiries from organisations within the NFP sector who seek clarification on obligations under funding agreements and public service delivery. Many NFPs express frustration at the varied reporting and accountability mechanisms in government contracts. If a NFP receives funding from several government funding programs, they often have multiple and diverse reporting obligations, each of which require reporting in different forms, at different times of the year, using different configurations of data. This is very inefficient for NFPs who have limited resources and have to divert them to meeting different reporting regimes, without achieving any greater accountability and quality control over service delivery.
- 5.3. In 2008, CPNS found on average recipients spent 15 paid hours applying for each grant, six hours acquitting and nearly two hours per form on other reports. It is likely to be even longer for NFPs in other states where a Standard Chart of Accounts has not yet been adopted by government.
- 5.4. At a Victorian level, we draw the Productivity Commission's attention to the recommendations put forward by the State Services Authority (**SSA**) in its 2007 review of not-for-profit regulation.³⁸ In particular, we highlight those findings by the SSA regarding improved funding agreements between government and the NFP sector, and the proposal to align quality standards and accountability requirements across various government departments, as well as consolidate reporting mechanisms. For example, Finding [7.2] of the SSA's report states:

To facilitate consistency in service quality standards and accreditation systems across Government, DHS, DOJ, DPCD and DEECD should explore opportunities to align quality standards and accountability requirements. Where policy objectives are aligned, requirements should be consistent with those in other jurisdictions (e.g. the Commonwealth).
- 5.5. Important progress on the need for harmonisation across departments is being made in Victoria on this issue under the guidance of the Office for the Community Sector, and this progress should be endorsed at federal level.

PilchConnect recommends:

- m. That State and Federal Governments work to ensure consistent accountability and reporting requirements in relation to publicly funded service delivery.

³⁸ See [www.ssa.vic.gov.au/CA2571410025903D/WebObj/NFP_FinalRpt/\\$File/NFP_FinalRpt.pdf](http://www.ssa.vic.gov.au/CA2571410025903D/WebObj/NFP_FinalRpt/$File/NFP_FinalRpt.pdf)

6. **CONCLUSIONS**

- 6.1. In economic terms, the NFP sector contributes (if an imputation is made for the value of services provided by volunteers) 4.9% of Australia's GDP. On this basis, the Australian Bureau of Statistics figures show that the NFP sector contributes more to GDP than the government administration and defence (4.1%) and mining (4.6%).³⁹
- 6.2. The figures above do not take into account the qualitative contribution of the NFP sector – for example, the role it plays in social inclusion and the delivery of government services. The NFP sector touches every Australian in some way, as a recipient and/or as a donor (of time or money).
- 6.3. While the sector is a major contributor to Australia's social and economic framework at the best of times, we note that in difficult economic climates, the NFPs are relied upon more than ever. As philanthropic funding and corporate donations become more difficult to source, it is extremely important that NFPs are able to deliver their services in the most efficient and effective manner to ensure maximum benefit.
- 6.4. The efficient and effective delivery of services can only be achieved where the NFP sector is not placed in a position where organisations must devote excessive resources to compliance and regulatory issues. In our submission, and drawing on outcomes of earlier inquiries into the sector, we believe that while the current regulatory scheme might be intended to promote transparency, it in fact wastes scarce NFP resources and does not achieve the best standards of accountability. As such, the economic and social contribution of the NFP sector to Australian society is not being maximised.
- 6.5. Without reform to the current regulatory environment incorporating a more efficient approach to regulation by removing unnecessary red tape (whilst maintaining acceptable standards of accountability), the vital contribution of the NFP sector will be hampered and Australia will continue to fall behind the standards of comparable countries.
- 6.6. While we acknowledge that our recommendations require net increased funding (for example, the establishment of an independent national regulator), we submit that this economic trade off is justified. Drawing to a fairly small extent on extra (but of course, finite) government funding to establish proper regulatory underpinning for the overall Australian NFP sector is, we believe entirely appropriate. All Australians (particularly those most disadvantaged and marginalised) will benefit in both economic and social terms if the NFP sector is supported in a way that allows it to grow, innovate and use its limited resources more efficiently.

³⁹ ABS, Australian National Accounts: Non-Profit Institutions Satellite Account, 1999-2000 at www.abs.gov.au/AUSSTATS/abs@.nsf/productsbyCatalogue/A41A434D8A63A4DCCA256C7E0076ABE2?OpenDocument