



Australian Government

The Treasury

House of Representatives Standing Committee
on Economics

**Inquiry into the Australian Charities and
Not-for-profits Commission (ACNC) draft
legislation**

**Supplementary submission by the Australian
Treasury**

July 2012

CONTENTS

SUPPLEMENTARY SUBMISSION – INTRODUCTION	2
Objects clause	2
Increase in red-tape due to other regulatory requirements.....	2
Interaction between ACNC and the Australian Securities and Investments Commission (ASIC)	3
Director liability	4
‘Likely’ contravention of the Act.....	4
Use of injunctions and the directions power	5
External conduct standards – terrorism	6
Level of reporting thresholds.....	7
Preparation costs of financial report.....	7
Deferral of reporting deadlines	7
Review and appeals framework.....	8
Consultation	8
Independence from the ATO	9

SUPPLEMENTARY SUBMISSION – INTRODUCTION

1. Treasury provided a submission to the House of Representatives Standing Committee on Economics's (the Committee's) inquiry on the draft ACNC legislation on 20 July 2012. Treasury also appeared before the Committee on 26 and 27 July 2012.
2. Below is Treasury's response to key issues raised by other witnesses that appeared before the Committee, and the other submissions received by the Committee.
3. Treasury's response to questions taken on notice is also set out below.

Objects clause

4. Some stakeholders expressed concerns about the fact that an explicit reference to reducing red-tape was not included in the objects clause of the draft legislation.
5. The establishment of a national regulatory framework, and a 'one-stop shop' regulator, would in itself, reduce regulatory burden on the sector. A Fact Sheet, included at [Appendix A](#), explains how the draft legislation will achieve this reduction in red-tape.
6. Treasury notes that the objects clause currently requires the Commissioner to have regard to the "benefits gained from minimising procedural requirements and procedural duplication by cooperation between the Commissioner and other Australian government agencies; and effective administration of the laws that confer functions and powers on the Commissioner".
7. In addition, a reference to red-tape reduction has been made in the Guide to the draft Bill, which provides that the ACNC Commissioner will "cooperate with other government agencies to oversee a simplified and streamlined regulatory framework for not-for-profit entities".
8. In response to concerns raised by stakeholders, Treasury is considering options for revising the objects clause to make the reduction of red-tape more explicit.

Increase in red-tape due to other regulatory requirements

9. Some stakeholders expressed concerns about the potential for an increase in red-tape, if the States and Territories do not harmonise their regimes with the ACNC framework.
10. The Australian Government is working collaboratively with the States and Territories, through the NFP Reform working group established under the Council of Australian Governments (COAG). One of the core deliverables of the working group is to review regulatory duplication for governance and reporting in the NFP sector, and recommend to COAG options to reduce or minimise regulatory duplication. A fundamental part of this work is considering the role that the ACNC will play in the regulation of the NFP sector and the scope to reduce regulatory duplication at a Commonwealth, State and Territory level.
11. In developing the reforms, Treasury prepared a Regulation Impact Statement (RIS) which was approved by the Office of Best Practice Regulation. The RIS identified benefits to the NFP sector, even if the Australian Government established the ACNC

without any corresponding changes at the State and Territory levels. However, the benefits to the NFP sector would be maximised if the States and Territories harmonised their frameworks with the new national regulatory regime.

12. The benefits, at the Commonwealth level alone, include an immediate reduction in regulatory burden for entities such as companies limited by guarantee. These entities will be subject to a simpler regime than currently applies under the *Corporations Act 2001* (the Corporations Act). There will also be a number of other benefits at the Commonwealth level, including the introduction of a 'charities passport' that will streamline the interactions between registered entities and government agencies. Further details about these benefits are included in the Fact Sheet at [Appendix A](#).
13. Some stakeholders expressed concerns that there would be an increase in regulatory burden at the Commonwealth level, as charities would still be subject to requirements contained in other Acts, such as the Corporations Act.
14. Consequential amendments are currently being drafted to other Acts, including the Corporations Act. A list of consequential amendments being considered to other Acts is included at [Appendix B](#). The consequential amendments are scheduled for introduction with the ACNC reforms, and would address duplication at the Commonwealth level.
15. As a result of the Government's decision to extend the commencement of the financial reporting framework, the first financial statements will not be due until 31 December 2014. This will provide further time to finalise the harmonisation of regimes at the Commonwealth, State and Territory levels. The NFP Reform Working Group of COAG has been asked to respond to COAG before its last meeting of 2012.

Interaction between ACNC and the Australian Securities and Investments Commission (ASIC)

16. Currently, ASIC is responsible for regulating companies limited by guarantee that are registered under the Corporations Act. These companies predominantly have an NFP purpose. Around 12,444 companies limited by guarantee were registered with ASIC as at 30 June 2011.
17. In addition, a small number of NFP entities may be incorporated as proprietary companies or public companies other than those limited by guarantee (for example, companies limited only by shares, or by shares and guarantee). These companies are also currently subject to ASIC's regulatory oversight.
18. The Government is currently drafting consequential amendments to clarify the delineation of responsibilities between ASIC and ACNC under the new regime. ASIC will continue to register companies, including companies limited by guarantee, but will have limited oversight of the financial reporting and governance arrangements of those companies that choose to register with the ACNC, as oversight of these arrangements will now be performed by the ACNC.
19. Currently, ASIC conducts surveillance of financial reports prepared by companies, registered schemes and disclosing entities, and their compliance with Part 2M.3 of the Corporations Act. ASIC will not continue to be responsible for financial reporting surveillance in respect of entities registered with the ACNC from 1 July 2013, as this function will instead be performed by the ACNC.

20. ASIC is currently responsible for registering authorised audit companies and registered company auditors, and is expected to continue to do so under the new regime.
21. ASIC is also expected continue its current oversight role with respect to liquidations and administrations undertaken under the Corporations Act.

Director liability

22. Some stakeholders raised concerns about director liability under the draft legislation. For example, the Association of Independent Schools of NSW expressed concerns that the reforms would erode the concept of limited liability for school boards.
23. The provisions relating to director liability were significantly revised and limited following the consultation process. The liabilities and offences that are imposed, in limited cases, on directors of incorporated charities, will ensure that individuals do not seek to hide behind the protection of a corporate veil to protect themselves from acts of deliberate misconduct.
24. The current exposure draft only imposes personally liability on directors of bodies corporate in respect of one offence provision, which is an offence arising from a failure to comply with a direction from the ACNC Commissioner. The penalty for this offence provision is 40 penalty units, which is lower than penalties for similar offences, for example, that are contained in the *Banking Act 1959* (the Banking Act).
25. Directors will only be personally liable for the liabilities of the body corporate in cases of dishonesty, gross negligence, recklessness, or a deliberate act or omission. Treasury notes that this test is used in other contexts, and has an established meaning.
26. Some stakeholders queried whether a 'deliberate act or omission' should be qualified with a reasonableness test, or some other requirement that the act or omission needs to occur knowingly in contravention of the law. This is the intention of the draft legislation, and to the extent that this intention is not clear, Treasury will examine options to clarify the drafting of this provision in consultation with the Office of Parliamentary Counsel (OPC).
27. Some stakeholders also expressed concerns that the director liability regime contained in the draft Bill was more onerous than that applying to large for-profit companies. This is not the case, as the governance standards are expected to be simplified, tailored for the NFP sector, and otherwise modified to take into consideration comments made during the consultation process. On 17 May 2012, the Government announced that the revised governance standards will be subject to further consultation and implemented through regulations.

'Likely' contravention of the Act

28. Some stakeholders raised concerns about the references in the draft legislation to "likely to contravene", and expressed concerns that mere suspicion on the part of the ACNC Commissioner would be sufficient to trigger this requirement.
29. The explanatory memorandum provides detailed guidance on this issue, and clarifies that rumour or mere suspicion on the part of the ACNC Commissioner would not be sufficient to trigger the requirement. Rather, the Commissioner needs reliable and accurate evidence which clearly indicates that there will be a contravention, for example, a contract for the transfer of assets contrary to the charitable purpose. The

draft legislation enables the Commissioner to intervene to prevent the breach from occurring, and proactively protect the charity's assets before they may be depleted.

30. In addition, a 'reasonably believes' test needs to be satisfied which ensures that the ACNC Commissioner will only revoke registration, or use enforcement powers for likely contraventions where any reasonable individual, provided with the set of information available to the ACNC Commissioner, would conclude that it is likely that a registered entity will contravene a provision of the Bill.
31. Some stakeholders expressed concerns about the 'likely to contravene' test, and in particular, that it did not necessarily ensure that the circumstance was 'more likely than not'. This is the intention of the draft legislation, and to the extent that this intention is not clear, Treasury will examine options to clarify this threshold in the draft legislation, in consultation with OPC.

Use of injunctions and the directions power

32. As the ACNC will take over the roles of other Commonwealth level regulators in cases where these other regulators are responsible for overseeing the governance structures and financial performance of NFP entities. The enforcement powers provided by this Bill are therefore modelled on the powers given to these other regulators including ASIC, the Australian Prudential Regulation Authority (APRA) and Australian Competition and Consumer Commission (ACCC).
33. The type of enforcement power used by the ACNC Commissioner will be determined by the kinds of actions which are required to address the contravention or non-compliance. In some cases, all that will be required is the issuance of a warning notice to compel self-correction, in other cases where an entity has persistently failed to meet regulatory obligations, the ACNC Commissioner may have to remove a responsible entity.
34. The power to issue directions provides the ACNC Commissioner with a mechanism to direct registered entities to address any contraventions of provisions to the ACNC Bill (including non-compliance with governance standards or external conduct standards).
35. The ACNC Bill also provides the Commissioner with the authority to apply for an injunction to restrain a person from engaging in conduct which contravenes the ACNC Bill (including non-compliance with governance standards or external conduct standards), or require a person to do a thing which ensures compliance with the ACNC Bill.
36. Broadly, the ACNC Commissioner can deliver similar regulatory outcomes when using directions and injunctions. However, both powers are required for the ACNC to take to take cost effective, proportional and targeted compliance action.

Cost effectiveness

- 36.1. The power to issue directions is an administrative instrument while injunctions are a judicial instrument. Directions are more cost effective from the perspective of all parties. Taxpayer funds do not have to be used to fund court proceedings while registered entities are able to use the review and appeal processes in Division 160 of the ACNC Bill if dissatisfied with directions, as opposed to taking judicial action.

Targeted

36.2. The power to issue directions provides the ACNC Commissioner with the flexibility to tailor specific solutions to address regulatory concerns. For example, the Commissioner can specify a particular class of acts, or particular classes of acts in a single direction. Injunctions can only be used to ensure compliance with the court's interpretation of law, therefore the scope to tailor solutions to address regulatory concerns would be limited.

Proportionality

36.3. Injunctions tend to be reserved for the more serious contraventions or in cases where directions have been issued and the relevant entity has not complied with the direction (see for example the Banking Act). If an entity person fails to comply with an injunction the person would be in contempt of court which is punishable by imprisonment, on the other hand, failure to comply with a direction could only result in a monetary penalty.

External conduct standards – terrorism

37. Some stakeholders queried the need for external conduct standards, and the extent to which NFP entities are being misused by terrorist organisations.
38. The purpose of the external conduct standards is to promote transparency and provide confidence across the sector and the general public that charitable funds and services are applied for legitimate purposes, and are not contributing to terrorist or other criminal activities.
39. Law enforcement agencies have provided information to Treasury citing investigations of NFP entities suspected of being misused by terrorist organisations. Forming an alliance between law enforcement agencies and the ACNC will considerably enhance the scope to maintain the integrity of the NFP sector from a whole of government perspective.
40. The external conduct standards are expected to be based on the recommendations of the Financial Action Task Force's (FATF) Special Recommendation VIII (SR VIII). The FATF is an inter-governmental body established in 1989 to promote measures for combatting money laundering, terrorist financing and related threats to the integrity of the international financial system.
41. As a member of the FATF, Australia has agreed to comply with the FATF recommendations. FATF SR VIII requires FATF members to 'combat the misuse of NPOs (non-profit organisations, that is, NFP entities) for the purpose of terrorism financing'. In FATF's last review of Australia's progress in 2005, it found that Australia was only partially compliant with SR VIII.
42. The Canadian Revenue Agency has undertaken an analysis on how FATF recommendations have been implemented in other countries. Further information is available at <http://www.cra-arc.gc.ca/chrts-gvng/chrts/ntrntnl-eng.html>.
43. Protecting the NFP sector from misuse by terrorist organisations is both a critical component of the global fight against terrorism and a necessary step to preserving the integrity of Australia's NFP sector.
44. In May 2012, the Government announced that the governance standards and external conduct standards would be set out in regulations, which would be subject to further

public consultation. This consultation process is expected to commence in the coming months. The governance and external conduct standards will commence from 1 July 2013.

Level of reporting thresholds

45. Several stakeholders expressed the view that the current reporting thresholds are too low, and argued that the thresholds should be increased.
46. As noted in our initial submission, 78per cent of registered entities fall within small tier, 11per cent in the medium tier and 11per cent in large tier. Any increase in the thresholds would dilute transparency and accountability for entities that are economically significant due to the size of their operations.
47. In addition, the thresholds contained in the draft legislation are based on thresholds applying under the Corporations Act to companies limited by guarantee. These thresholds were introduced in 2010, and were the subject of extensive consultation. The thresholds are also consistent with specific State regimes, such as Victoria, which may facilitate harmonisation with the States.

Preparation costs of financial report

48. Some stakeholders expressed concerns about the cost of preparing financial reports.
49. According to ATO data, the average administration cost for private ancillary funds (which is a fund that allows businesses, families and individuals to establish and donate to a charitable trust of their own, without the need to seek contributions from the public, for the purposes of disbursing funds to a range of other DGRs) is less than 0.8 of a cent for every dollar administered by the fund. This figure is not limited to reporting and auditing costs, but also includes costs associated with salary, rent, vehicle, fund raising and other expenses. As such, the financial reporting and auditing costs alone are expected to be considerably lower than this.
50. Based on ATO data, the vast majority of registered entities, 78 per cent, will not have to prepare a financial report, as they will fall into the small category.
51. Of the 22 per cent that will be required to report, not all will need to comply with the full suite of accounting standards, as some may prepare special purpose financial reports. Of those that do prepare general purpose financial reports, and need to comply with accounting standards, they will have the option to apply a far simpler set of disclosures, referred to as 'reduced disclosure requirements', developed by the Australian Accounting Standards Board. This will reduce the costs associated with the preparation of the financial report.
52. The Bill also significantly expands the range of individuals that conduct a review of a financial report, which will in turn, reduce review fees.
53. The Treasury is working closely with the ACNC Taskforce, the Australian Accounting Standards Board, and the Auditing and Assurance Standards Board, in settling details for the final reporting regime, to ensure we achieve a workable set of arrangements for all stakeholders.

Deferral of reporting deadlines

54. Some stakeholders expressed the view that the reporting framework should be further delayed.

55. On 17 May 2012, the Government announced deferral of the financial reporting regime, to enable further time for consultation. The financial reporting framework will now commence for financial years commencing on or after 1 July 2013.
56. As a result, the first financial reports will need to be lodged with the ACNC by 31 December 2014. This will provide registered entities with ample time to comply with the new framework.

Review and appeals framework

57. Some stakeholders raised the possibility of obtaining a stay on the suspension and removal of responsible entities.
58. The draft legislation provides a review and appeals framework, which is modelled closely on the existing review and appeals framework in Part IVC of the *Taxation Administration Act 1953* (TAA). Entities that apply for a review, or appeal a decision taken by the ACNC Commissioner are required to comply with the decision being reviewed until it is overturned. As such, the framework set out in the draft legislation is consistent with standard practice. Consultation was undertaken on the review and appeals framework in the draft ACNC legislation, and there was strong support for a model based on Part IVC of the TAA.
59. Enabling a stay on the removal of responsible entities could lead to considerable uncertainty, particularly as the registered entity's entitlement to registration may be in question. It may also raise substantial concerns about flow-on impacts on the ability of the ATO to protect revenue because of the strong link between the ACNC Commissioner's decisions and access to tax concessions. In line with existing ATO practices, the ATO (and the ACNC) will often allow the effect of decisions to be stayed, if this is appropriate given the particular circumstances.
60. In addition, deviations from the established framework may come at substantial cost to the Administrative Appeals Tribunal (AAT), and affect the timeliness of AAT decisions, and access to justice.

Consultation

61. Some stakeholders expressed concerns about the consultation timeframes and processes on the draft legislation.
62. The Government has undertaken extensive consultation on the draft legislation, including:
 - consultation undertaken on a scoping study, which commenced in January 2011, with a total of 162 submissions received.
 - public and targeted consultation processes commencing in November 2011, December 2011 (with a total of 108 submissions received) and May 2012 respectively;
 - ACNC Implementation Taskforce community consultation sessions held in all Australian capital cities and Townsville concluding in February 2012 which was attended by around 1,600 people; and
 - face-to-face meetings with numerous stakeholders.

63. A wide range of stakeholders participated in the consultation process, including NFP entities, academics, accounting and legal experts, and representatives of the States and Territories. The Government also consulted with peak advisory bodies, such as the NFP Sector Reform Council, the Charities Consultative Committee, and the Clubs Consultative Forum. A full list of public submissions made in response to the public consultation process is available on the Treasury website.
64. To facilitate further consultation with the sector, the Government delayed commencement of the ACNC from 1 July 2012 to 1 October 2012. On 17 May 2012, the Government also announced that governance standards, external conduct standards and the financial reporting requirements will apply from 1 July 2013, which will enable further consultation on these issues. These requirements will be implemented through regulations, and are expected to be released for public consultation in the coming months.
65. The draft legislation has been developed in close consultation with stakeholders, and the Government has been responsive to issues raised as part of the consultation processes. Detailed information about the changes made following the consultation process are set out in our initial submission.
66. Treasury undertook to provide the Committee with the number of submissions received as part of the public consultation process on the discussion paper relating to *A Definition of Charity*, which closed for consultation in December 2011. Treasury received 217 submissions on the discussion paper, including confidential submissions. It is important to note, however, that a considerable proportion of the respondents to this discussion paper had previously provided submissions to an earlier exposure draft Bill which was released in 2003. The respondents to the *2001 Inquiry into the Definition of Charities and Related Organisations* is publicly available at http://www.cdi.gov.au/html/public_submissions.htm.

Independence from the ATO

67. Some stakeholders expressed concerns that the ACNC may not be sufficiently independent from the ATO.
68. The ACNC will be a statutory office that is structurally separate from the ATO. There are a number of safeguards to ensure the independence of the ACNC. For example, the ACNC Commissioner will be appointed by the Governor-General, and will report directly to the Parliament each year, by way of an annual report given to the Minister.
69. The draft legislation also expressly provides that ACNC officers act independently of the ATO, for example, when making registration decisions. This structural separation will help to address any perceived conflicts of interest that currently exist with the ATO's revenue collection role and its current role as the default NFP regulator. At the same time, it ensures that the ACNC benefits from the economies of scale that come from having its administrative support provided by the ATO.
70. This is consistent with recent moves internationally. For example, in New Zealand, where the Charities Commission is being brought within other larger Government agencies to benefit from economies of scale, but nonetheless, maintaining a level of independence in decision-making.