



**CHARTERED SECRETARIES
AUSTRALIA**

Leaders in governance

20 July 2012

Committee Secretary
Standing Committee on Economics
PO Box 6021
Parliament House
CANBERRA ACT 2600

By email: economics.reps@aph.gov.au

Dear Committee Secretary

**Inquiry into the Australian Charities and Not-for-profits
Commission Exposure Draft Bills**

Chartered Secretaries Australia (CSA) is the peak body for over 7,000 governance and risk professionals. It is the leading independent authority on best practice in board and organisational governance and risk management. Our accredited and internationally recognised education and training offerings are focused on giving governance and risk practitioners the skills they need to improve their organisations' performance and are 'first-choice' options for those intent on pursuing a C-suite career.

CSA has unrivalled depth and expertise as an independent influencer and commentator on governance and risk management thinking and behaviour in Australia. Our Members are all involved in governance, corporate administration, legal practice and compliance with their primary responsibility being the development and implementation of governance frameworks in public listed and public unlisted companies, private companies, and not-for-profit organisations.

General comments

CSA welcomes the opportunity to comment on the Australian Charities and Not-for-profits Commission (Consequential and Transitional) Bill 2012 and the Australian Charities and Not-for-profits Commission Bill 2012 (the exposure drafts) and draws upon the experience of our Members in formulating our submission.

CSA strongly supports the establishment of the independent statutory office, the Australian Charities and Not-for-Profits Commission (ACNC). We have long supported the adoption of a new regulator for the not-for-profit (NFP) sector and this amended draft legislation is a very positive step in achieving the most appropriate reforms for the sector. CSA is of the view that the draft legislation will progress work towards improving transparency and public confidence in the NFP sector.

It is important that the reform process not only recognises the vital services and benefits that the NFP sector provides to communities through Australia, but also achieves benefits for the NFP sector through a reduction in the compliance burden, an increase in engagement with the sector, and the provision of information and guidance to the sector to assist entities to comply with their regulatory obligations.

In this regard, CSA has repeatedly recommended in our submissions to Treasury and the ACNC (through the ACNC Implementation Taskforce) for a slowing of the pace of reform to allow the NFP sector to properly engage with the government on the proposed suite of reforms; and for the separation of the proposed ACNC legislation to establish the new regulator from the legislation which will establish the duties, governance arrangements and operation of entities which the ACNC will regulate.

CSA therefore welcomed the government's announcement on 17 May 2012 that it would stage the NFP sector reform process to:

- commence the operations of the ACNC from 1 October 2012, and
- delay the commencement of the governance standards, including the external conduct standards, and the financial reporting framework to commence on 1 July 2013, with the first financial reports for medium and large registered entities now beginning to fall due after 31 December 2014.¹

CSA welcomes the current exposure drafts that act on this commitment to a two-staged reform process. CSA agrees that the extended start dates will give more time for charities to transition to the new regulatory framework and for the ACNC to provide guidance materials to help with the transition. CSA is of the view that the staged reform process is now much more likely to provide sufficient time for the new regulatory framework to be put in place without imposing onerous compliance burdens on the NFP sector.

CSA also welcomes the decision by the government to establish the ACNC in legislation, as reflected in the exposure drafts, and deal with the governance arrangements, external conduct standards and financial reporting detail in regulations. CSA is strongly of the view that this approach will result in a regulatory framework that fulfils the objectives of reducing the compliance burden for the NFP sector and providing for a light-touch regulatory framework.

CSA notes that the regulations will be the subject of further consultation and looks forward to providing comment when they are released for public consultation.

However, CSA notes that the exposure drafts still contain sections relating to the duties and financial reporting of entities that the ACNC will regulate (primarily concerning audit requirements). CSA strongly recommends that these matters are removed from the bills and dealt with in the regulations, as with all other aspects of financial reporting.

As we have noted in our earlier submissions, for the private sector, there is one Act that establishes the framework for ASIC and a separate Corporations Act that deals with the duties, governance arrangements and operation of companies that ASIC regulates. A great deal of effort was expended on the sequencing of the legislation, and it has served the private sector well. The current exposure drafts have moved strongly in this direction, which is to be commended, but further work is required to ensure that the sequencing is correct and that these bills deal only with the establishment of the ACNC, its regulatory and enforcement powers and how it operates.

CSA's main concern with the exposure drafts is the duplication of reporting that will result if the bills are passed in their current form. The draft legislation does not address the question of how the proposed regime will co-exist with existing parallel legislation. We encourage the Committee to recommend a closer examination of this area in particular. We accept that as a consequence of this recommendation a short delay may be required to the start date of the regulator. CSA strongly supports the establishment of the ACNC as soon as possible, with ongoing consultation with the sector as to the duties, governance arrangements and financial reporting of the entities it regulates, but it is also important to address any possible duplication of reporting before these bills pass. CSA is of the view that the NFP sector would support such a short delay, in order to

¹ The Hon David Bradbury MP & the Hon Mark Butler MP, 'Staging the Introduction of Regulatory Reform for the Not-for-profit Sector', Joint Media Release, 17 May 2012

ensure the legislation supports the policy objectives outlined by the government and the needs of the sector.

A key policy objective for the NFP regulatory reform is the creation of a one-stop shop regulator for the sector, and reduced compliance and red tape. Unfortunately, until the question is addressed of how the proposed regime will co-exist with parallel existing legislation, this admirable objective cannot be realised. CSA understands that there are parallel processes occurring to address some of these areas. However, lack of definitive timelines and recommendations leaves the sector uncertain and concerned.

Timeframe for consultation with the NFP sector

Part of the government's announcement on 17 May 2012 recognised that effective engagement and consultation with the NFP sector remains critical to the shaping of the reform process.² It is disappointing, therefore, to note that, yet again, there appears to be a lack of consideration of the needs and capacities of the NFP sector in the consultation on the current exposure drafts.

CSA has emphasised its concerns about inappropriate timeframes for consultation in almost every consultation undertaken concerning the NFP sector. CSA Members are extremely concerned about the period of consultation for the exposure drafts, being only 12 working days. The timeframe for the submission of feedback on a major piece of legislation that will affect the NFP sector for many years to come is unacceptably short and poses particular difficulties for the NFP sector.

CSA reiterates that many NFP organisations are staffed or managed by volunteers, who will be seeking to address the issues canvassed in the exposure drafts as part of their extra-curricular responsibilities. Requesting consultation on proposed legislation which is 166 pages long (and an explanatory memorandum which is 259 pages long) over such a short period does not provide sufficient time for volunteers to meet, discuss the exposure drafts and formulate considered responses.

A consultation on a major legislative imposition on the NFP sector occurring within such a tight timeline also appears to counter the very intent of the NFP reform process, of which one of the major aims is to reduce the onerous compliance burden on the NFP sector. The NFP sector has traditionally been under-resourced, yet the timeframe for this consultation places an exceptionally high burden on NFP organisations.

CSA itself believes that we can offer only a high-level review of the exposure drafts due to the short timeframe available for consultation, and we remain concerned that the consequences attached to this legislation will not be able to be properly assessed in light of the lack of proper consultation time.

Specific comments on the exposure drafts:

Duplication of reporting and expanding the legislation to cover the entire NFP sector

The release of draft legislation proposing the establishment of a national regulator for tax-endorsed charities and clarification that the governance arrangements and detail of financial reporting will be dealt with separately in regulations is a positive development. CSA commends the government for listening to the concerns of the sector and responding to suggestions from stakeholders as to how best approach the reform process.

CSA recognises that the intent is to have the founding legislation for the ACNC to be complete and passed before 1 October 2012. CSA is committed to ensuring that the NFP reform process is

² *ibid*

not unduly inhibited in its development, and supports the government's intention to ensure that the ACNC is operational as soon as possible. However, as noted earlier, we have concerns relating to duplication of reporting that we believe need to be addressed before this bill passes in parliament. We are also of the view that further clarification is required as to how the draft legislation will address the expansion of the legislation to cover the entire NFP sector.

CSA agrees with the Regulatory Impact Statement that 'Once the sector's new regulatory system is in place ... it will lead to a reduction in compliance costs and red tape faced by the sector'. The explanatory materials do, however, also point to transitional compliance costs that will be incurred.

CSA notes that many charities, which were created under state-based incorporated associations legislation, will now be faced with a parallel Commonwealth regulatory and reporting framework. While CSA welcomes the 12-month extension to reporting obligations that has been introduced, until such time as reporting for the sector is streamlined between Commonwealth and state governments, charities in the first instance (and possibly the entire sector in the future) are likely to be burdened with duplication of reporting.

CSA has previously recommended a referral of powers, as occurred with the Corporations Act, to ensure that charities in the first instance (and the entire NFP sector in time) have to respond to only one set of compliance obligations that operate nationally. However, given that such a referral of powers could take some time to effect, CSA recommends that consideration be given as to how best to ameliorate the burden of duplication of reporting. CSA suggests, for example, that one approach may be to put in place transitional arrangements whereby any charity currently reporting under state legislation is exempt from reporting under Commonwealth legislation until such time as the state legislation is repealed or a referral of powers is implemented.

CSA remains unclear as to how each legal form currently serving the sector will be brought into the regulatory framework without imposing additional compliance burdens. CSA notes, for example, that companies limited by guarantee are already subject to regulation by the Australian Securities and Investments Commission (ASIC), with a range of reporting responsibilities to ensure accountability and transparency, and their responsible individuals have duties as set out in the Corporations Act. Yet there is the potential in the current drafting of the proposed legislation which would potentially see its provisions apply to companies limited by guarantee in the future, thereby subjecting them simultaneously to two different regulatory frameworks. CSA believes that this is an unacceptable outcome, as it constitutes an expansion of compliance obligations rather than a reduction of them.

CSA understands that the intent is that companies limited by guarantee, even if incorporated under the Corporations Act, will automatically be regulated by the ACNC upon incorporation, but the exposure drafts do not clarify if this is so. CSA recommends that clarification is required as to how entities other than charities will be dealt with to ensure there is no duplication of reporting.

CSA also recommends that, in the same vein as the 'basic religious charity' exemption contained in the exposure drafts, consideration should be given to providing the Commissioner with the power/discretion to extend these exemptions to other types of organisations (for example, schools) where extensive reporting and compliance is already in existence and unlikely to be changed or amended as a result of the ACNC legislation, in order to ensure there is no duplication of reporting.

Governance standards and external conduct standards

CSA has previously welcomed and continues to support the introduction of principles-based governance standards for NFP entities. CSA welcomes the government's decision to deal with the governance arrangements which cover the content of a registered entity's governing rules, the conduct of the registered entity, and the processes that the registered entity must have in place in regulations established by the Governor-General. This provides a greater degree of flexibility concerning the establishment and future reform of any such standards. CSA notes that

these governance and external conduct standards have yet to be exposed for consultation and looks forward to providing feedback when they are released for public comment.

However, without further knowledge of how these governance and external conduct standards will be crafted, CSA is unable to comment on how the requirement in the exposure drafts for charities to comply with the governance standards will apply, or how charities will ensure that they comply with the requisite conditions of their registration. For example, in many respects, the imposition of the duty to notify, which is a new obligation that has not previously been the subject of consultation, will require a registered entity to notify the ACNC when it is non-compliant with the governance standards. Non-compliance will affect the charity's registration status and potentially expose the entity to the enforcement provisions of the proposed legislation, yet charities do not know what the governance standards will be, or whether they can comply with them. CSA is of the view that if the governance standards are genuinely principles-based, as promised, there should be little difficulty in charities being able to comply, particularly with education and support from the ACNC being provided to assist them to understand their compliance obligations. However, as noted previously, if the governance standards are prescriptive in nature, then charities will struggle to understand their compliance obligations and will need to seek external advice, at significant cost.

Notwithstanding this concern, CSA is encouraged by the statement in the explanatory materials that the standards:

are expected to be principles-based, specifying the outcome to be achieved, rather than detailing how an entity must meet the standards, in its particular situation.

CSA strongly recommends that the governance and external conduct standards and detail of financial reporting requirements be released for public consultation as soon as possible and prior to the bill being passed.

CSA is concerned that the Commission has the power, under the provisions of the exposure drafts, to remove a responsible entity, as a responsible entity may be an individual director. CSA notes that directors of incorporated entities are appointed by members and can only be removed by members, and that the power set out in the exposure drafts therefore grants more power to the ACNC than is granted to ASIC. CSA is of the view that this power needs to be revisited.

Financial reporting

CSA notes that the exposure drafts still contain some sections relating to the duties and financial reporting of entities that the ACNC will regulate (primarily concerning audit requirements). CSA strongly recommends that these matters are removed from the bills and dealt with in the regulations, as with all other aspects of financial reporting.

For example, CSA retains concerns that the draft legislation requires the reviewer to form a conclusion as to the financial report, access to information and record keeping, which are the same as the requirements for an audit. CSA notes that a review engagement is not designed to deliver the same level of assurance as an audit engagement. We suggest that the review requirement be clarified to ensure that organisations are not subject to audit requirements inadvertently.

A further area of concern however is the requirement for the audit report to describe 'any defect or irregularity in the financial report'. This is a very broad requirement which could be construed as a requirement to report on matters which would not normally be included in an audit report under Australian Auditing Standards where the auditor forms the view that the defect or irregularity is material.

CSA recommends that this could be replaced with an obligation similar to that imposed on auditors under s 311 of the Corporations Act. Under s 311 the auditor is required to report to the regulator where they have reasonable grounds to suspect a contravention of the Act, and it is

significant, or they have reasonable grounds to suspect a contravention of the Act that is not significant but will not be adequately dealt with by commenting on it in the auditor's report or bringing it to the attention of the directors (or responsible individual). However, this should be dealt with in the regulations under financial reporting, and not in the bill establishing the ACNC.

CSA commends the decision to provide for the possibility of entities that register separately to report together. However, without the regulations on financial reporting to hand to review, it is difficult to assess how this will operate. CSA is also concerned that the grouping of entities can only be done at the discretion of the Commission. CSA recommends that groups of entities that meet the 'control' definition in accordance with the relevant accounting standards should automatically be allowed to apply this collective and joint reporting framework.

We would welcome the opportunity to discuss any of our views in greater detail.

Yours sincerely

A handwritten signature in black ink, reading "Tim Sheehy". The signature is written in a cursive, flowing style.

Tim Sheehy
CHIEF EXECUTIVE