Submission to the House of Representatives Standing Committee on Economics

on the exposure drafts of legislation to establish the Australian Charities and Not-for-Profits Commission 2012

Victorian Government

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EXECUTIVE SUMMARY

This submission outlines the Victorian Government's position on the Australian Charities and Not-for-Profits Commission (ACNC) Bill and the ACNC (Transitional and Consequential) Bill 2012 exposure drafts (the Bills). Given the short time stipulated for providing submissions to the Committee, the Victorian submission has been limited to key issues only.

The Victorian Government supports efforts to minimise regulatory burden for the not-for-profit (NFP) sector, as evidenced by recent Victorian reforms. The Commonwealth has not established the case for regulating the governance of entities that currently are governed by State regulation (charities that are not companies).

The primary concern is that while the proposed reforms reduce duplication at the Commonwealth level, in many instances they are likely to *increase* duplication between the Commonwealth and States and Territories (States), nullifying the key objective of reducing the regulatory burden on the NFP sector. This has arisen because the role of the States as regulators has not been given due consideration.

Similarly, the proposed reforms have not yet been subject to a comprehensive Regulatory Impact Assessment (RIA). Noting that the problem of regulatory duplication has in part been deferred with the separate development of the regulations under the Bills, both the Bills and the regulations should be informed by the quantitative analysis and results of a detailed, jurisdiction- and sector-specific RIA.

Victoria notes that there remains a significant lack of clarity around the scope of the Bills, both in terms of the establishment phase of the ACNC and propositions for future expansion. Of primary concern, the definition of a charity is still not resolved. The Bills go beyond the current realm of Commonwealth responsibility and affect entities within the States' regulatory responsibility without setting out any mechanism for dealing with this overlap. This lack of clarity makes it difficult for the sector and for States as regulators to analyse the full effects of these Bills.

Given the concerns that remain, Victoria calls for greater and genuine consultation with States, in recognition of the key role they will continue to perform in the regulation of the NFP sector.

Recommendations

Victoria seeks to ensure that the stated objective of not-for-profit reforms – a transparent, efficient and appropriately regulated sector with a reduced regulatory burden - is achieved. The following recommendations will increase the likelihood that these aims can be met:

- The current and future scope of the ACNC must be revised and clarified.
- The Bills and regulations should be informed by a rigorous COAG-approved jurisdiction- and sector-specific RIA, which examines duplication between the Commonwealth and States. **Delaying the legislative timetable would enable this to occur.**
- A role for the States should be enshrined in legislation to ensure practical alignment between regulatory regimes and to provide for a high level of cooperation between regulators. This should include initial and ongoing approval of governance and external conduct standards by the Standing Council on Federal Financial Relations (SCFFR).
- Shared regulation options for the ACNC and State regulators in respect of those NFP entities regulated both federally and by a State should be enabled.

- The development of governance arrangements, standards and reporting frameworks should be more closely aligned to recent State–level reforms, such as the *Associations Incorporation Reform Act 2012 (Vic).*
- Provisions relating to audit and reporting should be consistent with existing State regulation to minimise cost and inconsistency.
- Proposed enforcement powers and penalties must be clarified for NFP entities regulated both federally and by a State.

These recommendations are discussed in more detail below.

1. Introduction

The Victorian Government welcomes the opportunity to comment on the Australian Charities and Not-for-Profits Commission (ACNC) exposure draft Bills.

The Victorian Government supports moves to consolidate the Commonwealth regulation of, and other involvement with, the sector. However, the case for a new national regulator, with greatly increased regulatory scope, has not been made out. Victoria's consistent position has been that State regulatory structures must maintain their functions and have complementary and co-operative relationships with Commonwealth regulation.

Having regard to the limited opportunity available to comment within the Standing Committee's consultation timetable, this submission outlines Victoria's key issues and is not a comprehensive assessment of the ACNC Bills.

Regulatory burden and the NFP Sector in Victoria

Victoria strongly supports the vital role played by approximately 120,000 NFP organisations operating in the State. Annually, the NFP and community sector delivers over $2.2 billion in Victorian Government services across a broad spectrum including aged care, children's services, environment, social services, law, sport, education and the arts.

The Victorian Government supports the objective of minimising regulatory duplication on charities, and the NFP sector more broadly, enabling organisations to focus resources on the important services and activities they deliver.

Regulation imposes significant costs on individuals, businesses, government and the economy. Governments should only look to regulate markets where there is a clearly identified risk of failure, and they should implement solutions that provide the most effective and least burdensome response with minimum government intervention.

Victoria has led efforts in Australia to reform the regulation of the NFP sector, and recommends the Committee have regard to the governance arrangements provided for in the *Associations Incorporation Reform Act 2012* as a model for best practice governance requirements for all NFPs including charities.

This recent reform process, focused on the approximately 37,400 incorporated associations registered in Victoria, involved extensive consultation with the sector and legal bodies involved in the regulatory system about ways to improve and streamline regulation. A copy of the *Associations Incorporation Reform Act 2012* is available at: http://www.legislation.vic.gov.au

Victoria is concerned to ensure that Commonwealth legislation to establish the ACNC enacts a reasonable, proportional and risk-based regulatory framework that supports charities and fosters community confidence and engagement with the sector without increasing burden.

2. Key Concerns

Victoria's key areas of concern with the ACNC Bills 2012 are:

Insufficient analysis of the "regulatory problem" and the duplicative effects of reform

Introducing new regulations, or amending existing regulation, should be done in response to clearly identified problems or failures in the market, and after a comprehensive analysis of the costs and benefits of different solutions that specifically target the problem.

The rationale for, and benefits of, imposing a new regulatory regime on NFP organisations which are not federally regulated entities have not been established. The NFP sector has a sound reputation for responsible governance and management and should not be exposed to an unnecessarily burdensome or complex regulatory regime.

Victoria does not consider the Commonwealth RIA undertaken in support of these reforms to be of sufficient scope or detail to justify additional requirements in respect of entities that are already regulated at State level. Victoria believes more can be done to quantify the analysis, and to identify impacts on jurisdictions. The RIA does not appear to include cost-benefit analysis, disclose assumptions, nor appear to have been assessed as adequate by the Office of Best Practice Regulation, which should be progressed as a first step. Victoria can provide more detailed comment on the RIA after the costs and benefits are appropriately identified.

In the absence of a demonstrated problem, such as widespread lack of transparency, diminished public confidence in the operation of charitable or NFP entities in Australia leading to reduced philanthropic contributions, or other threats to the viability and sustainability of the sector, there is no justification for proposing the creation of a new layer of regulatory oversight such as that established by the Bills.

Any legislative change should be clear and easily understood by those it affects. It is Victoria's view that if the Bills proceed in their present state and timelines, there will be significant confusion in the NFP sector. Victoria is concerned that confusion will be compounded by the Bills extending the reach of the ACNC to organisations that have not previously been regulated by the Commonwealth.

Commonwealth initiatives should not duplicate or disregard current State governance requirements, but rather recognise that there are existing frameworks in place. The proposed reforms largely marginalise the States' relationship with the NFP sector, which is both surprising and disappointing. This ignores the strong and balanced regulatory system currently in place at the State level, including the significant reforms that have been embarked upon, and the role of the States as significant procurers of services. This gap in the analysis also overlooks the significant benefits of subsidiarity and local knowledge in favour of a broad generic regulatory regime.

The Victorian Government supports the objective of "minimising regulatory duplication" for NFP organisations, especially with respect to existing Commonwealth regulations, which are concentrated primarily around tax and companies' legislation. While Victoria notes that much has been made of the potential benefit of the proposed reforms for those NFPs in receipt of funding from Commonwealth Government departments for service delivery, many of the regulatory hurdles faced by these organisations are caused not by legislative governance requirements, but rather Commonwealth service delivery contracts. This will not be resolved with the establishment of the ACNC.

Key areas of regulatory burden and regulatory duplication for the NFP sector identified by major reviews such as the *2010 Productivity Commission Research Report on the Contribution of the Not-for-Profit Sector* are in the areas of interstate or national fundraising and in grant and contractual reporting and acquittals. None of these issues is addressed by

the ACNC Bills.

What the Bills do instead is provide that those entities registered as charities with the ACNC will be subject to:

- new (additional) annual reporting and compliance obligations;
- extensive powers of regulatory oversight and intervention by the ACNC; and
- a range of new statutory obligations and offences.

The Victorian Government notes that, while the draft legislation reduces duplication at the Commonwealth level, it creates regulatory duplication between the Commonwealth and States. For example, of the 37,400 incorporated associations currently registered in Victoria, approximately 4,000 are also a charity. Approximately half of those organisations (2,000) also have Deductible Gift Recipient status with the Australian Taxation Office. This subset of State incorporated entities will be subject to duplicative regulation introduced by the Bills. In addition, there are approximately 511 non-distributing co-operatives that may also be subject to increased regulation.

There is a considerable risk that not only will the establishment of the ACNC lead to increased duplication, but that it will also have a disproportionate effect on small NFPs which are less able to absorb the costs and resource implications of additional regulation.

Poorly defined scope of the ACNC

It is significant to note that the meaning of the term “not for profit entity” for the purposes of the Bills remains uncertain. It is anticipated that consequential amendments will define the term "not for profit entity" - which is critical to the objects and structure of the entire ACNC. However, until defined, governments and the NFP sector face significant uncertainty regarding the ACNC’s exact scope.

For example, the ACNC Bill contains general statements that registration with the ACNC is "a prerequisite to access certain Commonwealth taxation concessions" (clause 15-5(3)) However, it is unknown which concessions will be included. Schedule 2 of the draft ACNC (Consequential and Transitional) Bill 2012 states that consequential amendments are still “to be drafted”.

The Bills also do not provide a mechanism for consolidation of existing Commonwealth regulation of NFP entities, including charities. If this is to occur, the relevant details would be expected to be included in consequential amendments (for example, to the Corporations Act), possibly supported by Memoranda of Understanding between the ACNC and existing Commonwealth regulators such as the Australian Securities and Investments Commission and the Office of the Registrar of Indigenous Corporations. In the absence of further information, Victoria is unable to comment on the extent to which the ACNC Bills reduce Commonwealth regulatory duplication for NFPs operating in Victoria.

The lack of clarity is of particular concern in relation to enforcement and penalties. The extension of the ACNC to NFPs which are charities regulated under State law raises serious issues with respect to enforcement and penalties.

Action by the ACNC against entities that are not federally regulated appears to be limited to revocation of registration or injunctions. The ACNC will not be able to issue warnings, give directions or accept enforceable undertakings if it considers the entity has, or is likely to, contravene penalty provisions (with the exemption of the external conduct standards).

This will mean that ACNC-registered entities regulated by either the Commonwealth or a State will be liable to different penalties for the same contravention or offence. This lack of regulatory proportionality is inconsistent, confusing, and unwarranted.

3. Victoria's recommendations for successful NFP regulatory reform

Victoria's proposed recommendations focus on best practice in the development of the Commonwealth's regulatory reforms.

3.1 Full examination of the regulatory impact of the Bills

Victoria has consistently emphasised the need for an RIA that complies with best practice principles. Given the vast differences in NFP entities, from global organisations to small localised sports and special interest clubs, it is imperative that the RIA be both jurisdiction- and sector-specific to analyse the impact on these very different entities. Without this analysis, it is not clear whether the Bills enact a reasonable, proportional and risk-based regulatory framework that supports charities, encourages community engagement and fosters confidence in the sector.

An RIA would also clearly identify those existing charities and entities that are currently regulated by the Commonwealth, and avoid the potential for the ACNC to impose additional red-tape on charities currently regulated by States.

Victoria is encouraged that the Commonwealth has agreed that COAG will be provided with a RIA, which identifies current and future regulatory duplication and provides options for avoiding or minimising this duplication. However, Victoria remains concerned that the Commonwealth's proposed timelines do not allow sufficient opportunity for the RIA to be considered and incorporated into the legislation or regulations. Victoria calls on the Committee to recommend that the Commonwealth ensure that, when the detailed RIA is completed, the outcomes are reflected in the reforms.

3.2. Consultation with States and Territories

Regulation of the NFP sector will continue to be a shared responsibility. While Victoria welcomes the statement in clause 185 (5) of the ACNC Bill that it does not override States' legislation, this now creates an uneasy tension where the duplication is acknowledged but not addressed. Victoria would like to see the Bills go further in addressing the duplication and acknowledging the important continuing role of States in the framework. It is in the interests of all parties to develop and agree ongoing arrangements to facilitate, as far as is practicable, seamless interaction between State and Commonwealth regulators, which minimises the burden on NFP entities.

Victoria has serious concerns that the Commonwealth's proposed approach risks creating significant confusion amongst NFP entities and existing regulators, leading to a complex and drawn-out reform process, with unnecessary and significant extra costs on the NFP sector.

The Commonwealth's NFP reform agenda is ambitious and includes multiple streams of work. Victoria is concerned that substantive and meaningful negotiation with the States must occur before finalisation of the Bills if there is to be a nationally-consistent regulatory system.

To avoid confusion, and to ensure a truly national approach, legislation intended to form the basis of a national system should be agreed by jurisdictions *prior* to introduction in Parliament.

Victoria calls on the Committee to recommend that the Bills are only finalised after full consultation and agreement with the States. Similarly, the governance and external conduct regulations should be developed in consultation with States, and be agreed by the SCFFR prior to introduction in Parliament. Any subsequent regulations should similarly be approved by the SCFFR, which should have ongoing responsibility to ensure that these are nationally consistent.

3.3 Shared operational approach for entities regulated federally and locally

Victoria notes, and supports, that a key focus of the ACNC is to ensure transparency and accountability of charities. This is to promote external accountability and foster community confidence and support for charities to which the public may provide funds.

By contrast, State regulatory frameworks for incorporated NFPs have a *dual* purpose of ensuring both external and internal accountability of the NFP entity to its members.

The ACNC Bills should reflect the ongoing role of State regulators in order to facilitate the best outcomes for the NFP sector. The legislation should also facilitate the new ACNC requirements without imposing additional burden on State-regulated NFPs by ensuring a co-operative approach to regulation.

Victoria therefore considers it is critical that the Bill provides for the ACNC to have a shared operational approach for entities regulated both federally and locally. This approach could include options for delegations and information exchange, such as:

- delegation of regulatory responsibility to State agencies, with State agencies as the primary regulator for charities, supported by the provision of detailed information to the ACNC;
- delegation of regulatory responsibilities by State agencies to the ACNC, with the ACNC as the primary regulator for charities, supported by the provision of detailed information to State agencies;
- ACNC and State agencies to both regulate in respect of charities, supported by detailed information exchange and collaboration, and/or delegation of specific regulatory requirements (for example, in respect of certain charities or functions);
- co-operative investigations with State agencies in respect of charities that are regulated by both levels of government; and
- sharing of information between the ACNC and State agencies for those entities regulated by both.

These arrangements would reflect the shared outcomes and intent of regulators, and with agreement on operational details, can maximise efficiency and effectiveness of the system by minimising the repetitive reporting and additional regulatory burden that the establishment of the ACNC would otherwise create.

The implications and implementation of these options will need to be considered, particularly for accountability, information sharing, privacy implications and enforcement purposes, but Victoria is of the view they present significant opportunities to provide a superior regulatory outcome for the sector and ensure the minimisation of regulatory burden and duplication.

3.4 Recognising the role of the States

Not only do States have the expertise to advise on best practice regulation, but alignment with existing State regimes is critical to avoid unnecessary regulatory burden and to enable implementation of a “report once, use often” framework.

States must have a role in determining the content of the governance standards and reporting requirements to be enshrined in regulations – both at the introduction of the ACNC Bills and as part of ongoing operational arrangements. The SCFFR is the appropriate body to undertake this role.

3.5 Governance arrangements, standard setting and reporting framework

The Assistant Treasurer announced on 17 May that the governance standards and reporting requirements would be extracted from the draft Bills, and later passed in regulations, following further consultation with the NFP sector.

Of particular concern to Victoria are the potential costs involved in the proposed reporting requirements. A simple solution is that reporting requirements be streamlined to specifically enable audits and reviews prepared under Victorian legislation to be accepted for the purposes of the ACNC, thus reducing duplication caused by the Commonwealth legislation.

The Bills empower the Commissioner to request additional information from entities and classes of entities. Victoria notes that these powers could be exercised to require information for up to six years in the past to undertake a "recognised assessment activity" on the grounds that "there is reason to believe" that an entity has breached the ACNC legislation (clause 60-80). "Recognised activity assessments" are defined in clause 55-10 to extend to registration, and compliance with the legislation and regulations. This power is therefore extremely broad, and unparalleled in Victorian legislation. Given that the regulations are yet to be completed, it is also uncertain what the reach of these powers will be. This has the potential to create significant uncertainty and administrative burden for the NFP sector.

Similarly, record keeping provisions require entities to retain records for "recognised activity assessments" (clause 55-5). As noted above, it is unclear what these assessments will capture, as this is not yet drafted, making this requirement both broad and uncertain.

Further, the ability of the ACNC to continue to treat an entity as small, medium or large, although its circumstances may have changed, under clause 205-25(5), has the potential to cause confusion for entities and their reporting obligations. This would need to be exercised with caution to prevent NFPs inadvertently failing in their reporting obligations if they move between entity categories.

There is also considerable potential for significant burden be placed on NFPs to comply with these powers. An appropriately light-touch regulatory approach would instead focus only on seeking additional information and reporting from entities where there is a strong rationale. The requirement for past information may also create administrative and regulatory burdens on NFPs, particularly where these entities were not regulated by the ACNC for the time period to which an ACNC determination relates.

3.6 ACNC powers and penalties

The Bills propose a broad range of powers for the ACNC, including extending power over non-Commonwealth regulated entities. For example, the Bills empower the Commissioner to suspend or remove responsible entities of registered NFPs (Subdivision 100-B). Under current definitions, this would capture trusts, which in Victoria are governed by the jurisdiction of the Supreme Court. This is an example not only of duplication, but of inappropriate powers of the ACNC in seeking to oust the legitimate jurisdiction of the Supreme Court of Victoria.

Victoria also notes that the Bills will create conflict between proposed and existing penalties for NFPs to be regulated both by the ACNC and States, as well as create new penalties. For example, the following breaches do not currently attract penalties in Victoria, but will under the draft Bills:

- Failure to give the Commissioner a statement within the required time;
- Failure by a registered entity to comply with a direction given by the Commissioner;
- Offence of a suspended or removed 'responsible entity' (e.g. director/trustee)

participating in decision-making that affects the business of the registered entity (strict liability);

- Offence of a suspended or removed 'responsible entity' (e.g. director/trustee) exercising the capacity to affect significantly the registered entity's financial standing (strict liability);
- Offence of a suspended or removed 'responsible entity' (e.g. director/trustee) communicating instructions to the remaining responsible entities (strict liability);
- Failure by an acting responsible entity to comply with a written direction from the Commissioner; and
- Failure by former trustee to give the acting responsible entity all books relating to the registered entity's affairs and identify and transfer property of the registered entity (strict liability).

Where NFPs are jointly regulated, the creation of the ACNC will in some cases introduce duplication of penalties for the same conduct across both jurisdictions. This "double jeopardy" regulation will potentially make NFPs liable to multiple and inconsistent penalties across jurisdictions. Furthermore, it is unclear how objections, review processes and appeals from penalties would operate in the event where NFPs were liable to both regulators for the same conduct.

Victoria reiterates its commitment to an effective and accountable NFP sector, and to working with the Commonwealth and other jurisdictions in the pursuit of this aim.