

**Inquiry into the Disclosure Regimes
for
Charities and not-for-profit Organisations**

**Submission
from
Group Training Australia Ltd**

August 2008

Executive Summary

Group Training Australia (GTA) Ltd is lodging this submission on behalf of its members.

GTA is the national association for a network of over 150 not-for-profit group training organisations (GTOs) operating from over 200 locations across Australia.

GTOs employ apprentices and trainees and hire them out to host employers for varying periods until the apprentice or trainee has completed their contract of training. A quick glance at some of the statistics on the number and characteristics of apprentices and trainees employed through group training arrangements is instructive. For example the group training network now employs:

- 13% of all new entrant apprentices and trainees;
- one in five traditional apprentices;
- one in five Indigenous apprentices and trainees;
- one in five school-based apprentices and trainees;
- one in ten apprentices and trainees with a disability; and
- increasing numbers of adult apprentices in the traditional trades.

This mechanism is uniquely Australian and has enabled many thousands of job seekers to secure an apprenticeship or traineeship which might otherwise not have been available to them.

This submission includes a comprehensive overview of the concept and origins of group training and the changing operating circumstances that have forced many GTOs to diversify in order to cross-subsidise their core business using funding derived from more profitable activities.

This submission also examines the concepts of 'community' and 'community service' in the context of considering how the not-for-profit sector should be treated for tax purposes.

Essentially we suggest that:

1. the term not-for-profit itself is misunderstood by people who believe that companies so classified should generate no surpluses and accumulate no reserves and that any redefinition should therefore seek to remedy this common misconception;
2. a whole of organisation classification approach should remain for not-for-profit organisations that meet appropriate criteria of community service. Rather than a "one size fits all" approach, it is suggested that there should be a process of "lifting of the corporate veil" to determine the underlying purpose of not-for-profit organisations ie. substance rather than form; and
3. on this basis, group training organisations should continue to enjoy not-for-profit status on their existing operations.

Introduction

Group Training Australia welcomes this opportunity to lodge this submission on behalf of its members in response to the inquiry into the disclosure regimes for charities and not-for-profit organisations.

You may be aware that this is a subject on which we have made submissions in the past. In 2000 we lodged a submission to the Treasury inquiry into the definition of charities and related organisations. In 2003 we lodged a further submission with the Board of Taxation commenting on the exposure draft of the then Charities Bill which was never enacted.

Given that the issues have not changed from our perspective we have drawn heavily on our 2000 submission in preparing this response to your inquiry. In doing so we have focused on the first term of reference as it gives us the scope to emphasise why the current arrangements are important to us and why any new arrangements would need to protect our interests.

Terms of Reference

(a) the relevance and appropriateness of current disclosure regimes for charities and all other not-for-profit organisations

We feel that the current arrangements are both relevant and appropriate to the circumstances of our member companies. We can best demonstrate this by informing you of the services they provide, the changing operating environment that they have had to contend with, and what outcome we need from the inquiry to ensure that our members can continue to fulfill their charter.

If you are persuaded by our arguments, and those of the many other organisations that are surely in a similar position to our own, we would expect that your recommendations will not be detrimental to our interests.

Before doing so however, it is worth making a comment on the very term not-for-profit. This term is much misunderstood, misleading and has bedeviled many organisations like the companies we represent. The term is commonly held to mean that any company that is incorporated as a not-for-profit should, as a matter of principle, ensure that its income does not exceed its expenditure thus preventing it from accumulating any surpluses or holding funds in reserve.

In other words, surpluses are held to be profits, which are assumed to be the exclusive preserve of companies that are in business to make money and distribute those profits to shareholders or members. This misconception shows a poor understanding of the principles of sound corporate governance and prudent financial management.

We regard our members as community service not-for-profit organisations with the emphasis on community service. They strive to generate surpluses, or make a profit if you will, as a matter of sound business practice and so that they might not only remain viable but also improve their services to the community.

This inquiry would do our sector a great service if any definition could lay to rest this misconception that not-for-profit means no surplus income.

The Concept of Group Training

GTOs employ apprentices and trainees and place them with host employers for varying periods until the apprentice or trainee has completed their contract of training. This network of companies collectively employs over 40,000 apprentices and trainees, or 13% of the national total, making it the largest employer of apprentices and trainees in Australia.

Our research indicates that over 50% of Group Training's host employers are small and micro businesses employing fewer than five (5) employees. Many of these businesses would not be involved in employment-based training if it were not for the services provided by Group Training.

The concept of Group Training began in the late 1970s in response to the needs of small employers in certain industries who were increasingly unable to commit to four year training contracts. Group Training offered employers the opportunity to engage an apprentice knowing that, if they ran out of productive work, the GTO would find an alternative placement and the apprentice could continue their training.

Group Training also proved to be an effective mechanism for placing the increasing number of out-of-trade apprentices whose employers were adversely affected by the economic downturns in the early 1980s and early 1990s.

While the earliest GTOs were established to meet the needs of specific industries, such as automotive and building and construction, and were often set up by the relevant industry association, an increasing number were established in regional Australia to serve the needs of local communities. Such companies would employ apprentices and trainees across a range of trades and occupations.

There are now GTOs serving most of regional Australia with most board members drawn from the local community and serving on a voluntary basis. Some boards are tripartite and include representatives of employer and employee associations as well as local government.

Group Training Organisations have strong connections with communities, whether it be within a particular region or, in the case of industry specific companies, with most of the key stakeholders dealing with employment and training issues within that industry. Whether industry specific or regional in focus, they are usually involved in more than just the core function of placing young people into training positions with host employers.

For example, most are now involved with schools in anything from providing careers advice to students, to managing and co-ordinating work placements for the increasing numbers of students undertaking vocational courses in years 11-12, to employing students as school-based apprentices and trainees. Their involvement in creating pathways from school to work for young people places

them at the forefront of efforts by governments to improve school to work transitions for young people.

Many GTOs provide community services using the skills and manpower of their apprentices and trainees. This might involve assisting the elderly or disabled with repairs and maintenance to their homes or project work in local clubs, parks and gardens. They also work closely with local councils, business chambers, and welfare organisations to enhance the lives of members of those communities and maximise the well-being of the community as a whole.

In addition to the convenience and flexibility they provide to host employers, GTOs also provide their apprentices and trainees with pastoral care at a critical time of their lives. Not only does the GTO field officer manage the training function and resolve conflict that might arise in the workplace, he or she may also find themselves dealing with personal crises as diverse as:

- homelessness
- suicide
- drug addiction; and
- relationship problems

Some GTOs have established foundations to assist young people in some aspect of their employment and training. Many disadvantaged young people, such as people with disabilities and Indigenous Australians, would not have obtained their trade qualifications had it not been for a GTO finding a position and supporting them through the duration of their training contract.

These activities have been well documented over the years. Many examples of this activity can be found in publications on the GTA website at www.grouptraining.com.au >National>Projects.

The Growth of Group Training

The growth of Group Training was assisted during the 1980s and early 1990s by the financial support of the ACTU-Lend Lease Foundation, which promoted the concept and facilitated the establishment of new companies.

Group Training subsequently attracted the support of governments, which could see the benefit they provided to young people seeking employment in the trades and the important contribution they made to national skills formation. In recognition of their efforts, not-for-profit GTOs started to receive government grants in the early 1980s to assist them with their operating costs.

As the number of GTOs grew, there followed a series of tax decisions, which were somewhat ad hoc, to provide them with various forms of tax relief. This included exemption from company tax, sales tax and in some cases, but relatively few, recognition as a public benevolent institution (PBI).

This last concession, which was granted to some and denied to others, gave some companies very significant benefits. It does, however, appear to have been applied inconsistently, which is curious in view of the fact that all GTOs share a common purpose and have the same core function.

Most GTOs initially incorporated under State/ Territory associations incorporation legislation, which provided a convenient and simple form of incorporation for not-for-profit companies. Over the years many more have incorporated as companies limited by guarantee and their constitutions reflect their not-for-profit objectives with the standard clauses precluding distribution of dividends to members and providing for the transfer of assets to another not-for-profit organisation with similar objectives in the event of their winding up.

Changing Operating Environment

The environment in which Group Training Organisations operate has changed dramatically since they were first established. GTOs have had to meet the challenges of a changed operating environment in order to survive.

Government support for Group Training has been diminishing for some time. In the early 1990s, the federal government moved to phase out operating support but subsequently rescinded this decision as a counter cyclical response to the recession of those years.

Even though most GTOs continue to receive operating support, the amount has not maintained its value in real terms. The quantum of funds available for operating support has not kept pace with the growth in the numbers of apprentices and trainees employed by GTOs, causing a diminution of the value of the support in per capita terms.

This reduction in the value of operating support is coupled with reductions in other funding, such as the value of employer incentives paid by the Commonwealth, and an increase in the costs of doing business, particularly those associated with occupational health and safety and the costs of workers compensation premiums.

The net result is that charge-out rates for apprentices and trainees have had to be increased to make up for this loss of operating support. At the same time companies have had to squeeze margins to ensure that they remain competitive and an attractive business proposition to host employers. The employment of apprentices and trainees is the first thing that host employers will dispense with if they need to cut costs.

This precarious funding situation has meant that GTOs have been forced, and indeed have been encouraged by government, to look elsewhere for alternative sources of funding that would enable them to become more self-supporting.

Consequently, many GTOs have expanded their operations and are now involved in the provision of a range of other services from which additional income is derived. These activities may include, but are not limited to:

- operating training facilities
- providing employment placement services, either independently or under contract from the Commonwealth as part of the outsourcing of the functions of the former Commonwealth Employment Service (CES)
- providing training and employment services under contract from State/ Territory governments; and
- providing traditional labour hire services

Group Training Organisations have been assisted in securing some of these alternative sources of income by a number of government reforms that have created commercial opportunities for both for-profit and not-for-profit companies in the non-government sector. In particular, these reforms include:

- opening up the training market to enable private training providers to compete with TAFE
- outsourcing a range of employment placement services, previously carried out by the former CES.

The alternative income stream provided by these commercial activities has effectively enabled many GTOs to cross-subsidise their core function from which little or no income is derived. This contention is supported by research conducted over the last 10 years or more and reported in:

1. A Best Kept Secret: Report on the Role and Effectiveness of Group Training Companies, House of Representatives Standing Committee on Employment, Education and Training, March 1995, page 9, para 2.15
2. Australian National Training Authority: Group Training Funding Model, KPMG Management Consulting, November 1997, page 68

While this diversification into other related commercial activities has its origins in the need to secure alternative sources of revenue, it is arguably also being sustained by factors other than pure financial need.

In particular, many GTO managers believe that there are also strategic considerations involved in assessing the need to diversify beyond the core function of Group Training. The opening up of markets that were formerly the preserve of the public sector has seen a proliferation of new service providers enter these markets, not always with positive consequences, other than to save governments money, at least in the short term.

There is a view held by many in the Group Training network that it is increasingly unwise for a Group Training Organisation not to tender for the provision of some of the other employment and training services that are on offer. The concern stems from the possibility that a GTO may find itself surrounded by a range of new service providers who do not necessarily work in partnership with the GTO and who may actively work against its interests.

These conflicts and tensions in the market place have often been cited by GTA during bi-lateral discussions with government.

Community Service Not-For-Profit

As indicated previously, Group Training Organisations are community service organisations in that they exist

- to work with communities,
- for the meeting of community needs through
- maintaining required levels and range of skills and in
- developing citizens through acquisition of skills and worthwhile employment.

GTA believes that any definition of a “community service” organisation must address the ultimate, underlying purpose of that organisation which should address in a significant way identified and agreed community needs. It must also exhibit operating processes that involve community representatives and institutions.

One aspect of community service organisations that is often overlooked is the ability to “get close” to the communities in which they operate. This often requires informal and less structured relationships than might apply in normal commercial circumstances. In addressing the notion of “community service” it would be inappropriate to ignore this aspect and try and introduce a relationship regime that was inflexible and reliant on form rather than substance.

It is also suggested that the term “community” may be variously interpreted. It could be geographical, industry, common interest. We do not have all the answers on this matter but think that the inquiry could benefit from a further look at this issue. Whatever the case, the important point to make is that organisations which provide community services respond to identified, legitimate needs other than their own survival and prosperity ie. they are outwardly focussed and pursuing objectives that are mutually beneficial, for themselves and the communities they serve. Their agenda for action is a shared agenda.

That said however they need to be viable. Following the introduction of the New Tax System on 1 July 2000, most Group Training Organisations were approved by the Australian Taxation Office (ATO) as Income Tax Exempt Charitable Entities (ITECs). Those that had full PBI status before the introduction of the New Tax System continued to enjoy this benefit.

The ITEC classification has enabled GTOs to bring all their commercial functions under this umbrella. This is the crux of the issue for our members. GTOs have diversified because it has become difficult to generate sufficient revenue from core business activity and undertake it to the standard that stakeholders, not the least of which is government, expect of them.

GTOs have been able to run these other business units at a profit, if we can use that expression, for the purpose of enabling them to carry out the business of Group Training. They are doubly served by the fact that much of this ancillary commercial activity is generally closely allied to their core business which enhances the provision of their services to their communities.

Moreover, as the legal employer of the apprentices and trainees, carrying out the business of Group Training means complying with laws that require the directors to ensure, inter alia, that the company's finances are in good order. Sound financial management means ensuring that the company has the reserves to meet a range of contingencies, which in the case of a GTO would include:

- funds to cover advance pays and holiday pays over the Christmas/ New Year period for upwards of 1,000 apprentices and trainees which is not recouped until host employers pay invoices anything up to 60 days later; and
- funds to cover down time when apprentices and trainees are returned by one host employer and cannot readily be found alternative employment with another, a phenomenon which is increasingly prevalent in the building trades or any other particularly cyclical industry

These reserves are accumulated profits by another name and can only be generated from profitable commercial activities.

Whole of Organisation or Activity-Based Assessment

The Treasury's 2000 discussion paper to which GTA responded at the time canvassed the common law interpretation of the definition of community service not-for-profit organisations and raised the possibility of an activities-based approach.

Although this no doubt derives some validity from Activity-Based Costing as a means of cost control in an industrial/administrative setting it is suggested that the more general application of such a principle requires some very serious examination. In effect it is suggested that the focus shift from the purpose for which an organisation exists to the specific activities undertaken in fulfilment of that purpose. Underpinning such a suggestion is the ability to "firewall" individual activities from each other, account for them separately and have them subjected to different legal and administrative treatments, whatever they may be.

Group Training organisations do not have the capacity to operate in such a way. The purpose for which they exist, the delivery of core group training functions, is

the singular focus of their activities, all of which are subordinated to the achievement of that purpose. It is not possible to think of their other ancillary activities as being anything other than supports to the main game. These activities do not have their own separate existence and any return on performance is applied to the total organisation.

In addition the managerial and administrative arrangements that would attach to the approval, ongoing conduct and reporting requirements that would inevitably be required would only serve to further divert precious resources away from the principal role of being a community service organisation.

Consequently, this Association has to strongly support the continuation of the notion of a whole of organisation assessment and point out that the removal or denial of benefits as presently understood to apply to not-for-profit organisations on this basis would drastically affect the viability of Group Training Organisations.

This applies not only to commonly accepted benefits such as income tax exemption and FBT rebate but also to specific requirements of not-for-profit status that attach to Commonwealth /State Government funding support to GTOs and possibly also to approval to operate as a Group Training Organisation under the legislation of some State and Territory governments.

Terms of Reference

(b) models of regulation and legal forms that would improve governance and management of charities and not-for-profit organisations and cater for emerging social enterprises

We do not believe we can add to this any more than has been raised above.

Terms of Reference

(c) other measures that can be taken by government and the not-for-profit sector to assist the sector to improve governance, standards, accountability and transparency in its use of government funds

The overwhelming majority of Group Training Organisations receive funding under what is now known as the Joint Group Training Program (JGTP). The JGTP is the source of funding that is mentioned above. It is no longer classified as operating support or recurrent funding. The program has long since been recast to become more consistent with the purchaser provider model so favoured by governments. Under this model outcomes are purchased by governments from any organisation in the market that meets certain eligibility requirements.

GTOs that wish to access these funds must comply with the Group Training National Standards. These set a basic level of operating standard which are designed to encourage continuous improvement in all aspects of the companies' operations including corporate governance. State Training Authorities (STAs) which administer the JGTP funds are also responsible for ensuring that GTOs comply with the standards by way of regular audits.

These measures, while not perfect, are believed to have been responsible for an overall improvement in operating standards since their introduction in 2002 and lifted the confidence of STAs in the probity of the group training network.

Conclusion

GTA Ltd thanks the Committee for the opportunity to make this submission to the inquiry and looks forward to its recommendations.

GTA Ltd will be pleased to provide the inquiry with any additional information it might need to assist in its deliberations.

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