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Dear Committee Secretary,

Thank you for the opportunity to provide a written submission to the 'Inquiry into the Disclosure regimes for Charities and not-for-profit organisations'.

This issue is an important one and the Mental Health Council of Australia supports the Standing Committee's efforts to examine the existing regimes, models of regulation and other measures within the not-for-profit sector.

The attached submission highlights key issues to be considered for the not-for-profit sector, with a particular emphasis towards improving the sector's sustainability through the implementation of reporting requirements and regulation reform in a flexible and well-considered manner.

If you would like to discuss this submission further, I can be contacted on (02) 6285 3100 or sebastian.rosenberg@mhca.org.au

Yours sincerely

A handwritten signature in black ink, appearing to read "S. Rosenberg".

Sebastian Rosenberg

Deputy Chief Executive Officer



**Inquiry into the Disclosure regimes for
Charities and
not-for-profit organisations**

Written submission by the

Mental Health Council of Australia

August 2008

There are more than 50,000 charities in Australia and their combined total income from Australian donors reaches almost \$3 billion annually. Of the 700,000 not-for-profit organisations in Australia, around half are incorporated, and only 35,000 of these employ staff. This accounts for 7% of the Australian workforce, which is over 600,000 employees. For the most part these organisations are entirely dependent upon the voluntary commitment of individuals (Woodward & Marshall, 2004).

The economic contribution of the sector is larger than both the mining and communications industry with an annual turnover exceeding \$30 billion and 4.7% of the Gross Domestic Product (NRNO, 2008).

These figures demonstrate the importance of ensuring effective governance and accountability for the sector. Regulation and standardized reporting requirements will ensure the integrity of the sector as well as increasing public confidence.

The difference between profit based and not-for-profit organisations relates to whether they are operating for the profit or gain of its individual members (ATO, 2008). The Australian Taxation Office (ATO) classifies an organisation as 'not-for-profit' if it can be established that its constituent or governing documents prevent it from distributing profits or assets for the benefit of particular people. Not-for-profits may be entitled to concessions in income tax, FBT and GST; however, this is not automatic, as certain other ATO requirements must also be met. Charities and other income tax exempt funds must obtain endorsement from the ATO prior to being able to access most concessions. The concessions available to not-for-profit organisations depend on how they are classified by the ATO, as outlined in Table 1.

Before not-for-profit organisations can receive tax concessions they must first be endorsed by the ATO. Part of this process requires that they have an ABN. The 'endorsement' means that organisations will have access to concessions. Those who are not endorsed must pay income tax, although they may be entitled to other tax concessions. GST is payable by organisations if their annual turnover is \$100,000 or more, although concessions may be available for 'endorsed' or certain other organisations.

At an individual level, it is widely accepted that staff working in the not-for-profit sector do not receive salaries comparable to those in the public sector. Traditionally, staff have been compensated through the tax concessions that these organisations receive. Through salary packaging and fringe benefit entitlements not-for-profit organisation employees are able to receive an enhanced income that is closer to what they would receive in the public sector. The work done by employees from the not-for-profit sector is invaluable and without these benefits individuals would almost certainly move to the public or private sector for significantly greater financial rewards. However it is noted that these benefits cannot be provided without proper standards and systems in place to ensure transparency and accountability to the relevant stakeholders. This is normal practice for the public sector and is systematically presented in annual and financial reports.

Table1: Summary of tax concessions and types of not-for-profit organisations

Tax concessions	Types of not-for-profit organisations				
	Charities			Income tax exempt funds	Other not-for-profit organisations
	Public benevolent institutions & Health promotion charities	Charitable institutions	Charitable funds		
Income tax exemption	✓ (1)	✓ (1)	✓ (1)	✓ (1)	✓ (2)(8)
FBT exemption (subject to capping)	✓ (1)				✓ (3)(8)
FBT rebate		✓ (1)			✓ (4)(8)
GST concessions for charities and gift deductible entities	✓ (1)	✓ (1)	✓ (1)	✓ (5)	✓ (5)(8)
GST concessions for non-profit organisations	✓	✓	✓		✓
Deductible gift recipient	✓ (6)	✓ (6)(8)	✓ (6)(8)	✓ (6)	✓ (6)(8)
Refunds of franking credits	✓ (7)	✓ (7)	✓ (7)	✓ (7)	✓ (7)(8)

(Source: ATO, 2008)

Notes to the table

1. The entity must be endorsed by the ATO to access this concession.
2. Only certain types of not-for-profit organisations are exempt from income tax. Many not-for-profit organisations are taxable, but may be entitled to special rules for calculating taxable income, lodging income tax returns and special rates of tax.
3. Public and non-profit hospitals and public ambulance services are eligible for this concession.
4. Certain non-government non-profit organisations are eligible for this concession.
5. The entity must be a deductible gift recipient to access this concession.
6. The entity must be endorsed by the ATO as a deductible gift recipient to access this concession. The only organisations that do not need to be endorsed are those listed by name in the tax law, including prescribed private funds.
7. The entity must be an income tax exempt charity, income tax exempt fund, or deductible gift recipient to access this concession.
8. Relates to certain types only.

Reporting requirements

The reporting requirements for the not-for-profit sector are determined by their legal structure, which can be varied and regulated by State/Territory or Federal legislation. The structure and regulation then dictates the organisation's reporting requirements which can range from none to extensive.

There needs to be some set 'minimum standard reporting requirements' taking into consideration the size and resources of the organisation. That is to say there should be a minimum level of reporting requirements for every organisation with the level of accountability to increase proportionately with the size of the organisation and/or its annual turnover. Without financial reporting requirements, organisations are vulnerable and more open to criticism. Requirements should be stipulated according to standardized not-for-profit regulation rather

than being dictated by the various Acts that organisations may be bound by due to their legal entity status.

The modern meaning of 'charity' does not have the same meaning as it once had with charities now including groups that have a number of areas of interest including the environment, human rights and various lobbying and political motivations (Johns, 2004).

Donors are not necessarily aware of how their donations are applied and might be surprised if they were. In all likelihood the majority of not-for-profits are acting appropriately and disbursing their funds in accordance with their published organisational mission statement and strategic plan, in a manner that would hold up to donor scrutiny. Checks and balances need to be in place to ensure that public confidence is maintained. Given the diversity of the not-for-profit sector, regulation is a difficult and daunting prospect particularly considering that the needs and issues of not-for-profit organisations vary considerably.

The requirements upon a large charity with an annual turnover of \$100 million will be substantially different to a small voluntary organisation running exclusively on donations received from a small number of people. Donors undoubtedly assume that the money they give will be used for the purpose that they donated it i.e. if they give money to a particular appeal, most people would like to think that their money will be used for that purpose. The Red Cross Bali Bombing Appeal is a good example of how this can go wrong. When it was revealed that donations were not being used exclusively to assist bombing victims the Red Cross suffered a significant public backlash which in turn affected donor trust in other charitable organisations.

If regulations were in place regarding reporting of the application of donated funds then this may have been avoidable. Currently donors have no way of ensuring that their donation is used for the purpose for which it was donated and not for other purposes (Murray, 2006). Standardised reporting requirements by not-for-profit organisations will boost transparency and confidence by donors at both the organisation and sector level.

Regulation reform

The regulatory framework for not-for-profits is complex and inconsistent with a lack of nationally consistent reporting obligations. The report 'A Better Framework – reforming not-for-profit regulation' involved a survey of 1,700 not-for-profit companies. They found that the main differences between not-for-profit and profit-based organisations were the following:

1. they rely heavily on volunteers;
2. they enjoy exemptions from income tax; and
3. they have more stakeholders to consider.

It was also identified that there are a myriad of options available regarding possible legal structures for newly forming not-for-profits. The National Roundtable of Nonprofit Organisations reported that there are more than 20 different ways to incorporate a not-for-profit organisation.

To achieve not-for-profit organisations that are transparent, accountable and able to withstand public scrutiny a number of changes need to be made. This will only be possible through the instigation of regulatory frameworks, standards and set disclosure requirements (Woodward and Marshall, 2004).

Their report put forward four recommendations for reform on this issue, including the following:

1. a single Commonwealth regulatory regime;
2. ASIC becoming the new regulator for all incorporated not-for-profits until a new not-for-profit regulator can be introduced;
3. the establishment of a specialist not-for-profit section within ASIC; and
4. a plain language guide and replaceable rules for not-for-profit organisations.

They also identified the need for the implementation of additional support services for not-for-profits including an advisory body that could provide low or no cost auditing, financial and taxation advice, legal advice, training for board members, dispute resolution and mediation for stakeholders.

With regard to public disclosure requirements, as long as not-for-profits are able to receive various tax concessions, therefore have the benefit of public funds through tax foregone, there should be a correlating responsibility through disclosure to the public. Of course the requirements would need to vary depending on the size of the organisation.

By implementing reforms and standardising the sector the not-for-profit sector will achieve a high level of transparency which will result in increased sector confidence. Currently the sector regulations are ad hoc and resources are being wasted on duplication and unnecessary and burdensome requirements. Any proposed solutions need to be simple but uniform with the flexibility to be augmented on a case-by-case basis to deal with the varied complexities of organisations large and small (Murray, 2008).

By streamlining the system not-for-profits would be better able to utilise their time and efforts on service delivery and capacity development. In this way organisations can move towards self-sustainability which would reduce the need for support from government grants and funding.

Sustainability

An example of this is the recent identification by the Mental Health Council of Australia (MHCA) that there was a need for an investment in the infrastructure of the mental health sector. With the Department of Health and Ageing's (DoHA) agreement, considerable time was spent planning how best to deploy this one-off program funding to achieve capacity growth in the sector. Consultations occurred with relevant MHCA members, including state peak bodies and some of the practices that have been employed elsewhere in the community sector were reviewed. The work of Nonprofit Australia and the reform that has taken place with the injection

of new national funding into the alcohol and other drugs sector provided some useful guidelines in how non-government organisational capacity building can work.

On this basis, together with consultations with various stakeholders including DoHA, it was agreed that the design of the Project would include two key elements:

- organisational possibilities workshops; and
- a capacity enhancement grants program.

What followed was the running of 14 workshops held nationally which involved showcasing best practice to smaller NGOs to assist them in thinking more laterally and directing their focus to building the foundations of their organisations rather than being all-consumed with service delivery. This was then followed up with the release of over \$6 million in grants whereby organisations could then utilise up to \$40,000 to address any capacity deficiencies within the organisation. Both aspects of the Program have elicited an overwhelmingly positive response with the project currently in the process of distributing project funds.

This is the first time that such an initiative has been undertaken by the Government and the feedback has been resoundingly positive. The majority of organisations, particularly the smaller ones, had not stopped to consider 'capacity building' as their time and efforts are usually solely focused on service delivery. By integrating the concept of capacity building and into the other raised issues of standardization and disclosure, the not-profit-sector can start seeing itself as a self-sustaining economic contributor rather than the "poor cousin". The MHCA has spent considerable time and effort encouraging organisations to strive for self-sustainability and projects such as the NGO Capacity Development Project are vital in re-programming the thought processes of these organisations. While the Project was successful, it is recognized that a one-off project won't yield long-term or ongoing benefits. Recurring projects and accompanying funding need to be available until the sector is able to stand on its own two feet. A major factor in achieving this sustainability will be the implementation of the recommendations put forward by the various bodies as cited in this submission.

Given the constant and consistent research and recommendations about what needs to happen, it is well and truly time for action. There is no disputing the significant contribution that the not-for-profit sector makes to the Australian economy and it is time that this was given the support and resources needed to enable organisations to improve their own efficiency and effectiveness in a long term and sustainable way.

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