



The General Manager
Corporations and Financial Services Division
The Treasury
Langton Crescent
PARKES ACT 2611

Dear General Manager

Re: Financial Reporting by Unlisted Public Companies

I am replying on behalf of the National Roundtable of Nonprofit Organisations to the invitation by the Hon Chris Pearce, Parliamentary Secretary to the Treasurer to provide comments on the issues raised in the above paper.

The National Roundtable of Nonprofit Organisations represents a broad cross section of the nonprofit sector in Australia and has a strong interest in better regulation of the nonprofit sector, including better corporate regulation and reporting. We also have an associated interest in the development and establishment of accounting standards which are better tailored to the needs and circumstances of nonprofit organisations in Australia.

Information about the Roundtable and its structure and objectives are attached to this submission.

The Roundtable has a strong interest in securing regulatory frameworks and requirements for nonprofit organisations which:

- are tailored to the varied needs of different types and sizes of organisations;
- contain accountability requirements which take account of the different needs and circumstances of nonprofit organisations from those which generally apply to private sector organisations; and
- are calibrated and proportional in terms of the nature and size of organisations and the associated risks associated with non-compliance with requirements and necessary good governance and stewardship of funds.

We therefore welcome and support the consultation process being undertaken by Treasury and are pleased to provide the following comments and any additional information or commentary which might be helpful in the context of Treasury's further development of the ideas contained in the Discussion Paper.

Yours sincerely

David Thompson AM
Chair
17 August 2007

Financial Reporting by Unlisted Public Companies

Submission to Treasury Consultations by

The National Roundtable of Nonprofit Organisations Limited

August 2007

Introduction

The National Roundtable of Nonprofit Organisations believes that all nonprofit organisations should be required to meet accountability requirements which take account of their size and purpose and which are tailored and proportionate to the wide diversity of size, purposes and activities of different nonprofit organisations. In that context, while we seek to reduce the burden of unnecessary and often costly regulatory requirements on nonprofit organisations, we also promote the need for better regulation which might in some instances mean more or different regulation.

In the context of the current consultation process, audited financial statements have an important role to play for some organisations in achieving necessary accountability for the way in which they manage their financial affairs and their stewardship of the financial resources they derive from members', government, philanthropic donors, business and the general public.

Nonprofit organisations exist and operate to achieve their purpose, rather than to achieve profits for their owners or shareholders. Accordingly and unlike for profit entities, they should be required, in addition to reporting to regulators and stakeholders on their financial performance, to also report on the extent to which they are achieving their purpose. This would go towards achievement of accountability on the basis of their primary reason for existence and assist in building and maintaining necessary trust and confidence from the many stakeholders which nonprofit organisations serve.

Accordingly, the Roundtable supports and endorses the views provided by the Queensland University of Technology Centre for Philanthropy and Nonprofit business on the need for introduction of requirements for reporting on achievement of purpose using narrative, financial and other measures. We also note that the UK Charity Commission (which has already implemented reporting requirements along these lines for charities) and the Office of the Third Sector are currently consulting on further reporting and accountability changes (http://www.cabinetoffice.gov.uk/third_sector/news/news_stories/070614_consultation.asp) which might usefully inform future developments in the Australian context.

Issues for comment:

- A. *Do you support the introduction of a differential reporting regime based on size for companies limited by guarantee? If so, what do you consider to be the appropriate criteria (both in terms of the indicators of size and the quantum of those indicators) for differentiating between those companies that are required to report and those companies that are exempt?*

The Roundtable strongly supports a proportional and differential approach to reporting and other regulatory requirements for nonprofit organisations – on the basis that all companies limited by guarantee should be required to prepare financial reports with differentiation on the standards of reporting and the requirement for audit. We suggest that the differential should be based on revenue as a reasonable proxy for levels of risk and the need for higher levels of accountability. The setting of the income or revenue thresholds for differential reporting could be somewhat arbitrary but could be informed by the costs of preparation of different levels of reporting and audits. It should also be noted that harmonisation of the requirements for reporting and auditing by incorporated associations would also be required to ensure that there is national consistency (the tables attached to the Discussion Paper illustrate well the significant inconsistencies which now operate across states and territories for associations) and no distortion of the choice of legal form which entities could choose for incorporation in the different jurisdictions.

- B. *Do you believe it is appropriate to differentiate between companies limited by guarantee by the nature of their operations rather than just size? If so, what nature of operations do you believe warrants greater transparency?*

The Roundtable believes that size (as measured by revenue) represents the best and most workable approach in this context. The wide diversity and mixes of activities undertaken by many nonprofit entities would make judgements by activity type difficult and complex and hard to implement in a consistent and objective manner.

- C. *Do you consider that companies limited by guarantee that receive any money through grants should have financial reporting requirements? If so, can this obligation be satisfied by the company providing special purpose financial reports to the grantor rather than preparing general purpose financial reports under the Corporations Act?*

Government agencies and other organisations which provide grants and other forms of financial assistance to nonprofit organisations impose extensive and often complex, costly and onerous reporting and acquittal requirements which they tailor to their own accountability needs and requirements. Many also require whole of organisation financial statements and audits in order to provide assurances about sustainability, viability and solvency. On that basis there should continue to be a requirement under the Act for general purpose financial reports.

- D. *If you support some companies limited by guarantee being exempted from financial reporting, what percentage of members should be required in order to require an exempt company limited by guarantee to prepare a financial report?*

The Roundtable does not support exemption for some companies limited by guarantee from financial reporting. Should the proposal to adopt differential levels of reporting and audits for organisations of different size be adopted, those entities which have lesser levels of requirements could be required to provide a higher level of reporting and/or auditing as a consequence of a resolution of members at a members' meeting or a decision of the Board. Companies limited by guarantee do not have voting shares it is not necessary to stipulate a percentage of members other than that required to carry any resolution under than that which generally applies to general meetings. ASIC should be able to require an organisation to undertake higher levels of reporting or auditing in circumstances where it has reasonable grounds for doing so.

- E. *If you support the retention of financial reporting requirements for all companies limited by guarantee, do you consider that there is scope to reduce the amount of financial information these*

companies are required to report? If so, what type of financial information do users need companies limited by guarantee to report (for example, related-party disclosures)?

As previously noted, all companies limited by guarantee which exceed the stipulated revenue threshold should be required to file and publish financial statements which are audited in accordance with relevant accounting standards (which we believe also need to be tailored to the particular needs and circumstances of nonprofit organisations). Companies which fall below the threshold should be required to produce financial reports which are not audited but for which an accountant can certify that the accounts have been kept in a manner consistent with good accounting practice and which are consistent with the needs and interests of its members. All companies limited by guarantee should be required to report on any related party disclosures to meet transparency and good governance requirements.

F. *Do you consider that there is a need to harmonise the financial reporting requirements of companies limited by guarantee and incorporated associations to provide a consistent reporting framework for not-for-profit entities in Australia?*

As noted in our comments relating to A above, it is important that there is harmonisation so there is a nationally consistent reporting framework for nonprofit entities and to avoid any distortions in the choice of legal form which entities adopt. The tables attached to the Discussion Paper clearly demonstrate the significant inconsistencies which currently apply to incorporated associations in different states and territories.

G. *In order to assist in progressing this project, it would be useful to obtain an indication from companies limited by guarantee of the cost of preparing a directors' report and audited financial report as required by the Corporations Act.*

The Roundtable does not have systematically collected and reliable information about the costs of preparation of directors' reports and audited financial statements as required under the Act for different sized and types of companies limited by guarantee. Many smaller companies report that audit costs represent a significant and disproportionate burden which would be obviated if they were not required. ASIC could usefully collect this information to better inform consideration of the costs of regulation for companies limited by guarantee.

H. *If some companies limited by guarantee were to be exempt from financial reporting, do you consider there is value in these companies continuing to be subject to some level of non-statutory external assurance as a means of promoting good governance? If so, what should this assurance relate to and how do you think this regime should be introduced (for example, through best practice guidelines issued by the professional accounting bodies)?*

The Roundtable does not support any exemption from financial reporting but would support the development and dissemination of good practice governance, accounting and reporting guidelines which could be issued by ASIC and/or the professional accounting bodies and by relevant sector peak organisations in some cases.

I. *For those companies limited by guarantee that are required to prepare financial statements, do you consider that there is a need to change the current audit requirements? If so, which aspects of the current requirements need to be reformed?*

For those organisations which would require an audit as a consequence of their revenue being over a stipulated threshold, or because it is sought by the Board, members or by ASIC, present audit requirements should continue to apply

J. *Do you support amending the Corporations Act so that companies limited by guarantee are specifically prohibited from distributing profits to members in the form of dividends?*

Amendment of the law to include such a prohibition might have some benefits in terms of obviating the need for the ATO, other regulators and other stakeholders to ensure there is an appropriate non-distribution clause in constitutions. This needs to be weighed against the need to consider allowing for distribution of profits by new and emerging hybrid legal forms which might be adopted by various types of social enterprises – along the lines of the UK's Community Interest Companies.