

NSW GOVERNMENT COMMENTS

CONSULTATION PAPER -REVIEW OF NOT-FOR-PROFIT GOVERNANCE ARRANGEMENTS

THE AUSTRALIAN CHARITIES AND NOT-FOR-PROFITS COMMISSION (ACNC): EXPOSURE DRAFT LEGISLATION

1 Introduction

- 1.1 The Commonwealth Government announced a range of measures as part of the 2011-12 Budget designed to improve and simplify the regulatory framework for the not-for-profit (NFP) sector at the Commonwealth level. These measures included:
 - reforms to Commonwealth tax concessions provided to the unrelated commercial activities of NFP entities;
 - the establishment of the Australian Charities and NFP Commission (ACNC) by 1 July 2012; and
 - the introduction of a statutory definition of charity for all Commonwealth laws from 1 July 2013.
- 1.2 The Commonwealth Government has committed to progress these reforms in consultation with State and Territory governments (herein referred to as the States) through the Council of Australian Governments (COAG).
- 1.3 The NSW government is actively participating in intergovernmental discussions to consider the implications of the reforms proposed by the Commonwealth for entities currently interacting with the State and State government bodies.
- 1.4 NSW recognises the significant economic, social, cultural and environmental benefits delivered through and by NFP entities, identified by the Productivity Commission in its 2010 Research Report, *Contribution of the Not-for-Profit Sector*.
- 1.5 NSW is committed to reducing the regulatory burden on the NFP sector to allow organisations to focus resources on the important services they deliver. As such, the NSW Government must carefully consider the impacts of any proposed changes to ensure that it produces better outcomes for NFP entities and the broader community.
- 1.6 State governments have considerable experience in managing state taxes (and any exemptions), and regulating fundraising, charitable trusts, unincorporated and incorporated associations. Therefore the role and functions of the ACNC must be carefully considered in order to create a regulatory environment that is streamlined, suitable and acts to remove regulatory duplication and promote continued participation.
- 1.7 Both the NSW and Victorian governments have recently reviewed their regulatory requirements for incorporated and unincorporated

associations in close consultation with the NFP sector, adopting a risk management approach. It will be important that any reforms at the Commonwealth level do not undermine the red tape reductions achieved in these and other jurisdictions.

- 1.8 Importantly, all Governments, through COAG, have undertaken to ensure regulatory processes in their jurisdiction are consistent with agreed best practice principles that will ensure regulation is only applied where necessary to address an identified problem and generates the greatest net benefit for the community.
- 1.9 To ensure regulatory action is effective and proportional to the issue and minimises restrictions on competition governments need to clearly consider a range of feasible policy options and consult effectively with stakeholders. It is also important that effective guidance is provided to regulators and regulated parties to ensure compliance requirements are clear.
- 1.10 A regulatory impact statement (RIS) discussing these options and impacts is normally prepared to canvass the regulatory options available in order to determine the relative merits of different regulatory approaches. NSW notes that the Commonwealth expects to release a RIS and this should inform discussion of the costs and benefits of various regulatory and governance options for the diverse range of NFP stakeholders.
- 1.11 NSW notes that a new statutory definition of charity is also under consideration by the Commonwealth and, once legislated, may impact government and/or Deductible Gift Recipient entities and funds operated by government or in support of government activities (e.g. Parents and Citizens Associations that provide vital financial and other support to public and private schools).
- 1.12 NSW considers that the establishment of the ACNC will not obviate the State's need to retain the power to determine NFPs eligibility for NSW tax concessions and other non-financial regulatory requirements that fall outside the ACNC functions.
- 1.13 NSW notes that resolution of the treatment of (charitable) social and affordable housing providers is particularly pressing, given the commitment by all jurisdictions to the significant growth of the not-for-profit community housing sector.
- 1.14 It is envisaged this sector will play a key role in addressing housing affordability and homelessness issues in Australia. Therefore, the Commonwealth needs to consider the potential overlap in administration between the proposed National Regulatory System for Community Housing Providers and the regime to be administered by the ACNC.

2 Australian Charities and Not-for-profits Commission Bill

General Comments

- 2.1 NSW notes that the object of the Bill is very broad, that is, “to promote public trust and confidence in NFP entities that provide public benefits”. The Commission’s powers to monitor and investigate and refuse or revoke the registration of entities covered by the legislation are only constrained by the defined objects of the Bill. NSW would support legislative clarification of the Bill’s objects to ensure any regulatory activity authorised by the Bill does not unduly inhibit NFP participation, activity and innovation.
- 2.2 Governance principles are under consideration but are yet to be decided. Given the importance of these principles for ACNC's operation and the potential for regulatory burden for NFPs, NSW considers that they should have status within a legislative instrument.
- 2.3 NSW notes that the exposure draft does not currently include important content such as the appropriate governance for specific entities, transitional arrangements and consequential amendments to other legislation. A full consideration of the reach of the proposed legislation and the extent of potential penalties for non-participation cannot be completed without this detail. NSW would be happy to provide additional comments to the Commonwealth when these provisions have been finalised.
- 2.4 The establishment of the ACNC supports the Commonwealth’s initial response to the Productivity Commission’s Report recommendations by setting up a ‘one-stop shop’ for registering NFPs for Commonwealth purposes, clarifying access to Commonwealth tax concessions for NFPs and introducing a statutory definition of charity.
- 2.5 Through the explanatory material, the Commonwealth has signalled its intention that the role of the ACNC will expand to include responsibility for the regulation of all NFPs in Australia. The Bill has been drafted to reflect an expansive regulatory role for the ACNC, consistent with this longer term view.
- 2.6 NSW is concerned this approach could pre-empt the outcome of future consultations with governments and the sector.
- 2.7 The Commonwealth and the States have not yet agreed to a model of ‘national regulation’ that will concurrently meet each government’s policy objectives to reduce red tape and maximise the contribution of the NFP sector. NSW believes that further consideration and discussion is required as to the most appropriate model and associated transitional provisions, particularly for the estimated 440,000 small and unincorporated NFP entities (see Productivity Commission Report).
- 2.8 It may be more appropriate for the Bill to reflect the role and functions of the ACNC in the short term as a ‘one-stop shop’ for registering and

regulating charities for Commonwealth purposes and for any consequential and transitional amendments to tax and other legislation to be likewise limited.

- 2.9 To assist the NFP sector, the legislation and the explanatory materials would benefit from clarification in several respects to show how the legislation is intended to operate in the short term while the States must continue to carry out their responsibilities in the regulation of incorporated associations, charitable trusts, fundraising and administration of State tax exemptions.

Constitutional limits

- 2.10 NSW, firstly, seeks clarification on section 2-15(e), "...for purposes relating to the granting of financial assistance to a State" as to its intent and purpose in relation to the regulation of State government bodies and the NFP sector.
- 2.11 NSW also notes that the Bill states the constitutional limits of the Commissioner under Section 2-15. This section gives the Commonwealth legislative power to validly enact the Bill in its limited application. However, as noted above, it would appear the object, powers and functions of the Commission have been drafted in anticipation of a greater level of legislative authority than has yet been considered or agreed by governments.
- 2.12 The Commonwealth does not at this time have the constitutional power to regulate the NFP sector on a comprehensive basis. Therefore, the Commonwealth must rely on a "patchwork" of powers to make laws in the area, such as the power with respect to taxation, constitutional corporations, external affairs and trusts with corporate trustees. The limits of the "patchwork" of powers are uncertain.
- 2.13 The Commonwealth has noted that one way to achieve constitutional certainty for its proposal for broad regulatory powers would be for a referral of State powers to the Commonwealth. However, this proposition is not under active consideration by COAG, although a COAG NFP Working Group has recently been established to consider possible regulatory harmonisation and other red tape reduction options.
- 2.14 The Commonwealth might still achieve practical comprehensive regulation without State cooperation processes through the use of incentives and penalties, particularly to the extent that the Bill may be a law with respect to taxation, trustee corporation and corporations powers. While registration under the ACNC is not mandatory, failure to register may jeopardise an entity's access to these tax concessions, grants and other benefits.
- 2.15 The Commonwealth and the States deliver substantial financial grants to NFPs of all sizes. Significant taxation concessions and exemptions are also extended to many NFPs. Commonwealth concessions include exemptions from income tax, fringe benefits tax, goods and services

tax, and the granting of franking credits and deductible gift recipient status.

- 2.16 Without seeing the consequential amendments in these various areas, it is hard to determine the intended reach of the Commission which is an important element for States and the NFP sector in the impacts of the proposed reforms.
- 2.17 Under section 109 of the Constitution (Inconsistency of laws), "When a law of a State is inconsistent with a law of the Commonwealth, the latter shall prevail, and the former shall, to the extent of the inconsistency, be invalid." The extent of any such conflict or overlap will depend on the precise terms of the regime.
- 2.18 The Bill does not clarify its relationship with other common law or equitable obligations and those arising under State statute law, and there is no explicit statement of the Commonwealth's intentions as to whether it will be the exclusive and exhaustive law on NFP regulation, or whether it will be intended to operate "concurrently" with State law. Where it is important for State laws to continue to operate, the Bill should specifically exclude those matters from the operation of the Bill or provide that, in the event of inconsistency or conflict, State law will prevail. It is important that these issues be clarified.
- 2.19 It is worth noting that Chapter 5D of the Corporations Act 2001 contains extensive provisions as to the regulation of trustee companies and generally they apply to the exclusion of all State laws dealing with the same subject matter. However, there are some exceptions – see section 601 RAE(2), (3) and (4), and section 601 WBK of the Corporations Act 2001 dealing with trustee companies.

Registration of not-for-profit entities: section 4-1.

- 2.20 The Bill provides the Commissioner of the ACNC with the power to register NFP entities under their specific NFP type or subtype. The entitlement to registration is very broad and fails to reflect the actual role and functionality of the ACNC in its initial years of operation when it is only intended to register charities, according to the proposed codification of current common law principles.
- 2.21 The Commonwealth has announced that it will introduce a statutory definition of charity for all Commonwealth laws from 1 July 2013. From this point, it is expected that the ACNC will determine charitable status according to Commonwealth legislation rather than the common law.
- 2.22 Whether the list of charitable purposes at section 5-10 is appropriate and has a strong enough definition by referring to common law is still subject to consultation. It is particularly important that the list is limited to those purposes that have a strong recognition in the existing common law and that future changes to this list are very carefully considered. Given the diversity in the NFP sector and the regulatory

activities of governments, it may be necessary to consider different criteria for specific types of entities or activities.

- 2.23 The aim of the legislation is to establish a regulatory regime that covers entities, either incorporated or not, which engage in charitable activities or operate to provide a public benefit through the use of public funds or concessions. Registration entitlement criteria include the requirement that the entity is a NFP entity.
- 2.24 The Bill fails to adequately define a NFP entity. Hence it is possible that the ACNC responsibility will extend to a broader range of entities. States have many incorporated associations and co-operatives that do not pursue charitable objectives nor do they receive public funding, but they may receive tax concessions. It is unclear if these entities are entitled to register under the ACNC Bill, which potentially captures them because of the lack of definition of 'not for profit entity' or the lack of any limit to the categories of entities it seeks to cover.
- 2.25 The position of NFPs that do not pursue charitable objectives nor receive public funding is not clear under the registration entitlement provisions and there is an absence of information about what impact this will have upon any current tax concession that would be available for these entities.
- 2.26 Many NFPs will continue to need to register with the States to gain incorporated status and may also need to register with the ACNC to avoid loss of their tax concessions and government grants. These entities may find themselves subject to additional reporting obligations, and monitoring and enforcement action.
- 2.27 There is also a great possibility that many unincorporated associations will fail to meet the requirements stipulated in the Bill and in the governance requirements to be determined by the ACNC. The NSW government will need to carefully consider the outcomes from the RIS with respect to the identified impacts, costs and benefits of applying such legislation and governance requirements to these entities.
- 2.28 The exposure draft and explanatory materials have not yet provided detail on what is required in constituent documents for entities required to be registered with the ACNC.
- 2.29 NSW seeks clarification as to whether the new national registration arrangements would permit incorporated associations to operate across State boundaries.

Reporting

- 2.30 NSW strongly supports the inclusion, in section 55-90, of a provision to allow an accounting period other than the financial year to be adopted.
- 2.31 NSW supports legislative clarity around the term "annual information statements". What are they and what will be required to be reported in

the annual statement by entities? In addition, the penalties for inaccurate, late and non-submission should be proportionate and be stipulated in a legislative instrument. Hence we are also then interested in how this will impact on our information sharing which depends on the detail that is required for these statements.

- 2.32 For NSW to assess opportunities to use these information statements to reduce reporting by charities there needs to be clarification on the extent of information required from small, medium and large NFPs and for surety to exist around the continuity of requirements. This might be better achieved by the inclusion of requirements in the Bill or subordinate legislation. NSW notes that consultation around these requirements is currently being considered through other processes.
- 2.33 The requirement that financial statements and notes must be prepared in accordance with Australian Accounting Standards and that audits or review must be undertaken by a registered company auditor, within the meaning of the *Corporations Act 2001* may impose a significant additional workload and cost on some charities and NFPs. It may also lead to a reduction in the level of pro bono services for NFPs if accountants/auditors have an increased workload for addressing general accounting needs of NFPs.
- 2.34 NSW is also concerned about any changes that increase compliance costs for organisations, many of which have minimal administrative staff or are completely volunteer run. Even small additional requirements could have a detrimental impact on the delivery of an organisation's programs and could act as a disincentive for these organisations to seek private giving to diversify their income.

Charitable Trustees

- 2.35 NSW is concerned about the proposals that will enable the ACNC to suspend or remove trustees and enforce directions, contained at section 143-120. Policy considerations in respect of the appropriate governance regime to apply to trustees are distinct from those that apply to other "responsible individuals", such as directors or individuals who are involved in decision-making of the registered entity. These differences are due to the distinct legal obligations of trustees under NSW law (similar obligations are likely to apply under other State/Territory laws), and the supervisory powers of the Court and the Attorney General in relation to charitable trusts.
- 2.36 Under existing NSW law, a trustee can only be removed in accordance with the terms of the trust instrument or by an order of the Court. The Court's power to remove a trustee is in its inherent equity jurisdiction and it will not easily be exercised. In considering such a course, the Court considers not only the due and proper administration of the trust and the interests of the beneficiaries but also the confidence reposed by the settlor in the selected trustee (*Guazzini v Pateson* (1918) SR(NSW) 275, 294).

- 2.37 The role of a trustee is an onerous and often long-term responsibility. The wishes of the settler (who, often in the case of charitable trusts established by testament, may have since died) should not be overlooked without due cause. Removal of the trustee may require the appointment of a new trustee if there are no remaining trustees. We are concerned that, in taking on this role, the ACNC will assume what is currently a judicial function. NSW queries what guidelines or protocols will be used to ensure that removal and subsequent appointment of trustees is appropriate and without bias.
- 2.38 The Department of Attorney General and Justice and NSW Trustee and Guardian (NSWTG) are of the view that the wishes of the settler who created the trust should be respected and be given considerable weight. The removal of a trustee and appointment of a new trustee are important decisions that a Court is best placed to make.
- 2.39 NSW is also concerned about the potential for the duties of a charitable trustee under NSW law to conflict with a registered entity's duties under the Bill, e.g. compliance with directions issued by the Commissioner may conflict with a trustee's duties under the terms of the trust deed, a court order, the NSW Trustee Act 1925 or the Charitable Trusts Act 1993.
- 2.40 Therefore, it is considered that the ACNC should not have the power to suspend, remove or enforce directions against trustees. Other more appropriate means of enforcement are available under a wide range of enforcement powers. These include revoking registration (thereby removing tax concessions) and/or pecuniary penalties.
- 2.41 Therefore, NSW laws relating to trustees should apply concurrently with the Commonwealth law, and in the event of inconsistency or conflict, should prevail.
- 2.42 The ACNC regulator should not have the power to suspend or remove trustees, or appoint new trustees, or make directions that conflict with trustees' duties under NSW law.

ACNC Register

- 2.43 Section 100-10 looks at the disclosure of information on the register that the Commissioner will maintain. NSW notes that the secrecy framework is concerned largely with ensuring compliance with Commonwealth government privacy principles. However, the Bill will enable certain personal information to be disclosed, e.g. the name of responsible individuals will be disclosed on the Register.
- 2.44 Section 100-10(1)(q) provides the Commissioner can require any other information relating to each registered entity that he or she considers reasonably necessary for the purposes of administering this Act. This provision delegates significant powers to the Commissioner given the broad object of the Bill. Provisions extending additional regulatory requirements with potential penalty implications would normally be found in subordinate legislative instruments and amendments subject to the application of regulatory impact criteria.
- 2.45 While not explicitly required in the Bill, NSW considers that Private Ancillary Funds and charitable trusts which do not seek donations from the general public, should not be required to disclose confidential information such as the names of individual donors. It may also be appropriate that all donors should have the capacity to determine the disclosure of information about their donations to reduce the potential for a significant reduction in donor activity.
- 2.46 Different disclosure requirements apply to a trustee as, for instance, a trustee has a duty of confidentiality and obligations to account to a beneficiary concerning the administration of the trust assets. (For this reason, for example the NSW TG is specifically excluded from the disclosure requirements under the Government Information Public Access Act 2009). We submit that similar considerations should apply in respect of public disclosure of NFP entities which are private charitable trusts.

Reviews and Appeals

- 2.47 NSW notes that the review and appeal provisions are yet to be drafted. Given the breadth of the ACNC's powers, the nature of decisions that may be made under the Bill and the likelihood of those decisions affecting people's interests and possibly the viability of NFP entities, we think that a merits review should apply in respect of the ACNC's registration and compliance decisions.
- 2.48 NSW seeks clarification on how the reviews, appeals and penalties process will work if NSW in the future agrees to adopt/adhere to this Bill and accept the definition of charity for one or more purposes. State objections, interest and penalty provisions would still apply, but NSW would be interested in knowing how and if the Commonwealth provisions have an impact and/or interact with State provisions.

- 2.49 NSW notes that there is also a risk that an NFP organisation funded by a State agency could have its registration with the ACNC revoked, thereby affecting its ability to provide its agreed funded services. This highlights the need to establish clear protocols between State funding bodies and the ACNC to ensure effective management of such a situation and the maintenance of adequate services. This will particularly apply during any transition period.

Secrecy

- 2.50 NSW is concerned that ACNC officers cannot be compelled to produce or disclose protected Commission information to a court or tribunal (section 180-15(3)) unless it is necessary to give effect to the Act. The effective administration of justice requires that courts be able to compel the production of relevant information in court proceedings, unless a privilege applies. We do not think that the regulatory and investigatory functions of the ACNC are sufficient reason to derogate from the general principles of the Evidence Act 1995.
- 2.51 NSW supports authorised disclosure by the ACNC to an authority of a State or Territory under section 180-25. Information sharing may enable NSW to work constructively with the Commonwealth to simplify tax concession arrangements for charities and NFP entities.

3 Explanatory materials

Reporting and auditing

- 3.1 Reporting requirements of NFP entities are not consistent and can sometimes be duplicative. However, given the diversity of the NFP sector, and the different relationships that NFP entities can have with different Australian governments, it is important that the explanatory material and the notes to the legislation are clear on what the 'report-once-use-often' general reporting framework for registered entities can actually provide.
- 3.2 The NSW Office of State Revenue (OSR) will continue to administer NSW taxes and concessions provided to various entities, including charities and NFPs. NSW will continue working with the Commonwealth and other jurisdictions to identify opportunities to streamline reporting requirements.