

# Final Report

## SCOPING STUDY FOR A NATIONAL NOT-FOR-PROFIT REGULATOR



**Australian Government**

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**The Treasury**

APRIL 2011

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ISBN 978-0-642-74718-1

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# Glossary

## Terms

Australian Accounting Standards Board	AASB
Australian Business Register	ABR
Australian Prudential Regulation Authority	APRA
Australian Securities and Investments Commission	ASIC
Australian Taxation Office	ATO
Canadian Revenue Agency	CRA
<i>Commonwealth Authorities and Companies Act 1997</i>	CAC Act
<i>Corporations (Aboriginal and Torres Strait Islander) Act 2006</i>	CATSI Act
<i>Corporations Act 2001</i>	Corporations Act
Council of Australian Governments	COAG
Deductible Gift Recipient	DGR
Financial Action Task Force	FATF
<i>Financial Management and Accountability Act 1997</i>	FMA Act
Internal Revenue Service (United States)	IRS
Ministerial Council on Consumer Affairs	MCCA
Not-for-profit	NFP
Office of the Registrar of Indigenous Corporations	ORIC
Public Benevolent Institution	PBI
Standard Business Reporting	SBR
Standard Chart of Accounts	SCOA

## Reports

1995 Industry Commission Inquiry Report, <i>Charitable Organisations in Australia</i>	Industry Commission Report
2001 Report of the <i>Inquiry into the Definition of Charities and Related Organisations</i>	Charities Definition Inquiry
2008 Senate Economics Committee <i>Inquiry into Disclosure Regimes for Charities and NFP Organisations</i>	2008 Senate Inquiry
2010 Productivity Commission Research Report, Contribution of the Not-for-profit Sector	PC Report
2010 <i>Review into Australia's Future Tax System</i>	AFTS Report
2010 Senate Economic Legislation Committee Inquiry into the Tax Laws Amendment (Public Benefit Test) Bill 2010	2010 Senate Inquiry

## Executive summary

This final report concludes the Government's 2010 election commitment for a scoping study for a national 'one-stop shop' regulator. As part of the scoping study, the Government released a consultation paper on 21 January 2011 which sought stakeholder comment on the goals of national regulation, the scope of national regulation and the functions and form of a national regulator. Consultation closed on 25 February 2011 and 161 submissions were received. Consultation was also undertaken with state and territory officials, sector representatives, and representatives from overseas governments and non-government agencies who have been involved in the NFP reform process in their respective jurisdictions.

This report presents findings of the study and provides the Government with a blueprint to implement a national NFP regulator.

Since the implementation of a national regulator is dependent on the cooperation of the states and territories, the report also sets out immediate and short term options to improve regulation and reduce red-tape at the Commonwealth only level.

Chapter one provides a background of the current regulatory environment of the NFP sector, including statistics on the sector as well as a discussion of its diversity. It documents the reviews and inquiries into the regulation and taxation of the NFP sector in Australia over the last 15 years, starting with the 1995 Industry Commission Report. The chapter concludes with a discussion of the outcomes of the recent consultation process as well as the objectives and discussions of this report.

Chapter two discusses the goals of NFP regulation, noting the significant stakeholder support for the goals of harmonisation and simplification in relation to reporting requirements as well as proportionality of regulation. The chapter recommends that the stated goals of NFP reform should be used to guide the NFP reform process.

Chapter three considers the scope of regulation of the NFP regulator, including the treatment of different legal forms of NFP entities as well as the role of existing regulators. It recommends that a principles-based regulatory framework be established, where the principles of regulation apply broadly across the NFP sector, regardless of entity type or industry. The chapter also recommends the introduction of a single regulator, with reporting to other regulators, such as ASIC, to be removed. The chapter notes that the role of sector specific regulators should be the subject of further review.

Chapter four discusses the registration function the regulator could perform, noting the potential efficiency gains that would result from a centralised registration process. It recommends that the regulator should determine the NFP status of entities, including charities and PBIs, with the determination being accepted by every Commonwealth agency. The chapter further recommends that the Australian Government work with state and territory authorities (through the COAG process) to ensure that the regulator's determination of NFP status applies throughout Australia, and be accepted by every government agency.

Chapter five focuses on the statutory definition of charity. The chapter reveals general stakeholder support for the introduction of a statutory definition, consistent with the recommendation of a number of reviews and inquiries already informed by public consultation. The chapter recommends the definition be based on the 2001 Charities

Definition Inquiry, noting the recommendations of the recent 2010 Senate Inquiry. The chapter further recommends that the definition of charity should be harmonised across Australian jurisdictions and the Government undertake further consultation before it is implemented.

Chapter six considers educative functions, recommending that the role of the regulator should be to assist in educating the sector about governance and reporting standards and support understanding of the new regulatory arrangements.

Chapter seven discusses fundraising, noting the high regulatory burden that results from inconsistent fundraising regulation and legislation across the states, territories and the Commonwealth. Given the complexity of the legislation, and the importance it has in supporting the work of NFP entities, the chapter recommends that the regulator work with the states and territories through the Ministerial Council for Consumer Affairs to review current fundraising arrangements.

Chapter eight provides an overview of the current reporting requirements applying to NFPs, noting their ad hoc, uncoordinated, complex and duplicative nature. The chapter discusses respondents' views on the 'report-once, use-often' framework concluding that such a framework would likely improve transparency and reduce compliance costs. It recommends that the regulator act as a central reporting coordinator of financial information.

Given that there is currently no single source of public information on the activities of charities and other concessionally taxed NFP entities, chapter nine considers the desirability of a public information portal. It compares developments in this area in overseas jurisdictions and recommends that the Government proceed with a portal for registered entities, with the regulator responsible for its establishment and maintenance.

Chapter 10 discusses governance, disclosure and compliance requirements, noting that while some NFPs have effective policies in place, most NFPs do not. The chapter documents the preference by respondents for a principles-based governance approach and recommends the implementation of organisational governance rules that are proportional to the size of entities, risk factors involved the extent of public and government assistance than an NFP receives.

Chapter 11 discusses options for the form of a national regulator and examines three alternatives for its establishment, namely, a referral of powers by the states to the Commonwealth, a cooperative legislative regime based on model Commonwealth legislation, or, a cooperative legislative regime based on model state legislation. The chapter concludes with the recommendation that the Commonwealth pursue the long term objective of a single national regulator and regulation of the NFP sector, noting the requirement to work with the states to achieve this outcome.

Noting that most regulated entities in Australia currently pay regulatory charges to contribute to, or cover, the cost of regulation, the final chapter considers funding options for the regulator. The chapter considers the arguments for and against a regulatory co contribution and recommends that the Government delay consideration of the collection of a co-contribution until the question of the possible replacement of existing fees has been determined.

Finally, we would like to thank all the stakeholders, academics and officials who provided us with valuable assistance in the preparation of this report.

# Summary of recommendations

## Goals

1. The goals of NFP reform, as outlined in the consultation paper, should be used to guide the NFP reform process.

## Scope of national regulation

2. A single regulator should be established for the purposes of governance, accountability and transparency of NFPs.
3. The NFP regulator should, as far as possible, be responsible for regulating all NFPs.
4. Entities that are currently regulated by ASIC should be incorporated within the regulatory framework as soon as new reporting and governance frameworks are implemented. ASIC should still retain responsibility for incorporation.
5. The regulator should administer a principles-based regulatory framework which would apply broadly across the NFP sector, although regulation should be proportional and tailored to address the specific needs and size of NFPs.
6. The options for reform in areas which require the cooperation of the Commonwealth, states and territories should be progressed through the COAG agenda, including the areas of incorporated associations and charitable trusts.
7. Further reviews should be undertaken in areas where there are opportunities for further reform. This may include reviews of existing regulators and the legal form of NFPs, including the company limited by guarantee structure.

## Registration

8. The NFP regulator should determine the NFP status of entities, including charities and PBIs. Initially, the regulator's determination should be accepted by every Commonwealth agency. The regulator should initially focus on determining the status of charities including PBIs, with this focus gradually extending to include all other NFP entities.
9. Through the COAG process, the Australian Government should work with state and territory authorities with the aim of ensuring that the regulator's registration applies throughout Australia, and be accepted by every government agency.
10. Entities should apply to have their status determined by the regulator on a voluntary basis. However, to access support provided by the Australian Government, and any state and territory governments that agree following conclusion of the COAG process, a NFP entity would need to be registered and regulated by the NFP regulator.

11. Administrative decisions taken by the NFP regulator should be subject to internal review; independent review by the Administrative Appeals Tribunal; and a right to appeal to the federal courts.

## Definition of charity

12. The definition should be based on the 2001 Charities Definition Inquiry, noting the recommendations of the recent 2010 Senate Inquiry, and taking into account the findings of recent judicial decisions, such as *Aid/Watch Incorporated v Commissioner of Taxation*.
13. The definition of charity should be harmonised across Australian jurisdictions.
14. The Government should undertake further consultation on the definition of charity.

## Education and compliance

15. The regulator should produce educational materials for the sector, including a centralised portal of information for NFP entities, web based training, 'how to' guidance materials, phone assistance, referral services for organisations requiring external advice, and ongoing consultation with the sector.
16. The regulator should also play a role in relation to educating the public about the sector, including through the oversight of complaints, concerns and surveys about its satisfaction with the sector.
17. Where possible the regulator should leverage off the existing resources and expertise already provided to the sector by peak bodies and government agencies.

## Fundraising

18. Issues common to both the national NFP regulator and NFP fundraising projects should be reviewed by the Government, with coordination between a national NFP regulator and the Ministerial Council for Consumer Affairs' current consideration of fundraising issues.

## Reporting

19. A 'report once, use often' approach should be adopted in relation to financial reporting from NFPs. Reporting should reflect 'smarter regulation' and the trade off between standard reporting and simple reporting should be carefully considered as part of the development of the standard report.
20. The regulator should act as a central reporting coordinator of financial and other information and as such should:
  - be responsible for the SCOA;
  - harmonise reporting requirements between Commonwealth, state, territory and local governments; and

- determine the form of the financial report in consultation with the NFP sector and government agencies.
21. Each entity should provide information for reporting purposes but the content should be proportional to the size of entities, risk factors and level of sector and government assistance. Small entities should be required to provide no more than a post card of information.
  22. The AASB should continue to ensure that Australian accounting standards take account of NFP issues and identify any gaps in this area.
  23. The regulator should work with the AASB to provide guidance on NFP accounting issues.
  24. Acquittal reporting should be outcomes based and should not include financial reporting or reporting related to organisational governance.
  25. Consideration should be given to bringing acquittals reporting within the regulator's 'report once, use often' framework where possible.
  26. Consideration should be given to utilising SBR for NFP reporting.

## Information portal

27. The Government should proceed with a public information portal for registered entities.
28. The information portal should be established and maintained by the regulator.
29. The portal should be operated in consultation with and link with the ABR.
30. The information to be displayed on the portal could include information on issues such as sphere of operation, income and expenditure, financial history, contact details of persons managing the entity, governing documents, annual reports, trustees' reports, and summary information returns.
31. NFPs should be allowed to control some of the content on parts of the site.
32. NFPs should be able to make qualitative statements about their activities and performance.
33. The portal should provide NFPs with centralised government guidance and information.
34. The portal should allow links to other websites, including those which provide information on other Government accreditation and licenses.

## Governance, disclosure and compliance

35. Organisational governance rules should be proportional to the size of entities, risk factors and receipt of public and government assistance.
36. The regulation of service provision should remain with existing entities.

37. Government contracts should no longer mandate organisational governance requirements for NFPs.
38. Treasury should undertake a review to determine what, if any, should be the core organisational governance principles applying to registered NFPs.
39. Over the long term, the regulator should be provided with powers regarding asset protection, the suspension and/or removal of responsible persons, registration and deregistration, the enforcement of governance rules, investigative processes; enforcement powers, including civil penalties and the imposition of fines, proportional compliance activities, and, dispute resolution processes.

## The form of the national regulator

40. The Commonwealth should pursue the long term objective of a single national regulator and regulation for the NFP sector, noting that the Commonwealth does not have the constitutional power to implement this alone.
41. The Australian Government should seek agreement with the states and territories on a single national regulator through COAG.
42. As setting up a national regulator will take time, the Government should improve Commonwealth regulation for the sector in the interim, ensuring that regulatory overlap at a Commonwealth level is removed.

## Funding of a national regulator

43. The Government should consider whether or not to collect a supervisory co-contribution, as NFP entities are brought within the new regulatory framework and once it is possible to replace existing fees.
44. If a supervisory co-contribution is adopted, it should be tiered to reflect the resourcing constraints of smaller NFP entities.

# Chapter 1

## Introduction — The current NFP regulatory environment

### The NFP sector

The NFP sector broadly consists of entities which seek to achieve a community, altruistic or philanthropic purpose, and who are involved in the supply of goods and services that have a social value greater than the price that a consumer could or would otherwise pay. The NFP sector can also be defined in broad terms, as encompassing all those in the economy who are not households, government or businesses that operate for profit.

The NFP sector is characterised by its diversity, with entities ranging from micro-sized sporting and recreational clubs to large national and multinational charitable organisations. The sector consists of approximately 600,000 entities, and contributes around \$43 billion to GDP per annum.

NFPs have a long history of delivering services to their members, their clients or to the wider community such as through the provision of welfare, education, sports, arts, worship, culture and community services. Through providing opportunities that promote self connection and influence, the sector lays the foundations for an active civil society.

### Current statistics

The NFP sector is growing in size and importance to the Australian economy. The NFP sector grew at an average rate of 7.8 per cent per annum in the period from 1999-2000 to 2006-2007.<sup>1</sup> This is partly due to the growing trend for governments to contract with NFP entities to undertake service delivery. This has significantly changed the way the sector is funded, and the related requirements to better manage risk and return have resulted in a need to improve the simplicity and transparency of regulatory arrangements for the NFP sector.

In addition to its growing economic role, the sector also makes a significant contribution to the wellbeing of Australians. The PC Report noted four broad ways that NFPs contribute to community wellbeing: through service delivery and concomitant opportunities for participation; by exerting influence on economic, social, cultural and environmental issues; through connecting the community and expanding social networks; and by enhancing community endowment through skills and asset investment. Given the importance of these benefits to both current and future generations of Australians, it is vitally important that the sector is well regulated so that it remains accountable to the communities it serves.

In recognition of the vital economic and social role it plays, the Government provides significant support to the sector. Government funding to the sector in 2006-2007 was

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1 Productivity Commission Report, Contribution of the Not-for-profit Sector, 2010, p xxix.

\$25.5 billion. Overall government funding has grown from 30.2 per cent of sector income in 1999-2000 to 33.2 per cent in 2006-2007.<sup>2</sup>

Governments have traditionally provided funding to the sector to pay for the sector's delivery of programs and services on behalf of governments. For example, the Australian Government currently provides \$444 million through the Family Relationship Services Program to NFPs to provide family services such as counselling.

Substantial funding is also provided to the NFP sector through government expenditure on education, for example, non-government schools were provided \$14.9 billion in 2008, and higher education providers were provided \$11.4 billion in 2009.

In addition, Commonwealth, state, territory and local governments provide a range of generous tax concessions to eligible NFP organisations, including an income tax exemption, DGR status, refundable franking credits, and fringe benefits tax, goods and services tax, land tax, payroll tax and municipal rates concessions.

Total quantifiable Commonwealth tax expenditures provided to the NFP sector in 2010-2011 were estimated to be in the order of \$3.3 billion. Unquantifiable tax expenditures to the sector are likely to be of similar magnitude. For example, the 2009 *Tax Expenditures Statement* states that the income tax exemption for charities is unquantifiable but estimated to be in excess of \$1 billion per annum.

State tax expenditures to the sector, (not published by all states) are also substantial. For example, Victoria's tax expenditures to the NFP sector were estimated to be in the magnitude of \$759 million in 2009-2010.

The community also provides significant support to the sector. Total philanthropic donations to the sector reached \$7.2 billion in 2006-2007<sup>3</sup> and an estimated value of \$14.6 billion was provided in volunteer time.<sup>4</sup>

## Recent reviews and inquiries

There have been several reviews into the regulation and taxation of the NFP sector in Australia over the last 15 years, starting with the 1995 Industry Commission Report. The sector has largely supported the recommendations made by these reviews and has called for prompt government action and implementation of a reform agenda.

A consistent theme has emerged from these reviews that the regulation of the NFP sector should be significantly improved by establishing a national regulator and harmonising and simplifying regulatory and taxation arrangements.

The 2001 Charities Definition Inquiry recommended consideration of the establishment of a comprehensive national administrative framework for the charitable and related sector and an independent administrative body for charities and related entities.

The 2008 Senate Inquiry recommended the establishment of a single independent national regulator for NFP organisations.

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2 Productivity Commission Report, Contribution of the Not-for-profit Sector, 2010, p54.

3 Productivity Commission Report, Contribution of the Not-for-profit Sector, 2010, p72.

4 Productivity Commission Report, Contribution of the Not-for-profit Sector, 2010, p53.

The Committee further recommended that the national regulator should have similar functions to regulators overseas. The Committee proposed a broad role for the NFP regulator, including:

- registering NFP organisations;
- educating the sector and encouraging compliance;
- educating the public about the role of NFP organisations; and
- developing and maintaining an accessible, searchable public information portal.

The 2010 AFTS Report recommended that a national charities commission should be established to monitor, regulate and provide advice to all NFP organisations.

The AFTS Report recommended that a charities commission should also be tasked with streamlining the NFP tax concessions (including the application process for gift deductibility), and modernising and codifying the definition of a charity.

The PC Report recommended the establishment of a 'one-stop shop' for Commonwealth regulation by consolidating various regulatory functions into a new national registrar. The Commission further recommended that while ultimately the registrar could be an independent statutory body, it should initially be established as a statutory body corporate within ASIC.

The PC Report recommended that the regulator undertake a variety of functions including:

- assessing the eligibility of NFP organisations for Commonwealth tax concession status;
- endorsing and maintaining a register of endorsed organisations;
- registering and regulating NFP companies limited by guarantee;
- providing a single reporting portal for corporate and financial information; and
- investigating compliance with regulatory requirements.

The 2010 Senate Inquiry recommended the establishment of a single independent national commission for NFP organisations.

The Committee recommended that the regulator undertake a broad range of activities including:

- promoting public trust and confidence in the charitable sector;
- encouraging and promoting the effective use of charitable resources;
- developing and maintaining an accessible, searchable public interface;
- processing annual returns submitted by charitable entities;
- monitoring charitable entities and their activities to ensure that registered entities continue to be qualified; and
- monitoring and promoting compliance with relevant legislation.

## Election commitment

In its 2010 election campaign, the Government committed to strengthen the NFP sector, through:

- a new Office for the NFP Sector supported by a new NFP Sector Reform Council;
- a scoping study for a national 'one-stop shop' regulator for the NFP sector, to remove the complex regulatory arrangements currently in place and streamline reporting arrangements;
- greater harmonisation and simplification between Commonwealth, state and territory governments on NFP issues, including regulation; and
- reducing red-tape for government funded NFP organisations.

The Government tasked Treasury with undertaking a scoping study to determine the role, functions, feasibility and design options for a 'one-stop shop' NFP regulator.

On 21 January 2011 the Government released a consultation paper on the design options for a national NFP regulator.

The consultation paper discussed the features of a best practice regulatory framework and sought the views of stakeholders in relation to:

- the goals of national regulation;
- the scope of national regulation;
- the functions of a national regulator; and
- the form of a national regulator.

## Outcomes of the consultation process

The Government released a consultation paper on 21 January 2011 to ascertain the views of the sector on the goals of national regulation, the scope of national regulation and the functions and form of a national regulator. Consultation closed on 25 February 2011 and 161 submissions were received.

The consultation process demonstrated significant support for a national regulator and national regulation, and for NFP reform to be a priority.

Many of the proposals in the paper, such as the goals of regulation, received broad support, in the consultation. However, it should also be noted that in some instances, issues of contention may arise on the detail of proposals which received support in the consultation. In these instances further consultation on detailed proposal will be appropriate.

Some submissions, acknowledged that the process of simplification and harmonisation will be time consuming. Taking a partnership approach and building trust will allow the reform process to be successful.

The need to undertake a careful and thorough approach to reform that does not duplicate or increase compliance costs for the sector was a key theme of the consultation. Many submissions queried how current duplication could be avoided, given the range of requirements across different levels of government and different agencies within the one level of government. Some submissions doubted the ability of these 'disparate' government agencies to work together.

Some submissions, for example, Beyond Blue, suggested:

*A key consideration in the introduction of the NFP regulator is the development of a clear transition process. This will ensure that regulatory requirements are not duplicated; NFPs are aware of their obligations under the new regulator; and information held by existing Government agencies, relevant to the scope of the national regulator, is transferred to this body.*

Given these concerns, breaking down the reform process into manageable goals within an overall reform timeframe, and prioritising identified issues that can be addressed immediately, would be a way of making progress that the NFP sector would be likely to support.

Many submissions only answered questions that were relevant to their organisation. This reflects the diversity of composition of the NFP sector and the diversity of interests relevant to different organisations.

The outcomes of consultation on each of the issues that were set out in the consultation paper will be analysed in detail in this report.



# Chapter 2

## Goals of NFP regulation

### Introduction

In the consultation paper on the *Scoping Study for a National NFP Regulator*, the Government sought the views of the sector in relation to what goals the regulation of the NFP sector should seek to achieve. Clear goals for the regulation of the NFP sector are essential to guide the direction for the regulatory reform process, in order to deliver the best outcomes for the public, the sector and governments.

The consultation paper set out a series of proposed goals for NFP regulation and sought the views of stakeholders in relation to whether these goals were appropriate and adequate and the relative importance of the goals outlined by the paper. The consultation paper stated that:

*NFP regulation should promote a strong and sustainable NFP sector through good governance, transparency and accountability to underpin strong philanthropic engagement in the community. Regulation which achieves these goals is essential to underpin public confidence in the sector and to assist the public and government in the effective and efficient allocation of resources to meet community needs.*

*Regulation of the NFP sector should:*

- *place minimal costs on NFPs in order to allow better direction of NFP resources to philanthropic objectives;*
- *remove current regulatory duplication;*
- *streamline requirements, including reporting, so as to provide consistency and minimise compliance costs;*
- *provide a 'one-stop shop' for NFP entities, to assist all NFP entities to more easily access information that helps them understand and comply with their regulatory obligations;*
- *be simple, transparent and flexible;*
- *provide NFP entities with certainty as to their rights and responsibilities; and*
- *be proportional to the size and complexity of NFP entities, and to the public monies and risks associated with NFP entities.*

*Simplicity and transparency will provide a solid foundation, and sufficient flexibility for the sector to grow sustainably over time and tailor its services to meet those evolving community needs. Regulation should be flexible enough to allow opportunities for the sector to develop through expansion or consolidation. Regulation should also provide for the capacity development of NFP entities.*

*Appropriate monitoring and compliance activities are essential to public confidence in the sector, particularly given the trend for increased government funding for service delivery. Regulation must ensure that donors and volunteers are confident that regulation protects the assets of charities and NFPs and monies donated by the public, and minimises the risks of malfeasance.*

*A NFP regulator should work with the sector to provide support and education in order to improve understanding and compliance with regulatory requirements. A national NFP regulator can provide an interface for government and sector interaction, permitting a better exchange of information and allowing the government to better respond to emerging issues and to maintain a modern and adaptive framework.*

## Summary of consultation

Generally submissions to the consultation were supportive of the goals of national regulation set out in the consultation paper and felt that they were appropriate and adequate. There was significant support for harmonisation and simplification, particularly in relation to reporting requirements. Proportionality of regulation was also strongly supported. Some submissions stated that the goals were equally important and should be seen as part of a whole package of NFP reform.

Many submissions largely supported the goals of the paper with some reservations. Only a small number of submissions were not supportive of the goals proposed in the consultation paper. Some of these submissions were concerned about the scope of regulation or expressed reservations in relation to the 'autonomy' or 'independence' of the sector as a result of improvements to regulation.

Ten submissions stated that they did not support the goals. Several of the submissions that did not support the goals of regulation were largely concerned with the impact of changes to regulation of certain types of entities, such as some religious organisations.

Some submissions suggested a broader role for the regulator, including acting as a facilitator for NFP organisations, by managing their interactions with governments, and acting as an advocate for the sector in these interactions. Some submissions also suggested the provision of higher levels of education than that envisaged in the consultation paper, including initiatives such as providing additional recognition, recruitment and/or training to directors and responsible individuals for NFPs.

Some submissions, such as the University of Melbourne's, supported the goals of the paper and provided views on the relative importance of these different goals.

This submission viewed the key distinguishing feature of NFPs as the pursuit of public or community benefit, rather than profit. As a result, the ultimate goal of regulating the sector is to provide a foundation for a strong and sustainable NFP sector to achieve these altruistic goals and deliver important benefits to the community.

From this ultimate goal a number of other goals were identified, including:

- the promotion of public trust and confidence in NFPs;
- ensuring the commitment of NFPs to purposes for the public benefit;

- ensuring appropriate transparency and accountability to donors, beneficiaries, other stakeholders, and the public;
- promoting compliance with legal obligations;
- ensuring efficient and effective allocation of resources;
- preventing abuse, self-dealing or other misuse of NFPs;
- improving the effectiveness of NFPs; and
- ensuring the sustainability of community organisations.

Other long term goals of regulation can include:

- promoting capacity building within the sector; and
- promoting a strategic, enterprising approach to management.

In considering the goals of NFP regulation, Melbourne University also noted that it is important to consider the general principles of good regulatory design as they apply to the NFP sector. Regulation should:

- place minimal costs on NFPs in order to allow better direction of NFP resources to philanthropic objectives;
- remove current regulatory duplication;
- streamline requirements, including reporting, so as to provide consistency and minimising compliance costs;
- provide a 'one-stop shop' for NFP entities that will assist NFP entities to access information that helps them understand and comply with their regulatory obligations;
- be simple, transparent, accessible and flexible;
- provide NFP entities with certainty as to their rights and responsibilities; and
- be proportional to the size and complexity of NFP entities, and to the public monies and risks associated with NFP entities.
- be integrated and consistent with other laws; and
- be enforceable.

Melbourne University also noted that the goals of NFP regulation need to take account of a range of distinctive aspects of the regulatory context of the NFP sector, including:

- the focus of organisations on achieving a community, altruistic or philanthropic purpose (the mission orientation of NFPs);
- the provision of what are commonly termed in economics 'public goods' or 'quasi public goods' which cannot be efficiently provided by the market;
- the diversity of the sector, including size and activity;

- the role of the sector in enabling an active civil society;
- the growth of the NFP sector including the growth due to government contracting for delivery of government services; and
- the contribution of the sector to community wellbeing.

## Issues

The goals set out in the consultation paper received strong support in the submissions, indicating that, broadly, these goals are appropriate and adequate to guide the NFP reform process.

One issue of controversy was the degree to which the regulator should act as a facilitator or advocate for the NFP sector. Some submissions argued for this approach while others saw the role of the regulator as primarily to administer the law.

The arguments for the regulator to act as an advocate or a facilitator for the sector include that this would take account of the altruistic goals and public benefits provided by the NFP sector and that 'sector development' should be a key focus of the regulator's activities.

The role of a regulator is to administer the law, thus regulating a sector. While this role can include providing education and support to a sector, this needs to be balanced such that it does not lead to a conflict of interest between the regulator's roles. While it is important that a new regulatory framework for the NFP sector should be designed to allow sector growth and development, the regulator will be responsible, primarily, for administering the law.

## Findings

The goals of NFP sector regulation as articulated in the consultation paper, and elaborated on in the discussion above, are appropriate and adequate and should guide the NFP reform process. These goals may also be taken into account in the development of the mission statement of the NFP regulator.

While a regulator should provide appropriate levels of education to assist the sector to understand and comply with their regulatory obligations, the role of a regulator should not extend to facilitator or advocate for the sector.

## Recommendations

1. The goals of NFP reform, as outlined in the consultation paper, should be used to guide the NFP reform process.

# Chapter 3

## Scope of national regulation and a national regulator

### Introduction

The NFP sector is characterised by its diversity, with entities ranging from micro-sized sporting and recreational clubs to large national and multinational charitable organisations, and consists of approximately 600,000 entities. The services provided by NFPs include the provision of welfare, education, sports, arts, culture and community services, and their goals are as diverse as the services they provide.

Of the 600,000 entities, it is estimated that around 400,000 access Commonwealth tax concessions, either through the ATO's registration process for some NFP entities (endorsement) or by self-assessment.

Australian governments recognise the valuable role played by the NFP sector and provide important support to NFP entities through tax concessions, reduced regulatory fees and exemptions from prudential regulation. Australian governments also offer specific grants and have developed loan funding programs for NFP entities. In the context of the significant level of public support provided to the sector, it is vital that the sector is well regulated, transparent and accountable.

Several recent reviews and inquiries into the NFP sector have consistently recommended that a national regulator should be established for the NFP sector, the AFTS Report, the PC Report and the 2010 Senate Inquiry.

NFP entities are constituted through a variety of legal forms, including corporations, incorporated associations, unincorporated associations, charitable trusts and entities created under special statute or letters patent.

There are also a number of regulators for different purposes, including the ATO, ASIC, ORIC, state Attorneys-General, and state Offices of Fair Trading.

The scope of regulation of a NFP regulator will need to consider both the treatment of different legal forms of NFP entities and the role of existing regulators.

### ATO regulation of Commonwealth tax concessions and private ancillary funds

The ATO currently acts as a default regulator of charities and NFPs at the Commonwealth level through its role of determining charitable status and administering charitable tax concessions.

In addition the ATO acts as the regulator for private ancillary funds. The Australian Government is also introducing reforms to regulate public ancillary funds at a Commonwealth level.

## ASIC regulation of companies limited by guarantee

Currently, there are approximately 11,000 NFP organisations that are constituted as companies limited by guarantee, representing less than 2 per cent of all NFP entities, and less than 7 per cent of all incorporated NFP entities in Australia. These entities are regulated by ASIC, and fall under the Corporations Act. The Corporations Act does not require a company limited by guarantee to conduct itself as a NFP entity; the preclusion from distributing profits or surplus assets to members is generally provided for as a clause in the company's constitution. The presence of this type of clause in a company's constitution is required for the company to omit 'Limited' from its name.<sup>5</sup> A company limited by guarantee is however prevented from paying out a dividend to its members.<sup>6</sup> Members' liability is limited to an amount that the members agree to contribute on winding up if there is a deficit.

A company limited by guarantee must register with ASIC and comply with the same governance requirements and disclosure obligations as for-profit corporations, including the statutory directors' duties and rules facilitating member participation.

From 30 June 2010, the financial reporting obligations for companies limited by guarantee have been either reduced or streamlined with the establishment of a three tier differential reporting framework. Under these requirements, small companies limited by guarantee are generally exempted from financial reporting and auditing requirements, while other companies limited by guarantee are provided with streamlined assurance requirements and simplified disclosures in the directors' report.

It should however be noted that DGRs are not exempt from these reporting requirements. This is because as a DGR they are considered to have a level of both government and public support that warrants an obligation to report on the use of that support.

ASIC are also responsible for the regulation of professional trustee companies. As a result, corporate trustees of charitable trusts are subject to Commonwealth regulation. Following legislation enacted in 2009, the provision of traditional services by trustee companies is now regulated as a financial service under the Corporations Act.

## ORIC and corporations incorporated under the Corporations (Aboriginal and Torres Strait Islander) Act 2006 (CATSI Act)

ORIC is responsible for the regulation and governance of Indigenous corporations registered under the CATSI Act. ORIC currently regulates approximately 2,600 Indigenous corporations, approximately 80 per cent of which are NFP organisations.

The activities of ORIC include advising organisations on how to incorporate, providing corporate governance training, mediating disputes, making sure corporations comply with the law and intervening when needed.

Registration under the CATSI Act is mostly voluntary. However, some corporations, such as registered native title bodies corporate determined by the Federal Court of Australia under the *Native Title Act 1993*, and royalty associations under the *Aboriginal Land Rights (Northern Territory) Act 1976*, are required to register under the CATSI Act.

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5 Sections 150 and 151 of the *Corporations Act 2001*.

6 Section 254SA of the *Corporations Act 2001*.

There are special governance arrangements for Indigenous corporations. All corporations are required to have a rule book (constitution) that sets out the corporation's aims, its name, a process for resolving disputes and any other matters the corporation wishes.

Like the Corporations Act, the CATSI Act provides a system of replaceable rules that gives guidance on critical matters related to internal governance.

Corporations are registered as small, medium or large. Each corporation will report according to their registered size and income. All corporations have to prepare a general report. The general report contains the basic details of directors, current members, the contact person/secretary and the document access address/registered office. It also contains some other information about taxation status. Keeping this information up to date and keeping proper financial records are the key compliance requirements for corporations.<sup>7</sup>

All small corporations with an income of less than \$100,000 only need to provide a general report. Small corporations with an income of \$100,000 or more, and all medium and large corporations, must provide a financial and directors' report in addition to the general report. The financial and directors' report is more comprehensive for large corporations and any other size corporation with an income of \$5 million or more.

### State and territory regulation of incorporated associations

The states and territories are responsible for the regulation of incorporated associations. As of the 2008-09 financial year, there were 136,000 NFP incorporated associations registered in Australia.<sup>8</sup> While largely similar, there are some differences in the legislative requirements for incorporated associations across jurisdictions, such as regulatory requirements and eligibility criteria for incorporation. This makes it difficult for incorporated associations to operate across jurisdictions and increases their compliance burden. The different requirements may encourage forum shopping.

While legislative requirements vary across jurisdictions, most focus on the association's purpose, and have the requirement that the association must not be formed for the purpose of obtaining a profit.<sup>9</sup> Uniquely, in the Northern Territory provision is made for the incorporation of a trading association, formed for the purpose of trading or disbursing profits to its members.<sup>10</sup> This expands the concept of an incorporated association to include circumstances which are expressly excluded in other jurisdictions.

If incorporated associations wish to 'carry on business' outside their home jurisdiction, they are required to register with ASIC as an Australian registered body, and are allocated an Australian Registered Body Number (ARBN).<sup>11</sup> Australian registered bodies are subject to provisions of the Corporations Act when conducting business interstate. As a result, incorporated associations operating outside their jurisdiction are subject to dual reporting obligations in some circumstances (for example, upon changing the name of the entity or replacement of directors) to both ASIC and the relevant state or territory authorities. This duplication, while minimal, is inefficient and increases the compliance costs to entities. A national NFP regulator, tasked with the authority to monitor and supervise incorporated associations, would remove the inconsistency and duplication.

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7 Office of the Registrar of Indigenous Corporations, *Get in on the Act: A Guide to the Corporations (Aboriginal and Torres Strait Islander) Act 2006*, February 2010.

8 Productivity Commission, *Report on the Contribution of the Not-for-profit Sector*, 2010, p 58.

9 Section 18(6) of the *Associations Incorporation Act 1985* (SA), Section 4(4) of the *Associations Incorporation Act 1987* (WA).

10 Section 4 of the *Associations Act 2010* (NT).

11 <http://www.asic.gov.au/asic/asic.nsf/byheadline/Registrable+Australian+Bodies?opendocument>

All incorporated associations are required to maintain accurate accounting records, and many states require annual reports to be lodged under their respective governing statutes. All states and territories, except South Australia and Western Australia, require every incorporated association to lodge annual returns articulating the financial position of the entity. Only prescribed associations are required to lodge annual returns in South Australia, and in Western Australia the Commissioner has the discretion to order an association to submit financial statements.<sup>12</sup> Queensland, New South Wales, and the Northern Territory have based the extent of their reporting requirements on a proportional approach<sup>13</sup>, with larger associations being subject to stricter requirements, including annual audits. In Victoria, Tasmania, and the Australian Capital Territory prescribed associations are required to present audited accounts to the Registrar.<sup>14</sup> However, the reporting thresholds vary widely across each jurisdiction.

The requirements imposed by state and territory Associations Incorporation Acts have historically been less onerous than the conditions of the Corporations Act making this structure a popular choice for NFP entities.<sup>15</sup> However, recent changes to requirements for companies limited by guarantee have reduced the regulatory burden, and in many cases, the requirements are less onerous than those applying to incorporated associations, for example, reporting requirements.

It is unclear why more NFPs have not adopted the company limited by guarantee structure under the Corporations Act. In order to address issues arising from large entities remaining under the associations incorporation acts, all jurisdictions, except Queensland, have enacted provisions which allow for the transfer of incorporated entities to a company limited by guarantee under the Corporations Act.<sup>16</sup> All jurisdictions, except Tasmania, allow for such transfer to be forced by the Registrar.

### State and territory regulation of charitable trusts

A charitable trust is established to manage and distribute funds to individuals and organisations for a charitable purpose and for the benefit of an appreciable section of the public. They are established by the execution of a trust deed, either via inter vivos or testamentary transfer. Charitable trusts developed under the law of equity, and were traditionally administered by the courts of equity and the Crown. Trusts were considered charitable if their purpose fell within the preamble to the *Statute of Charitable Uses* enacted by the English Parliament in 1601 (commonly referred to as the Statute of Elizabeth). In order to be considered charitable, a trust's purpose had to fall within one of the four heads of charity:

- the relief of poverty;
- the advancement of education;

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12 Section 36 of the *Associations Incorporation Act 1985* (SA). Section 39(3) of the *Associations Incorporation Act 1987* (WA).

13 Section 58 of the *Associations Incorporation Act 1981* (Qld), NSW ss 42 – 49, ss 47 – 48 *Associations Act* (NT).

14 Section 30D of the *Associations Incorporation Act 1981* (Vic). Section 24 of the *Associations Incorporation Act 1964* (Tas). Section 79 of the *Associations Incorporation Act 1991* (ACT).

15 <http://www.asic.gov.au/asic/asic.nsf/byheadline/Registering+not-for-profit+or+charitable+organisations>

16 Part 7 of the *Associations Incorporation Act 2009* (NSW). Part VIIA of the *Associations Incorporation Act 1981* (Vic). Sections 25B – 25E of the *Associations Incorporation Act 1964* (Tas). Part 5 of the *Associations Incorporation Act 1985* (SA). Part IIIA of the *Associations Incorporation Act 1987* (WA). Part 7 of the *Associations Act 2010* (NT). Part 6 of the *Associations Incorporation Act 1991* (ACT).

- the advancement of religion; and
- other purposes beneficial to the community.

Charitable trusts play an important role in the NFP sector. The Trustee Corporations Association of Australia (TCA), comprises eight private trustee corporations and the state and territory Public Trustees, and manages 2,000 charitable trusts and foundations with assets of \$3.9 billion, which in 2008-2009, distributed \$180 million. However, there may be many more charitable trusts in existence that are not administered by TCA members.

Australian states and territories have enacted legislation governing the broad duties and responsibilities of trustees.

While the terms of a trust are generally fixed once declared by the settlor, unless provision is made in governing documents, the court is able to vary the objects of a trust. Intervention by an Attorney-General is required to dissolve or administer a charitable trust. In most Australian jurisdictions Attorneys-General have limited or no supervisory or investigatory powers with regards to charitable trusts.

Without a means of gathering information, the Attorneys-General are restricted in their capacity to monitor and remedy any breaches of trust. There are also discrepancies across states and territories relating to the removal of trustees, with some jurisdictions providing for this in statute while others remain silent. The varying powers of Attorneys-General and courts across states and territories mean that regulation is inconsistent and could result in forum shopping.

The Commonwealth has assumed responsibility for regulating professional trustee companies and regulates some trust funds through its corporate trustee laws. For example, private ancillary funds are regulated at a Commonwealth level, as discussed above.

### Regulation of other legal forms

Approximately 440,000 organisations are small unincorporated NFPs. These entities largely fall outside the current regulatory system, although many access taxation concessions.

Some entities, such as churches and religious organisations, are incorporated by special statutes or Royal Charter, or are branches of international organisations, and in some cases fall outside of the current regulatory system.

### Other NFP regulators and regulation

There are several regulators of the NFP sector which regulate specific sections of the NFP sector, rather than regulating on the basis of legal form.

For example, regulation of housing services by NFP entities is currently being developed. In a joint communiqué of 16 December 2010, the Housing Ministers Conference agreed to implement a nationally consistent regulatory system for NFP housing providers, with the goal of providing more opportunities for growth within the NFP housing market.

Under this agreement, regulation of the housing sector would be based on collaboration of governments to implement a nationally consistent regulatory system (a national code) that will aim to promote the growth of the NFP housing sector.

Another example is in the area of fundraising, where regulators exist in each state to ensure fundraising activities are carried out in accordance with the legislation.

There are also frameworks in place where bodies are responsible for regulating some aspects of the activities of NFPs, such as quality assurance, including childcare and health services. There would likely be some overlap, particularly in the areas of governance and financial reporting, between these regulators and a new NFP regulator. For example, child care quality assurance is undertaken by the National Child Care Accreditation Council, which is a NFP organisation funded by and accountable to the Australian Government.

### Summary of consultation

The consultation paper discussed the scope of regulation and the extent to which it would extend to all legal types of NFPs. It raised the view that effective regulation of NFPs needs to apply broadly across the sector, despite the diverse group of entities, and their various legal forms, and that it should improve the confidence that government agencies can have in the NFP sector, particularly where agencies provide grants and contracts to NFPs.

Two regulatory options were posed in the consultation paper:

- regulation of entities that receive public donations, are in receipt of tax concessions, or receive government grants and/or government funding; and
- regulation that is proportional to the level of benefits and support received as well as taking into account the varying size and complexity of the organisations in the NFP sector.

The aim of consultation was to gauge what stakeholders viewed as appropriate scope for a national regulator and regulatory reform.

Submissions varied in their views on the scope of any new national regulator, reform or regulation of the NFP sector. A slight majority of submissions favoured regulating all entities that receive public donations, government funding or tax concessions regardless of the legal structure. Other views expressed included that regulation should:

- be based on risk, complexity, size, or annual turnover of an entity;
- not apply to NFP entities that have incorporated, are independently audited and already produce financial statements which comply with Australian accounting standards;
- apply according to the level of support and benefits received by the entity, so priority should be to regulate entities with government support;
- exclude NFPs if their income was below a certain threshold;
- focus, initially, on unincorporated organisations;
- be determined by reference to a common definition of NFP;
- allow some scope for different treatment of NFPs, but monitoring and reporting requirements should be streamlined for all; and
- apply to all entities regardless of legal form as excluding any entities would create inconsistencies.

Some submissions stated that a single regulator regulating different types of bodies may increase regulatory burden of some NFPs. Others called for the creation of a new NFP legal structure. Some stated that constitutional issues may mean that different legal forms will need to be treated differently. Others noted that entities established by statute may require legislative change if included in a national regulatory framework.

It should be noted that many submissions did not address this question.

Some submissions stated that entities already subject to regulation, for example by ASIC, should not be regulated by the NFP national regulator. For instance, the Royal College of Pathologists Australasia stated that in their view:

*it is the large and complex organisations that are most likely to be adequately regulated presently and those organisations should not be subject to further regulation.*

A few submissions noted that smaller entities may not have the in-house expertise or the capacity to meet compliance requirements.

Many universities and independent schools, religious charities and various peak bodies opposed a new regulator and stated that their current regulation provided sufficient accountability.

There were varying views on the inclusion of ORIC and NFP housing within a national regulator. Nine submissions supported incorporating the functions of ORIC into a NFP regulator. Qualified support for incorporating these functions was expressed in 14 submissions. Seven submissions did not support the incorporation of the functions of these other regulators into the NFP regulator.

Therefore, most submissions were generally supportive, but raised concerns as to the level of integration, and to what degree it was appropriate and possible for a NFP regulator to cover all the issues relating to Indigenous corporations and the housing sector.

Some concerns were raised, for example, that Indigenous entities were not all NFP entities and that change should not hamper development, or lose the current support role that is undertaken by ORIC, in relation to developing good governance. The University of Melbourne submitted:

*An important issue is not to lose the existing specialist experience, community engagement and expertise in the current regulatory agency, such as ORIC.*

The North Queensland Land Council submitted:

*The CATSI Act and ORIC were specifically set up to cater to the specific needs of the indigenous community ... [they] believe that a lot of good will be lost if the indigenous specific ORIC was now made simply a branch of some larger regulator. It is likely to be seen as downgrading the importance of the indigenous community and thus counterproductive.*

Most submissions did not address the question of whether the supervision of charitable trusts should be moved from the State Attorneys-General to a national regulator. Of the submissions that did, a large majority of them (around 90 per cent, including the Trustees Corporations of Australia) supported the role of a national regulator in supervising charitable trusts as it ensures consistent regulation for all NFP entities, with some submissions

suggesting that their support is subject to the proviso that the regulator is adequately resourced to perform this function.

Some submissions thought state operations may be best placed to support the regulator in specific state by state initiatives, or activities could be monitored more effectively at the state level.

Some submissions stated that the private ancillary funds model would be inappropriate for the supervision of charitable trusts.

In summary, a slight majority of submissions favoured regulating all NFP entities that receive public donations, government funding or tax concessions regardless of the legal structure over those that said regulation should be commensurate to the public benefits or size and complexity of the activities involved.

## Issues

The NFP sector is diverse and current regulatory frameworks are complex, with regulation for different and overlapping purposes, at the Commonwealth, state and territory levels.

Regulation at the Commonwealth level includes regulation by the ATO for the purposes of tax concessions and private ancillary funds, ASIC regulation of companies limited by guarantee and ORIC regulation of Indigenous corporations.

Regulation at the state and territory levels includes regulation of incorporated associations and charitable trusts, although there is also some Commonwealth regulation of these entities, as discussed above. In addition, states and territories regulate fundraising activities of NFPs.

The regulation of the NFP sector also varies in focus, with some regulation based on entity type, for example ASIC regulation, some focused on activities, such as fundraising, and other regulation aimed at specific parts of the NFP sector, for example regulation of NFP housing.

There are advantages in the maintenance of multiple regulators of the NFP sector. It allows for specialist skills to be developed by regulators and for specialist arrangements, such as the governance role of ORIC. In addition it allows for regulatory regimes to be adapted to the regulatory needs of specific entity types and for local approaches.

However, there are significant disadvantages in having multiple regulators of the NFP sector. Specifically, it results in complex, overlapping and duplicative regulation, and a lack of transparency, making it difficult for the public to understand the NFP sector. Ultimately it leads to an unnecessarily high regulatory burden for NFPs.

The best results—in terms of reduction of red-tape and regulatory duplication—could be achieved for the sector by ensuring that regulation applies broadly across the sector regardless of legal form, activity or section of the NFP sector.

A single NFP national regulator would centralise regulation in one location, and there would be scope for a NFP regulator to act as a central point for organisational governance, accreditation and reporting requirements, using a 'report-once, use-often' model. This model would allow for a NFP regulator to coordinate the collection of reports for other regulators.

This would address a key concern raised by stakeholders about duplication of regulation, or an increased regulatory burden. This concern has particular application where there is currently regulation in place.

Inclusion of all entities within the scope of reporting would lead to a greater level of public understanding of the entire NFP sector. It may also result in higher levels of confidence in NFP entities and may result in greater levels of monetary and voluntary contributions. However, as noted by submissions to this paper, many small and micro-sized NFP entities may have limited administrative capacity.

If some NFPs were excluded from the new regulatory framework, such as Indigenous corporations and NFP housing providers, they would not have a 'one-stop shop' for their governance, regulatory and reporting frameworks.

Where regulatory overlap can be removed to a single regulator, such as ATO and ASIC regulation, regulation could be undertaken by the NFP regulator. This would remove regulatory overlap and help provide a 'one-stop shop' for NFPs. The regulation of Indigenous corporations by ORIC could also be moved to the national NFP regulator, however specific complexities in relation to ORIC may mean that further discussion and further review may be necessary to determine the best way to incorporate these entities without losing the benefits of the specialist skills and expertise in this area, and the relationships developed with the Indigenous community. Moving ORIC into the regulator may also have significant advantages, such as the ability to extend the experience in relation to ORIC to all Indigenous NFPs (including those not currently regulated by ORIC) and allow all NFPs to be regulated in a similar manner.

Another area where there is potential for the removal of regulatory overlap is where both the Commonwealth and states and territories are involved in regulation of the NFP sector, such as the regulation of incorporated associations and charitable trusts, there are several options for the regulatory framework to be simplified. These may include harmonisation of legislation or the introduction of national legislation, these options could be pursued by Australian, state and territory governments through the COAG agenda.

An alternative approach where there is overlapping Commonwealth, state and territory legislation, would be the adoption of a single legal form for NFPs, this could be achieved through the company limited by guarantee entity type. It is unclear why more NFPs have not chosen this legal structure, particularly given the recent changes to the requirements of this entity type. This legal form could be reviewed to determine the appropriateness of this structure for NFPs.

## Findings

A single regulator should be established for the purposes of governance, accountability and transparency of NFPs. This will assist the sector to have a clear, coherent and consistent set of regulatory obligations.

Regulatory duplication should be removed by exempting entities from overlapping regulation, such as removing reporting to ASIC for entities regulated by the NFP regulator. This will require cooperation between the Commonwealth and the states and territories.

Existing regulators that regulate for the purposes of governance, accountability and transparency should be rolled into the NFP regulator. Regulators that regulate service quality standards should remain separate, however, overlap of governance, accountability and

transparency obligations should be removed to provide a consistent national regulatory framework.

Where there is regulation targeted at ensuring quality for services provided by NFPs, the regulatory framework could be streamlined to ensure that governance, accountability and transparency were regulated by a single national NFP regulator. Regulation for service delivery could remain in place with any duplication in the areas of governance, accountability and transparency moved to a national NFP regulator.

A principles-based regulatory framework should be established, to apply broadly across the NFP sector, regardless of entity type or industry, although regulation may be proportional and tailored to address the specific needs and size of NFPs.

### **Recommendations**

2. A single regulator should be established for the purposes of governance, accountability and transparency of NFPs.
3. The NFP regulator should, as far as possible, be responsible for regulating all NFPs.
4. Entities that are currently regulated by ASIC should be incorporated within the regulatory framework as soon as new reporting and governance frameworks are implemented. ASIC should still retain responsibility for incorporation.
5. The regulator should administer a principles-based regulatory framework which would apply broadly across the NFP sector, although regulation should be proportional and tailored to address the specific needs and size of NFPs.
6. The options for reform in areas which require the cooperation of the Commonwealth, states and territories should be progressed through the COAG agenda, including the areas of incorporated associations and charitable trusts.
7. Further reviews should be undertaken in areas where there are opportunities for further reform. This may include reviews of existing regulators and the legal form of NFPs, including the company limited by guarantee structure.

# Chapter 4

## Registration

### Introduction

Recognising the valuable role played by the NFP sector, Australian governments provide significant support to NFP entities through access to tax concessions, reduced regulatory fees and exemptions from prudential regulation. Australian governments also offer specific grants and have developed loan funding programs for NFP entities.

To access support provided by Australian governments, an entity has to be recognised as a NFP or a sub-category of NFP entity such as a charity or a PBI. Currently, government agencies administering support autonomously determine charitable status as part of the process of distributing support. For example, NFP entities—including charities and PBIs—have to submit endorsement forms to the ATO to be eligible for tax concessions such as income tax exemptions, fringe benefits tax and GST concessions. Application forms require entities to provide information on operational and governance framework, and financial position.

Similar information is often provided to government agencies managing NFP specific contracts for service delivery and grants earmarked for NFP entities including, state revenue authorities that provide access to state specific tax concessions, APRA if a religious charitable development fund is applying to be exempt from the requirement to be authorised under the *Banking Act 1959*, and ASIC to be eligible for reduced annual review fees.

### Summary of consultation

The Government's consultation paper sought the sector's views on simplifying and streamlining mechanisms for accessing tax concessions. Several respondents were of the view that having a process whereby a NFP entity would be endorsed and registered for the purposes of interacting with government could reduce administrative expenses. Further, respondents who are actively involved in the delivery of services on the Australian Government's behalf commented that 'red-tape' faced by NFP entities accessing grants and government contracts imposes significant compliance and administrative costs.

For example, the Chamber of Commerce and Industry of Western Australia submitted:

*At present NFPs must register with each potential government funding body as a suitable grant or contract recipient. This process may involve lodgement of documentation and information such as the constitution, registration of business name, financial statements to assess viability, organisation statistics and data... What is sought is a one point process where a NFP is recognised as an organisation fit to receive grants or to undertake government contracts, which would then be recognised by any government body.*

The majority of respondents were of the view that simplifying the administration of tax concessions would reduce compliance costs faced by NFP entities. It is likely that simplifying

administration processes more broadly would generate compliance costs savings through reduced duplication.

For example, the Australian Catholic Bishops Conference submitted:

*Any process that simplifies and streamlines the mechanisms for the assessment, granting and monitoring of concessional treatment and thereby reduces the regulatory burden and associated compliance costs for NFPs will make organisations more effective and efficient and increase the funding and support they can provide to the community.*

## Issues

In recognition of the role played by the NFP sector, Australian governments provide NFP entities with access to a range of support. To access the support they are entitled to, NFP entities are required to be registered as a NFP entity or a sub-category of NFP entity, such as a charity or a PBI, on numerous occasions by the various government agencies administering support.

This duplication of effort can drain resources, increase administrative expenses, and detract from the benefits of these concessions. Increased administrative costs are most significant when a NFP entity operates across numerous jurisdictions and therefore has to interact with Commonwealth, state and territory government agencies to access available support.

Implementing a centralised approach to registering entities as NFPs or charities would remove the need for NFP entities to be endorsed and registered on numerous occasions. Broadly consistent with the current situation, NFP entities would apply to be endorsed and registered as a NFP entity or charity on a voluntary basis, but registration would be needed to access support provided by Australian governments. Ultimately, this would simplify the sector's regulatory framework and reduce administrative expenses.

A move toward a centralised system would also eliminate duplication of government administration and therefore administrative expenses for NFPs.

The greatest benefits in terms of reduction in compliance and administrative costs would be achieved if registration applied throughout Australia, and became accepted by every agency of the Commonwealth and of the states and territories. Current legislation does not cater for the Australian Government to mandate that state and territory agencies accept the decisions made by Commonwealth bodies such as registrations of entities as NFPs.

A move toward a centralised registration framework would need to ensure access to information by government agencies to administer their laws and fulfil their responsibilities. Currently, government agencies have highly specialised responsibilities and are required to administer different aspects of the law. Information required to fulfil responsibilities has been gathered in part when endorsing and registering entities as NFPs. Therefore, to ensure agencies continue to undertake their role and responsibility effectively they must have access to the same level of information, which could be achieved through information sharing arrangements.

Ensuring that agencies continue to administer allocated laws and fulfil their responsibilities would cater for specialisation and consistent application of the law across all sectors of the Australian economy, including the NFP sector. Furthermore, separating endorsement and registration functions from administration and management of government support could help address concerns in relation to conflicts of interest.

The NFP sector is particularly concerned over potential conflict of interest in ATO responsibilities. Currently, the ATO administers Australia's tax law and functions as the regulator for the NFP sector at the Commonwealth level. These roles could be perceived as potentially having conflicting objectives which may generate inefficient social and economic outcomes. If a government body were responsible for registering NFP entities, the ATO would be able to focus on its core role of administering the tax law. To provide tax concessions, the ATO would check and accept an entities registration, and verify whether the entity fulfils all other conditions set out in the tax law, such as the 'in Australia' special conditions or the general anti-avoidance rules.

The ATO is the principal revenue collection agency and as such there are strong arguments to support continuing the ATO's role in administering the NFP tax concessions. If the functions of regulating NFPs and administering the tax concessions were both to be undertaken by the NFP regulator then concerns over a perceived conflict of interest would remain. Furthermore the administration of the tax concessions needs to be consistent and in accordance with the rest of the tax laws.

This split of functions is consistent with other jurisdictions. For example, in the United Kingdom the Charities Commission is responsible for registering charities, while Her Majesty's Revenue and Customs is responsible for administering tax concessions.

NFP entities are entitled to independent review of administrative decisions. There are well-established review and appeal procedures, which among other things extend procedural fairness to parties affected by administrative decisions. For example, most agencies decisions are subject to internal review, independent review by the Administrative Appeals Tribunal, and a right to appeal to the federal courts. These mechanisms have worked well and offer affected parties an effective means for review of decisions.

## Findings

A government body should be given the responsibility to endorse and register NFP entities. Registration should be recognised by agencies at the Commonwealth, state and territory levels. This would lead to the greatest reductions in compliance and administrative burden from both the sector's and governments' perspectives.

An NFP regulator would be best placed to determine the status of NFP entities. The NFP regulator would oversee the performance of the sector and collect relevant information on the financial and operational performance of NFP entities. This information should be used as a basis to determine an entity's NFP status, register entities and monitor entities ongoing eligibility to operate under a specific NFP status. NFP entities should be able to apply to have their status determined and be registered on a voluntary basis, noting that they would need to be registered to access government support.

The regulator would also establish information sharing arrangements with government agencies to ensure they have the information required to administer allocated laws and responsibilities. Implementation of a centralised registration framework would require negotiation with state and territory governments. In the interim, the NFP regulator's determinations should be accepted by all agencies at the Commonwealth level.

Administrative decisions on NFP status made by the NFP regulator should be subject to established review and appeal procedures currently used by Australian Government bodies.

## Recommendations

8. The NFP regulator should determine the NFP status of entities, including charities and PBIs. Initially, the regulator's determination should be accepted by every Commonwealth agency. The regulator should initially focus on determining the status of charities including PBIs, with this focus gradually extending to include all other NFP entities.
9. Through the COAG process, the Australian Government should work with state and territory authorities with the aim of ensuring that the regulator's registration applies throughout Australia, and be accepted by every government agency.
10. Entities should apply to have their status determined by the regulator on a voluntary basis. However, to access support provided by the Australian Government, and any state and territory governments that agree following conclusion of the COAG process, a NFP entity would need to be registered and regulated by the NFP regulator.
11. Administrative decisions taken by the NFP regulator should be subject to internal review; independent review by the Administrative Appeals Tribunal; and a right to appeal to the federal courts.

# Chapter 5

## Definition of charity

### Introduction

#### The common law

Australia does not have a statutory definition of charity. The common law definition of charity is based on the Preamble to the *Statute of Charitable Uses* (enacted by the English Parliament in 1601 and known as the *Statute of Elizabeth*); *Commissioners for Special Purposes of Income Tax v Pemsel* [1891] All ER Rep 28 (Pemsel's case) which classified the categories of charitable under four heads, and subsequent court cases.

The four categories or 'heads' of charitable purposes identified in Pemsel's case are:

- the relief of poverty;
- the advancement of education;
- the advancement of religion; and
- other purposes beneficial to the community not falling under any of the preceding heads.

A public benefit requirement is central to the common concept of what is charitable, and under common law, there is a presumption of public benefit for charities under the first three heads of charity. For the fourth head of charity, the onus is on the purported charity to prove that it is acting in the public benefit.

#### Previous reviews and inquiries

In 2003, the then Government attempted to provide a statutory definition of charity at the Commonwealth level in the Charities Bill 2003 based on the recommendations of the Charities Definition Inquiry.

The Charities Bill 2003 codified the key principles of the common law definition of charity and charitable purpose, and included a list of charitable purposes and requirements that an entity must be not-for-profit; the dominant purpose or purposes must be charitable; and a charity must operate for the public benefit. The definition also expressed disqualifying purposes and had the effect of overturning the presumption of public benefit for the first three heads of charity.

While the bill did not proceed, the definition of charity was extended by the *Extension of Charitable Purpose Act 2004* which conferred charitable status on the provision of child care, self-help groups and closed or contemplative religious orders. It was later extended to include the limited provision of rental dwellings under the National Rental Affordability Scheme.

More recently, the AFTS Report and the PC Report recommended adopting a statutory definition of charity. 2010 Senate Inquiry also recommended a statutory definition of charity and a test of public benefit.

The PC Report recommended a definition in accordance with the recommendations of the Charities Definition Inquiry, on the basis it would:

- ensure an appropriate Australian definition for our modern, social and economic environment;
- create clearer and more consistent principles; and
- reduce confusion and costly legal disputes.

Since the attempt in 2003 to codify a definition of charity, there have been developments both in Australia and overseas. In Australia recent judicial decisions have created uncertainty on the meaning of charity. In the *Commissioner of Taxation v Aid/Watch Incorporated* [2010] HCA 42, the High Court extended the definition of 'charity' to include further advocacy-type organisations. This decision has created uncertainty on the extent to which a charity can engage in political advocacy and has created uncertainty for the charitable sector, the public and government.

Overseas, the United Kingdom (UK) has enacted a statutory definition of charity in their Charities Act 2006, and expanded the list of charitable purposes beyond the four heads to include purposes such as environmental protection, human rights, animal welfare, conflict resolution and amateur sport. It also overturned the presumption of public benefit, requiring all charities to explicitly demonstrate a public benefit. The UK Charities Commission, established by the Charities Act 2006, is tasked with providing guidance as to the operation of the public benefit requirement.

Other jurisdictions that have codified a definition of charity since 2003 include Scotland, Ireland, Northern Ireland and New Zealand. The definitions are anchored on the same body of common law as Australia, but there are differences in the definitions, including the lists of charitable purposes. While the process of developing a statutory definition of charity was often challenging, overall, these other jurisdictions have had positive outcomes in enacting a statutory definition.

The statutory definitions in these jurisdictions have generally been enacted at the same time as a new regulatory framework for charities has been introduced including the establishment of a regulatory body for charities. The experiences by other common law jurisdictions in implementing a definition will provide valuable guidance in developing a codified definition, and will contribute to the development of a best practice model, providing clarity to the public, the charitable sector and the government.

## Summary of consultation

On the whole, consultation indicated that stakeholders are generally supportive of enacting a definition of charity, as it would provide greater certainty for the charitable sector and the public, and it is more appropriate that Parliament consider its meaning as opposed to the courts.

There has been some state and territory government support for a statutory definition of charity as it will provide a platform for harmonisation across the Commonwealth and state and territory jurisdictions.

During consultation there was concern with the proposal of a statutory definition of charity. The concerns were generally confined to specific sectors, and overall, submissions were varied in their view of the introduction of a definition of charity, with most not voicing an opinion, one way or the other.

Those that supported the proposal wanted the definition to be modernised, while others feared that a statutory definition would result in politicisation and greater uncertainty. For example, the North Queensland Land Council stated that:

*The difficulty with introducing statutory definitions is that there will inevitably be a period over which the interpretation of those definitions is challenged and has to be interpreted by the Courts. Any major change in definitions is likely to lead to a period where the law is unsettled for a period... On the other hand, there is a need to simplify and perhaps move away from the more archaic concepts of what constitutes a charity.*

Overall, religious groups opposed the proposal of a statutory definition, mainly citing that the presumption of public benefit would be overturned. For example, the Anglican Archdiocese of Sydney stated in its submission:

*Experience of other equivalent legal regimes to ours in Australia suggests there is nothing to be gained by replacing reliance on the common law definition of charity. If there is a need to clarify the status of an expanded range of purposes as charitable, then this can be done by way of legislation as an extension to the common law rather than in replacement of it.*

*Likewise, we consider that recent calls to remove the public benefit presumption which currently applies to religious and certain other charitable purposes would be a retrograde step, however well intended. The public benefit presumption has worked well as a mechanism for avoiding undue litigation about the question of public benefit. It remains open to the Courts to find that the presumption has been displaced and that income tax exempt status should therefore not be granted.*

There has always been a high degree of opposition to the restriction placed on advocacy. The sector has already achieved Governmental agreement to the principle of not restricting advocacy in the National Compact. The Aid/Watch decision was supported in the consultation.

## Issues

Although there are a number of sector specific concerns with enacting a statutory definition, overseas experience has indicated that the benefits clearly outweigh the costs and that enacting a definition has not resulted in any significant difficulties for most charities. This is to be expected as a statutory definition seeks to codify the key principles of the common law definition of charity and not replace the common law.

Some of the main benefits of having a statutory definition are considered further below.

### ***A platform for harmonisation***

A major benefit of a statutory definition of charity is that it would provide a platform to harmonise the definition of charity between the Commonwealth and state and territory jurisdictions (subject to consultation with the states and territories).

As of 2007, it was determined that there were 178 pieces of Commonwealth, state or territory legislation that involved 19 separate agencies regularly determining the charitable purpose or status of an organisation. The terms 'charity' and 'charitable purposes' are found in state and territory taxation laws, such as payroll tax, as well as other legislation, including trustee law, fundraising, collections law, and incorporation laws. The meaning of charity is inconsistent across jurisdictions, with some states having sought to expand the existing definition of charity. For instance, there is different treatment between states and territories on the acceptance of sporting bodies as charitable. Such inconsistency creates confusion in the sector. Definitions can also differ between pieces of legislation within the one jurisdiction.

Furthermore, the current processes for determining and recognising charitable status can vary significantly between Commonwealth and state and territory government agencies. As such, a charitable organisation currently needs to go through various agencies, providing the same information to attain charitable status for a range of purposes, imposing a large administrative burden on both charities and regulators. Harmonisation of definitions would provide greater certainty for those organisations operating across jurisdictions within Australia.

There would be significant benefits from a harmonised definition of charity for all levels of government, making it achievable in the long term that an organisation can be assessed as being charitable for all purposes by a single agency, greatly reducing the administrative burden on charities and will provide consistency of treatment for a range of purposes.

### ***Increases certainty and accessibility***

Since the attempt in 2003 to define charity, the uncertainty surrounding the meaning of charity and charitable purposes has increased. As noted above, other common law jurisdictions have enacted definitions, and have benefited from increased clarity.

A statutory definition would provide greater certainty in the determination of whether or not an entity or activity is charitable, for the NFP sector, the regulators, and the general public while retaining the flexibility of the common law.<sup>17</sup> Recent judicial decisions have added to uncertainty around the meaning of 'charity' and 'charitable purposes'.

Commonwealth, state and territory governments provide a range of generous tax concessions to charities. A statutory definition will provide a clear framework for assessing access to the tax concessions available to Australian charities. It would ensure that tax concessions are properly targeted and thus boost public confidence in the charitable sector.

Further, a statutory definition would make the key principles of common law more accessible to the charitable sector which may reduce their administrative costs (in particular, those of small charities).

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<sup>17</sup> The flexibility is provided by the inclusion of an 'other' category in the definition of a charitable purpose which provides the courts with the scope for finding 'new' purposes to be charitable in accordance with ongoing changes in society.

### ***Parliament can consider what is charitable***

A statutory definition of charity has the advantage that it can be altered by Parliament over time to ensure it remains appropriate and reflects modern society and community needs.

Under the current approach, where charitable law is generally determined by the courts, changing the law is time consuming and costly. Many charities do not have the resources to have their disputes heard. Furthermore, a court decision can be based on certain facts and circumstances so its scope can be uncertain and likely to result in further cases.

A statutory definition allows Parliament to bring the meaning of charity in line with contemporary community expectations in Australia without requiring costly and time consuming litigation to determine what is charitable. Parliament can consider wider issues related to charities, it can conduct enquires and reviews and it can ensure that the definition of charity remains appropriate in accordance with societal needs and expectations.

### ***Alternative option***

An alternative to a statutory definition which includes in legislation, the key principles of the common law, would be to comprehensively codify both the definition of charity and charitable purpose. That is, it would gather together all the relevant case and statutory law on charities and restate it as a complete and exclusive statement of the law.

A comprehensive codification would be complex to implement as many areas of charity law are currently unclear. It would be more difficult for stakeholders to reach agreement on all the principles of the definition and so would be a time consuming process. It would also result in a loss of the flexibility of the common law. It would be more difficult to provide a platform for harmonisation between the Commonwealth, states and territories because of the need to reach agreement on the terms of a definition.

## **Findings**

The outcome of the consultation process indicated that there is general support for a statutory definition of charity.

This is consistent with the recommendation of a number of reviews and inquiries that the common law meaning of charity be replaced with a statutory definition. These reviews were informed by public consultation.

The final content of the statutory definition of charity should be the subject of further consultation.

## Recommendations

12. The definition should be based on the 2001 Charities Definition Inquiry, noting the recommendations of the recent 2010 Senate Inquiry, and taking into account the findings of recent judicial decisions, such as *Aid/Watch Incorporated v Commissioner of Taxation*.
13. The definition of charity should be harmonised across Australian jurisdictions.
14. The Government should undertake further consultation on the definition of charity.

# Chapter 6

## Education and compliance

### Introduction

Currently education about governance and compliance obligations is provided to NFPs by government agencies that deal frequently with the NFP sector as well as peak body organisations.

- For example, a significant educational role is undertaken by ORIC with respect to indigenous organisations set up under the CATSI Act.
- The ATO also provides educational information in relation to taxation and compliance obligations at the Commonwealth level through its website, news service and its dedicated information phone service. The ATO also maintains its engagement with the sector through industry forums such as the Charities Consultative Committee.
- Some state departments with responsibilities for areas such as health, arts and sport also provide educational information to NFPs. In particular, those agencies which provide direct grants and have service delivery contracts with NFPs take on a role in educating the sector in relation to governance and compliance obligations.

Education about governance is also provided by non-government bodies and peak body associations such as Philanthropy Australia and the Australian Institute of Company Directors.

In New Zealand, the Charities Commission provides online resources, guided by feedback from the charities it regulates. Its 'income' section for example, provides information to charities to enable them to locate, apply for, attract or generate income for their organisation. The 'financial management' section provides information on how charities can manage money and remain accountable to stakeholders. The 'communication and IT' page provides resources to enable charities to communicate using the most appropriate language, format, messages and timing, and to influence outcomes. Its governance section provides information to help charities to develop and address governance policies and/or issues. There is also information on planning and evaluation as well as human resources.

In the United Kingdom, the Charities Commission publishes guidance, reports and factsheets on topics including starting up a charity, regulator principles, trustee duties and management, accounting and reporting, charity governance, (including resource management, risk and environmental responsibility), working with other charities and specialist guidance for different sized charities as well as resources for charity advisers, local authorities and other audiences.

## Summary of consultation

The majority of respondents were of the view that management of educational and compliance initiatives by the NFP regulator would be beneficial for both the sector and public. Several respondents were of the view that education (covering auditing, legal advice, training and financial advice) should be a core function of the NFP regulator. Several respondents noted that a simplified regulatory framework would reduce the need for additional education.

In general it was submitted that educational and compliance activities would result in easier access to accurate advice, and would promote compliance. The Cerebral Palsy League responded that educational initiatives would:

*...give more credibility to the sector and provide a one-stop-shop for organisations, reducing the risk of non-compliance, confusion as to responsibilities and provide a simpler framework for business operations.*

Some respondents commented that educational initiatives would especially benefit smaller and newer NFP entities. The Consumers Health Forum submitted:

*...the small size and voluntary nature of many NFP organisations means that many do not have the expertise 'in house' to support compliance with regulatory requirements. Education and support would be invaluable for these organisations, and would also benefit larger NFPs.*

The remainder of submissions were less positive about the benefits of these initiatives and were wary of duplication. They were of the view that the regulator should focus on its regulatory functions, as opposed to educative ones. For example, Community Employers Western Australia submitted:

*...caution must be exercised in introducing a body that takes on a supervisory and accountability function, while also providing a supportive/educational function. This could be contradictory and confusing, and the implications and risks of such joint roles need to be considered further.*

Some respondents felt that there was no need for additional educational guidance, as it is already being provided successfully by peak body organisations. Jason Wilk, for example, submitted:

*...the Peak Body associations understand the specialty regulatory needs of their constituents far better than any centralised government body ever will so it raises the question, should the National NFP just own Tax & Association type regulations and leave all the other regulatory things like Privacy, SPAM, AML/CTF, Health Act, WorkCover with the existing regulators and empower the Peak Bodies to provide the education.*

## Issues

In educating the sector, any regulator needs to balance the sector's demands for guidance, resources and assistance with its ability to effectively regulate. That is, any regulator must remain sufficiently independent from the sector and from stakeholder outcomes so that it carries out its regulatory role fairly and effectively. Overseas experience suggests that

regulation is compromised (for example through lenient outcomes) when a regulator develops too great an interest in the outcomes of a particular regulated entity.

Where a regulator becomes too focussed on assisting NFPs to achieve certain outcomes, NFPs may no longer respect the important role the regulator plays in regulation at the entity and sector levels. To be effective, regulation must be seen as legitimate, accountable and transparent by both the sector and the community as a whole.<sup>18</sup>

Another risk is that entities may become too dependent on the regulator's guidance and view it as representing the state of the law.

Any regulator therefore needs to strike the right balance between providing sufficient levels of education and advice without playing too great a facilitative role.

## Findings

A role of the regulator should be to assist in educating the sector about governance and reporting standards and encourage understanding of and compliance with new regulatory arrangements. The regulator should leverage off existing resources that are provided by peak body organisations and government agencies, and where possible, direct users to this information, by way of web-links. This will ensure that educational guidance does not merely replicate what is already being provided by other sector participants.

Where there are information gaps, the regulator should fill these gaps through the issuing of fact sheets, guidance materials and reports. The regulator should maintain a call centre to answer enquiries and provide referral to peak bodies and government agencies where appropriate.

To ensure that information provided remains relevant, useful and beneficial, the regulator should seek feedback on the content and usability of the educational content once it is operational.

Educational initiatives should be easily accessible and should include guidance materials similar to those currently published on comparable jurisdiction's charities websites and by referral services for organisations requiring external advice. Educational materials should link to those already provided by peak-body organisations.

Whilst stakeholders were highly supportive of the regulator having an educative role, the regulator should not provide advice or educative support that would compromise its regulatory role.

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18 Dr Christine Parker, *Self Regulation and the Not-for-Profit Sector*, (May 2007), p 4. (A report prepared for the State Services Authority by Dr Christine Parker, Associate Professor and Reader, Law School, University of Melbourne).

## **Recommendations**

15. The regulator should produce educational materials for the sector, including a centralised portal of information for NFP entities, web-based training, 'how-to' guidance materials, phone assistance, referral services for organisations requiring external advice, and ongoing consultation with the sector.
16. The regulator should also play a role in relation to educating the public about the sector, including through the oversight of complaints, concerns and surveys about its satisfaction with the sector.
17. Where possible the regulator should leverage off the existing resources and expertise already provided to the sector by peak bodies and government agencies.

# Chapter 7

## Fundraising

### Introduction

The states and territories have responsibility for the regulation of fundraising activities by NFP organisations and impose requirements on entities conducting fundraising activities. Such requirements add to the regulatory burden of the NFP sector and need to be considered as part of any regulatory reform to the sector.

Fundraising plays an important role in the NFP sector, as it is the main way that NFP organisations are able to raise funds to continue undertaking their activities. It is also often the main way that NFP organisations interact with the public, and the more complex the administrative issues they have to deal with the fewer resources they have to dedicate to effective fundraising.

One of the key issues facing the sector is that existing fundraising legislation is outdated and does not reflect the way many of today's fundraising activities are carried out. The outdated nature of the legislation and jurisdictional differences has resulted in some traditional fundraising activities being over-regulated. Over-regulation in these traditional areas imposes a significant administrative burden on NFPs, diverting resources from their core activities, particularly where organisations undertake fundraising activities in multiple jurisdictions.

The existing legislation also makes it particularly difficult for organisations to operate across borders. Organisations operating across borders generally have to register and gain a licence to operate in each jurisdiction, placing a large administrative burden on the sector as a whole.

Outdated legislation also results in additional complexity with the new methods of fundraising being utilised, such as internet, telephone, television and radio appeals. These new methods of fundraising are often under-regulated, and because of their nature, inevitably involve cross-jurisdictional issues. The internet is increasingly playing an important role for NFP organisations in raising funds from the public. Outdated legislation also makes it difficult for the sector, regulators and the public to know what is permissible, and to monitor activities across jurisdictional borders.

In July 2010, the MCCA announced that it would commence a project to harmonise fundraising legislation under the oversight of COAG's Business Regulation and Competition Working Group. At present, fundraising regulation ranges from no regulation in some jurisdictions to significant regulation in other jurisdictions. It is worth noting that while most jurisdictions have some regulation on fundraising activities, the Northern Territory currently has no regulation at all. There are also differences in the nature of the NFP organisations that are regulated across jurisdictions.

## Summary of consultation

The majority of respondents highlighted that fundraising issues are a key concern for NFPs operating across state borders. The lack of consistency in regulation and legislation adds to the overall regulatory burden for NFPs.

Submissions to the consultation paper were generally supportive of the view that a national NFP regulator administering such laws may better reflect the increasing cross-border nature of fundraising.

Many submissions noted that they currently report various forms of data, across different levels of government and according to the nature, size and scope of functions, including on fundraising activities. As the McGrath Foundation stated:

*...substantial information is currently provided to government and includes audited financial statements, annual returns, police clearances for directors, details of every collection for each state, details of bank accounts and specific details of fundraising undertaken.*

The Wesley Mission submitted:

*...the harmonising of Fundraising Legislation for the sector under one body would remove the complexities that [they] currently face. The mix of state and federal fundraising regulation creates a number of inconsistencies producing administrative burdens on many organisations who engage in fundraising activities.*

*This complexity diverts time and attention from core activities. This is especially true in broadly targeted internet, telephone, television and radio appeals.*

## Issues

Fundraising is an important channel through which NFP entities finance their activities. Fundraising legislation has not kept up with changes in technology and the sector's operations. The current inconsistency across jurisdictions regarding fundraising regulation and policy, as well as limited reference to new methods of fundraising, has added complexity to the sector's regulatory framework and increased regulatory burden.

Fundraising legislation covers a complex and widespread array of issues including registration and permission to undertake fundraising, and taxation arrangements. Work undertaken by MCCA analysed key issues and areas of inconsistency across jurisdictions regarding fundraising regulation and policy. The issues were separated into three broad stages of the fundraising process which are pre-solicitation, moment of solicitation and post-solicitation.

This work found that there are few areas of common approach in current state and territory fundraising legislation and policy, and that this divergence and complexity potentially made harmonisation difficult. An outline of the main issues identified are provided below.

## Pre-solicitation

Jurisdictions use different terminology to describe the set of regulated activities commonly referred to as fundraising, including 'fundraising appeals', 'appeals for support' and 'collection for a charitable purpose'.

Most jurisdictions have a form of licensing, registration or scheme of authorisation that operates differently with respect to who is licensed: some jurisdictions register a charity that is then entitled to authorise third parties to fundraise on its behalf, while other jurisdictions license the party that is to conduct the fundraising activity. There is also no common period of authorisation to fundraise under the various regulatory schemes and the information required to obtain authorisation differs in each State and may vary depending on the nature of the body or entity.

## Moment of solicitation

The issues regarding the moment of solicitation are fundraising conduct and information disclosure requirements. All state and territory regimes regulate various aspects of how fundraisers interact with the public while soliciting donations.

Regulations regarding the information that fundraisers should disclose vary. Information disclosure requirements commonly include regulation of face-to-face, door-to-door collecting and telemarketing campaigns and deal with issues relating to whether the collector is paid for their services.

There are different requirements in each jurisdiction relating to fundraising by commercial fundraising organisations (that is organisations that may conduct campaigns on behalf of charitable or NFP organisations for reward) and private participators that may offer support to philanthropic causes, such as by dedicating a percentage of sales to a particular cause. For example, some jurisdictions have requirements that apply to both commercial fundraisers and private participators, whereas other jurisdictions have specific requirements that may relate only to commercial fundraisers or only to private participators.

State and territory fundraising legislation is also largely silent in relation to electronic fundraising, particularly in reference to fundraising via the internet or mobile telecommunications. Only some jurisdictions' definition of 'solicit' or 'collection' includes reference to the internet or fundraising by email, fax or other means.

## Post-solicitation

All jurisdictions have some reporting requirements that apply to entities that are required to be licensed, registered or authorised, however these requirements vary. Some jurisdictions detail their reporting requirements in their primary legislation while others, reporting obligations are imposed by way of conditions upon the relevant licence.

However, as there are no Australian Accounting Standards specifically for the NFP sector and no uniform definitions of key terms such as 'administration' and 'fundraising' expenses, there is no consistency in financial reporting by fundraisers, which makes it difficult to compare reports.

All jurisdictions maintain a publicly accessible online register of fundraisers but this is not required under legislation for all jurisdictions and the extent of information available on those registers is broadly similar but there are some variations. Preliminary analysis of the state

and territory registers of fundraisers suggests that at least 450 fundraisers, representing around 4 per cent of all fundraisers, are registered in multiple jurisdictions.

These statistics do not capture the number of organisations that would like to operate across borders but are discouraged from doing so by the regulatory environment. Moreover, they do not count national organisations that are registered as state branches, nor do they count multi-jurisdictional corporate and third party fundraisers that do not have to be registered in most states. The number of NFP organisations 'crossing borders' through the internet is likely to be higher still.

## Findings

Given the complexity of fundraising legislation, and the importance it has in supporting the work of NFP organisations, the work with the states and territories through MCCA<sup>19</sup> to develop national approaches to NFP fundraising legislation should be considered in the context of broader regulatory reform for the NFP sector. The Government's work could focus initially on harmonising NFP fundraising laws with regard to specific issues which affect NFP entities operating across state borders.

An approach that focuses on harmonising NFP fundraising laws in a limited number of areas could facilitate the development of nationally consistent approaches to fundraising regulation by having significant areas of common interest with the other reforms being progressed as part of the wider NFP reform agenda.

Consideration of fundraising issues, particularly in relation to commercial and third party fundraisers and disclosure requirements, will necessarily involve consideration of fundraising via the internet or through the use of telecommunications. This will interact with existing national laws on consumer protection, such as the Australian Consumer Law and other laws operating in specific sectors, and have particular relevance to the Australian Government's work to address scams and cyber security issues for consumers. In this context, reforms to fundraising will need to be considered at the Commonwealth level both in the context of the NFP fundraising project and through the broader NFP reform process.

## Recommendations

18. Issues common to both the national NFP regulator and NFP fundraising projects should be reviewed by the Government, with coordination between a national NFP regulator and the Ministerial Council for Consumer Affairs' current consideration of fundraising issues.

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19 From 1 July 2011, MCCA will become the COAG Legislative and Governance Forum on Consumer Affairs (CLAGFOCA).

# Chapter 8

## Reporting

### Introduction

Existing reporting arrangements for the NFP sector are ad hoc, uncoordinated, complex and often focused on a particular activity of the entity (for example, acquittal of grants) and do not provide information on activities. This current system imposes a significant administrative burden on entities but may not provide adequate information to the public, recipients of NFP services or governments.

Recent reviews of the NFP sector have called for significant improvement in relation to reporting requirements for NFPs. Current reporting requirements do not reflect the level of funding provided to the NFP sector by the public and by governments.

### Current reporting requirements and developments

The reporting obligation of a specific NFP entity depends on its legal form and activities. NFP entities may have a large, and in some instances, duplicative reporting burden. Other NFP entities that are unincorporated and receive no government funding have no reporting requirements.

There are four main types of reporting undertaken by NFP entities:

- corporate and financial reporting associated with the legal structure under which entities are incorporated;
- financial, governance and performance information required for obtaining or acquitting government funding, or government funded service delivery contracts;
- tax reporting, such as by private ancillary funds; and
- fundraising reporting.

Incorporated associations operate under a tiered reporting framework in the states and territories, with the relevant threshold for the highest tier lower than the thresholds that apply to companies limited by guarantee under Commonwealth legislation. For example, the *Associations Incorporation Act 2009* (NSW) divides associations incorporated in NSW into two tiers for reporting purposes.

- Tier one associations are those whose gross receipts exceed \$250,000 or current assets exceed \$500,000. They are required to prepare audited financial reports and financial statements to their members at an annual general meeting (AGM).
- Smaller, or tier two associations are required to submit financial statements to members at the AGM. Both tier one and tier two organisations must lodge annual financial summaries in the approved form within one month after the AGM.

Reporting requirements for incorporated associations generally vary between states and territories, adding to complexity and compliance costs faced by entities operating across multiple jurisdictions.

Reporting for companies limited by guarantee is also tiered, but with higher thresholds. A tier one company, defined as a 'small company limited by guarantee' comprises companies with annual revenue less than \$250,000 which do not have DGR status. Tier one companies do not have to prepare financial reports or have them audited, nor prepare a director's report, or notify members of annual reports. Tier two comprises companies with annual revenue less than \$250,000 that have DGR status, and companies with annual revenue between \$250,000 and \$1 million, irrespective of whether the company has DGR status. Tier two companies can elect to have financial reports reviewed, rather than audited. They must prepare a directors' report, although with less detail than required of other companies. The company must give annual reports to any member who elects to receive them. Tier three companies are those with annual revenue of \$1 million or more. They must prepare audited financial reports, a directors' report and must give their annual reports to any member who elects to receive them.

Reporting requirements associated with funding arrangements for the delivery of government services generally involve complex reporting obligations and result in the duplication of reporting requirements. The sector has indicated that this is particularly evident with acquittal of grants.

NFP entities entering service delivery contracts with the government are required to provide information on financial health and performance, general capabilities and governance structures. This information is also required to be provided to regulatory agencies such as ASIC.

Some work has been done to improve reporting practices. A new national standard chart of accounts (SCOA) for reporting by the NFP sector has been developed and is being adopted by Commonwealth, state and territory governments. New South Wales, Victoria and Queensland adopted the SCOA on 1 July 2010, with other jurisdictions planning to follow suit from 1 July 2011. The SCOA will make sure that different governments ask for basic financial information in the same way so that NFPs can report in a standard format. The SCOA does not however reduce the need for organisations to report multiple times, instead, it standardises reporting terms. Adoption of the SCOA by NFPs is currently voluntary.

## The Australian Accounting Standards Board

The AASB could play a role as part of any framework for harmonising reporting.

The AASB is an independent agency of the Australian Government with responsibility to make accounting standards under section 334 of the Corporations Act, to formulate accounting standards for other purposes and to participate in and contribute to the development of a single set of international accounting standards for worldwide use.

One general aim of the AASB is that all standards should be sector-neutral—meaning that there will be no need to have standards that are specifically developed for the government sector, the NFP sector or the for-profit sector. There are however some standards which exclude NFP entities or public sector entities from their application and offer alternative guidance; for example, AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance*.

The AASB has a NFP (private sector) Focus Group that is designed to increase participation by those involved with these entities in the accounting standard-setting process and enhance feedback from the perspective of a significant group of preparers and users of financial reports.

The Group comprises members with expertise and involvement in charitable and related organisations who are a key source of information for providing feedback to the AASB on selected projects.

The Group assists the AASB at all stages of the standard setting process, including in identifying issues and priorities of particular interest to the NFP sector and providing input during the development phases of projects from both a user and preparer perspective.

## Standard Business Reporting

Similarly, the adoption by NFPs of SBR may provide another means of reducing the reporting burden. The Australian Government's SBR initiative, implemented on 1 July 2010, allows businesses (including NFPs), with contemporary SBR-enabled software to lodge a range of financial and payroll returns to a number of state, territory and Australian Government agencies. It is possible to extend SBR to additional reporting requirements, including those specific to the NFP sector in order to reduce the regulatory reporting burden.

SBR is a mechanism that allows reports to government agencies, using commercial business software, to be drawn from business accounting, payroll and other records to be compiled and submitted electronically through a single channel.

A core component is the SBR Taxonomy, a dictionary of agreed and harmonised definitions providing context for information sought by agencies. The SBR Taxonomy has been designed to be compliant with Australian and international accounting standards. It allows individual elements of data to serve multiple purposes without requiring additional manipulation.

SBR provides a single 'sign-on' credential and does not require businesses to log onto multiple portals.

It reduces the reporting burden for organisations through reduced effort in compiling and submitting reports to government agencies. In particular, it does this by using commercial business software to automatically pre-fill information, providing an electronic interface to agencies directly from accounting software, and providing validation and confirmation of receipt of reports.

SBR has been co-designed by Australian, state and territory government agencies in partnership with software developers, businesses and their accountants, bookkeepers, tax agents and payroll.

A prerequisite for extending SBR into specific NFP reporting would be the clarification and consolidation of reporting requirements for all agencies and jurisdictions. In addition, further consultation with stakeholders such as the software developers that support this sector would be necessary to ensure their support for this expansion.

Some examples of the reports currently in scope for SBR include the Business Activity Statement (for the ATO), financial statements (for ASIC), and payroll tax returns (for state and territory government revenue offices).

## Summary of consultation

Respondents were asked about the information that they currently provide to government. Less than half of the submissions responded to this question, but those that did said that a wide variety of non-uniform requirements are currently in place, with some overlapping.

A significant proportion of the compliance burden on NFP entities relates to grant acquittal requirements imposed by funding agencies within the Commonwealth, states and territories.

Submissions received on the scope and functions of any NFP regulator suggest that the sector's compliance costs are significant and that there is scope to streamline and remove reporting duplication. For example, Rotary Australian World Community Service Limited stated that:

*...the 'report-once, use-often' model of reporting offers a streamlining of compliance requirements and a huge potential saving by reducing the duplication of reports for various users. This is particularly so where an entity is in receipt of grants from various governments or government agencies.*

In a similar vein UnitingCare Australia submitted:

*...there would be enormous benefit in all governments committing to a policy of report once use often, especially in relation to organisational and compliance data requests.*

PriceWaterhouse Coopers also pointed out that a 'report-once, use-often' approach would facilitate competition amongst NFPs:

*Streamlined access to information by users would assist comparison: as competition for funding continues to grow, parties who receive funding requests are likely to seek to better understand the methodology behind the organisations' operations in order to draw conclusions on both the efficiency and the effectiveness of the organisation. Having a one-stop-shop would make it easier to access this information.*

Six respondents supported that concept of 'report-once, use-often' so long as it delivered the promise of reduced reporting. For example, the Victorian Government cautioned that:

*...it is important to ensure that single standard reporting arrangement does not end up adding to the number of reports required or reporting required.*

The area of duplicative grant acquittals and associated audit costs was confirmed as a key priority in this consultation process. An example of the duplicative nature of the current process and what would need to be reviewed was submitted by the Benevolent Society:

*The Benevolent Society receives around three-quarters of its income from federal, state and local government agencies or authorities. Each federal, state and local agency or authority issues its own range of funding or grant agreements. In addition, each funding program within an agency or authority may issue its own funding or grant agreement. Each government funding contract sets up a separate regulatory framework. Currently, the Benevolent Society has approximately 100 different contracts on-foot with federal, state and local government agencies.*

*The Benevolent Society has over 800 staff and 700 volunteers supporting more than 31,000 children and adults each year, primarily in New South Wales and Queensland. They deliver 122 programs in 55 locations covered by over 100 contracts with federal,*

*state and local government agencies, the total value of which is around \$50 million per year. As a company limited by guarantee, the Society is already subject to an annual audit by a qualified auditor as part of its Corporations Act and Australian Accounting Standards requirements/obligations, but different government agencies also require their grants to be individually audited. The potential for big compliance cost savings is clear, but so is the risk of unintentionally increasing compliance costs.*

Other submissions lamented the fact that acquittal reporting is not in line with accounting standards and suggested that entities should only have to prepare and lodge one report covering all grants received during a year.

The submissions indicated that there was support for applying SBR to the NFP sector, especially if sufficient resourcing and support is provided to encourage take up. For example, the Institute of Chartered Accounts responded:

*SBR is the means whereby the 'report-once, use-often' goal can be brought about. Appropriate tagging of the information will enable the automatic generation of a variety of financial reports.*

Some respondents indicated that SBR would appeal to larger NFPs as the set up costs for smaller NFPs would be prohibitive. PriceWaterhouseCoopers responded:

*Some larger NFPs would welcome the opportunity to use SBR. Given their importance to the sector it will be worthwhile to implement. However, the use of SBR should not be made mandatory as many smaller NFP entities are not likely to have appropriate resources available. They would have to pay agents to do this for them which would be an unnecessary cost, reducing the funds available for charitable purposes.*

Three submissions called for the involvement of the Australian Accounting Standards Board as part of any reporting harmonisation project. For example, PriceWaterhouseCoopers commented:

*A NFP Regulator should also work together with other regulators and other bodies to ensure there is no duplication of activities and possible creation of inconsistent and incompatible rules. Examples of these bodies are: ASIC, the ATO, Australian Auditing Standards Board (AUASB), AASB. It is our view that Accounting and Auditing Standards should be provided by the AASB and AUASB regardless of the type of entity. However the NFP regulator should liaise with these bodies to ensure the standards applying to NFP's are meeting the users' needs.*

## Issues

Australians have a high level of philanthropic engagement and provide significant philanthropic support to the sector. Despite this, the Australian public and Australian governments know very little about the operations of this growing sector.

Reporting requirements ensure that NFPs are accountable to the public that uses their services and products and helps fund their activities (both directly and indirectly by way of tax concessions). Reporting also promotes a culture of self-compliance by making the activities of NFPs more transparent and therefore open to sector, regulator, public and government scrutiny.

In designing a reporting framework, the regulator would need to balance the accountability and transparency gains that reporting provides with the compliance burden currently faced by many entities in the sector. The framework must also recognise the Government's use of reporting as a risk mitigation tool, that is, as a means of reducing the risk that NFPs may use public monies for non-allowable purposes, for example, for purposes outside the terms of a grant or outside the tax law.

Anecdotal evidence suggests that reporting for auditing purposes is very expensive, with audit costs reaching \$1,000 per grant in addition to the auditing costs for financial reports. Any reporting framework should therefore balance the benefits of a rigorous audit process with the burden and costs involved in requiring some NFPs to complete them.

Similarly, the reporting framework should balance the benefits that SBR may promote, with its costs and utility, especially for smaller NFPs.

## Findings

Based on the submissions there is strong support for the introduction of a 'report-once, use-often' reporting system as it will lead to efficiency gains and compliance savings. Whilst a 'report-once use often' approach may increase the reporting burden for smaller NFPs, this increase is expected to be small. There was concern from stakeholders that if not properly implemented, a new reporting framework would add to the reporting burden. To be effective and deliver on the promise of 'report-once, use-often', the regulator should not only be a central collector of reports but should harmonise reporting requirements between the Commonwealth, state, territory and local governments; determine the form of financial reports in consultation with the NFP sector and government agencies and take responsibility for the SCOA.

The introduction of a 'report-once, use-often' system is likely to improve transparency and compliance, and, if reports are published on the information portal, will promote public trust and confidence in the sector, improve competition amongst sector participants and increase philanthropic engagement.

The current burden on NFPs caused by the grant acquittal process is high and is taking away from the time, money and resources of many NFPs, particularly smaller NFPs. This burden would be markedly reduced if acquittals reporting were outcomes based and does not include financial reporting or reporting related to organisational governance. The greatest simplification would occur if the acquittals reporting process could be brought into the regulator's 'report-one, use-often' framework where possible.

To ensure compliance with current accounting standards, the regulator should work with the AASB to ensure that the standards that currently apply are AASB compliant and relevant to the sector.

Finally, applying SBR to a new NFP reporting framework, as supported by many respondents, would provide a consistent government approach to reporting for software developers and businesses and leverage off the infrastructure and mechanisms that have been developed for SBR. It may however be difficult to encourage take up of this product, as many smaller NFPs may find it an unnecessary expense.

## Recommendations

19. A 'report-once, use-often' approach should be adopted in relation to financial reporting from NFPs. Reporting should reflect 'smarter regulation' and the trade-off between standard reporting and simple reporting should be carefully considered as part of the development of the standard report.
20. The regulator should act as a central reporting coordinator of financial and other information and as such should:
  - be responsible for the SCOA;
  - harmonise reporting requirements between Commonwealth, state, territory and local governments; and
  - determine the form of the financial report in consultation with the NFP sector and government agencies.
21. Each entity should provide information for reporting purposes but the content should be proportional to the size of entities, risk factors and level of sector and government assistance. Small entities should be required to provide no more than a post card of information.
22. The AASB should continue to ensure that Australian accounting standards take account of NFP issues and identify any gaps in this area.
23. The regulator should work with the AASB to provide guidance on NFP accounting issues
24. Acquittal reporting should be outcomes based and should not include financial reporting or reporting related to organisational governance.
25. Consideration should be given to bringing acquittals reporting within the regulator's 'report-once, use-often' framework where possible.
26. Consideration should be given to utilising SBR for NFP reporting.



# Chapter 9

## Information portal

### Introduction

There is currently no single source of public information on the activities of charities and other concessionally taxed NFP entities. Some information is currently publicly available, for example, in relation to tax concessions on the ABR, financial reports from ASIC (fees generally apply for access to this information) and from state and territory agencies in relation to incorporated associations (fees also generally apply for access to this information). South Australia currently provides information about entities that hold a 'charity licence' on its charities website.<sup>20</sup>

The United Kingdom, New Zealand, Singapore and the United States have all utilised public information portals to improve transparency and accountability in their respective charitable sectors. While difficult to measure, anecdotal evidence from New Zealand and the United Kingdom suggests that these portals have increased public engagement with the sector and have enhanced sector connectivity.

### Summary of consultation

The majority of respondents were in favour of an NFP public information portal, reasoning that it would reassure people about the legitimacy of the sector. The Melbourne Community Foundation supported the introduction of a portal on the basis that:

*The goal of a single national regulator is to promote the public interest, trust and confidence in the NFP sector by providing relevant, useful and accessible data and information about the sector.*

Similarly, Whitelion Inc. responded that a portal would:

*have a range of benefits to stakeholders across the community. Through listing all registered charities, the public would be better able to find information on a given charity, and indeed confirm the validity of a charity should there be doubts as to a charity appeal. Further, for Government agencies and philanthropic funders, the centralised provision of general purpose financials on an information portal provides scope for greater efficiency and rigour in risk assessments. Whitelion believes that a NFP information portal has the potential to increase transparency in the sector, and thus build public trust in the NFP sector.*

There were differing views regarding the type and level information to be shared on the portal. A common theme was that the portal should only display information that is useful and non-duplicative. For example, Jason Wilk cautioned that a portal may merely replicate a 'multitude of portals that already exist care of the peak bodies and interest groups that understand that unique issues faced by their constituents.'

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<sup>20</sup> [http://www.charities.sa.gov.au/default.asp?action=charities\\_list](http://www.charities.sa.gov.au/default.asp?action=charities_list).

Another theme concerned the level of disclosure required by NFPs. Some respondents, such as CPA Australia Third Age Network Committee, favoured a very high level of disclosure, stating:

*No information should be withheld from public access unless it can be proved — not merely asserted — that its release would cause harm. Harm would not include mere embarrassment.*

Other respondents expressed concern over the publication of private information. World Vision, for example, wanted to exclude:

*any information which would be 'personal information' under the Privacy Act or which has been provided on the basis of confidentiality by an NFP entity to the regulator.*

Respondents suggested that the portal should make public:

- a searchable list of registered entities;
- the focus of the organisation and the areas in which it operates;
- a company's constitution;
- annual information statements;
- information on governance obligations;
- educational tools;
- information on funding options; and
- broad statistics on the sector.

Few respondents indicated that certain information should not be made public. This information included:

- financial data;
- addresses of membership;
- information leading to inadvertent identification of clients or client circumstances; and
- donors' names.

## Issues

To be effective any public information portal should strengthen the sector and public engagement. A portal should also bring about greater sector connectivity so that sector participants can learn from each other, share findings and pool resources where appropriate.

An effective portal would enable NFPs to realise the goals of the 'report-once, use-often' framework since it would allow for the publication of reports and thereby reduce the reporting burden.

The utility of any public information portal will depend on the relevance of the information that is published, its accessibility and the extent to which it is used to achieve the goal of 'report-once, use-often.' Accessibility may be enhanced if NFPs are able to control some of the content on the site. Any regulator needs to consider the feedback of the sector to ensure that the information the portal provides remains relevant and useful.

## Finding

The lack of a single source of public information for members of the community seeking to access reliable information on charities and DGRs reduces public confidence in the sector, restricts informed choices and philanthropy and public engagement more generally, and discourages appropriate levels of sector accountability and governance.

The introduction of a public information portal would provide a single, easily accessible source of detailed information about NFP entities in Australia and will benefit the public, the NFP sector and governments.

The NFP information portal should be based on overseas models, including the New Zealand Charities Commission website, the UK Charities Commission website and the Guidestar websites in the UK and USA.

The information portal will provide education and support materials for NFP entities as well as providing information on the activities and accounts of entities which receive tax concessions and broad statistics about the sector for the information of the public. Providing this information will result in higher levels of confidence in relation to donations and volunteering, and a greater level of public understanding of the NFP sector as a whole. Both these benefits will support the philanthropic engagement of the public in the long term.

The form, content and functionality of the information portal should be subject to ongoing feedback from stakeholders.

## **Recommendations**

27. The Government should proceed with a public information portal for registered entities.
28. The information portal should be established and maintained by the regulator.
29. The portal should be operated in consultation with and link with the ABR.
30. The information to be displayed on the portal could include information on issues such as sphere of operation, income and expenditure, financial history, contact details of persons managing the entity, governing documents, annual reports, trustees' reports, and summary information returns.
31. NFPs should be allowed to control some of the content on parts of the site.
32. NFPs should be able to make qualitative statements about their activities and performance.
33. The portal should provide NFPs with centralised government guidance and information.
34. The portal should allow links to other websites, including those which provide information on other Government accreditation and licenses.

# Chapter 10

## Governance, disclosure and compliance

### Introduction

While some organisations have effective and thorough governance policies in place, the arrangements for other organisations do not meet community expectations in relation to organisations in receipt of public monies. Recent trends have seen higher levels of governance and accountability required of both the commercial and government sectors in Australia, however, the NFP sector has largely been ignored. The overall governance and accountability arrangements in the NFP sector have not kept pace with international trends to improve the governance of the sector.

Whilst NFPs are unlikely to have shareholders, they are still accountable to those interested in the development and running of the entity, such as members, donors and other stakeholders.<sup>21</sup>

In New Zealand, the *Charities Act 2005* requires the New Zealand Charities Commission to educate and assist charities in the area of best practice in governance and management. As such, its website provides various resources about suitable governance policies and procedures.

In the United Kingdom, the Charities Commission website also provides resources to assist trustees improve the effectiveness of their charity, and uphold the principles of their regulatory framework.

In Canada, the Canada Revenue Agency offers charities extensive educative and guidance materials, including webinars on governance issues, such as avoiding non-compliance.

In the United States, the Internal Revenue Service (IRS) sees the role of good governance as increasing the likelihood that organizations will comply with the tax law, protect their charitable assets and, thereby, best serve their charitable beneficiaries. Current IRS positions on NFP governance are best reflected in the reporting required by the revised Form 990, which provides a checklist of governance activities.

Improved governance arrangements will lead to greater transparency within the sector and consequently help to promote trust, confidence and philanthropic engagement with the public.

### Minimum standards

There are various minimum governance standards that currently apply to the sector. The Corporations Act, for example, contains various duties regarding directors' conduct and penalties for their breach. Current legal duties incumbent on directors include the duty to act in good faith in the best interests of the objects of the company, not to act for an improper

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21 ICSA Principles of Good Governance for Charities, p 4

purpose, to act with care and diligence (subject to the business judgement rule), not to improperly use position or information, and to avoid a conflict of interest. These rules are currently only applicable to the minority of NFPs registered as companies limited by guarantee. Mangers of incorporated associations owe similar common law duties.

Trustees are also subject to various common law duties, including a duty to acquaint themselves with the terms of the trust, to execute the trust according to its terms and the general law, to protect and preserve the trust property, to exercise discretionary powers or discretions in good faith, upon a real and genuine consideration and according to the purpose for which the power was conferred, not to delegate except as permitted by the trust instrument, and to invest as permitted under the trust deed and legislation.

The various state and territory trustee acts and trust acts require trustees to exercise a power of investment with the care, skill and diligence that a prudent person would exercise in managing the affairs of other persons. Additionally, trustees are required at least once in every year to review the performance of trust investments and must have regard to a number of matters when making an investment. In addition, the trustees/directors must ensure that the trust is not accumulating more than permitted by the trust deed or the ATO.

Various obligations also apply to incorporated associations and their committees of management. For example, in South Australia committee members are required to act honestly and with reasonable diligence in the discharge of their duties. In the Northern Territory and South Australia, committee members are prohibited from doing acts with intent to deceive or defraud the association, its members or creditors. In New South Wales, the Northern Territory, South Australia and Victoria, committee members are prevented from making improper use of their position, or of information gained by reason of their position, or gain directly or indirectly an advantage for themselves or any other person or to cause detriment to their association. Most states and territories also have rules imposing a duty on members to disclose pecuniary interests in a contract or a proposed contract.

Whilst the rules governing trustees appear comprehensive, in reality their scope is quite limited, given the difficulties associated with compliance action.

## Dealing with risks of corruption, money laundering and terrorism financing in the NFP sector

There are risks of corruption in the NFP sector as in any sector. As the NFP sector broadly holds the trust of the community, it can be particularly at risk. Its high use of volunteers and the lack of resources available to check on their credentials and supervise their activities are also a risk factor.

At the most serious end of the scale, individuals may seek to infiltrate NFP entities to launder money or finance terrorism. A combination of low reporting requirements and sending money overseas provides an opportunity for such individuals.

Another example of corrupt conduct may be the false acquittal of a government grant, or its expenditure on purposes it was not intended for. A similar example may be the spending of donor funds on private purposes.

The fundraising process may be corrupted if NFPs use fundraising companies that claim an inappropriately high proportion of publicly donated funds for their fee; an amount higher than 10 per cent may be considered inappropriate by the public.

As a member of the FATF (an inter-governmental body dedicated to combating money laundering and terrorist financing), Australia has agreed to comply with FATF recommendations. FATF Special Recommendation VIII (SR VIII) requires FATF members to 'combat the misuse of NPOs (nonprofit organisations, that is, NFPs) for the purpose of terrorism financing'. In FATF's last review of Australia's progress, it found that Australia was only partially compliant with SR VIII.

## Summary of consultation

Respondents to the consultation paper were asked about the appropriateness of the core rules and the regulatory framework as proposals to improve governance. There was broad support from 31 submissions for the suggested core rules and regulatory framework, while 35 submissions opposed specific rules like the power to suspend NFP officers and impose a decision-making structure. Those respondents preferred that the Corporations Act be used as a model and that a principles-based, not prescriptive, approach be taken. Twenty two submissions completely opposed the suggested core rules and the regulatory framework.

The Australian Institute of Company Directors described the 'core rules' approach as one having 'serious misgivings' with 'risks of unintended consequences in terms of administrative burden, compliance risks and costs, and the shifting of liability (especially to volunteers).'

The submissions noted that reforms need to take account of the high level of volunteerism and the reluctance of volunteers to pay for training. They also noted that stricter governance requirements will deter volunteers from participating on NFP boards. A regulator providing training would assist to encourage volunteers to participate in the NFP sector. Meals on Wheels, an organisation that relies on over 70,000 volunteers, stated:

*Meals on Wheels services are staffed almost exclusively by volunteers. The potential for a new NFP regulator to assist services to better understand their regulatory requirements may be of great benefit, particularly to small, individually incorporated services. This service, if offered, would need to be simple, supportive, and encouraging, and not necessitate costly or time consuming training obligations.*

The submissions noted that reforms need to take account of the high level of volunteerism and the reluctance of volunteers to pay for training. They also noted that stricter governance requirements will deter volunteers from participating on NFP boards. A regulator providing training would assist to encourage volunteers to participate in the NFP sector.

The NFP Project at the University of Melbourne's Law School expressed doubt whether the proposed rules would replicate existing duties or whether the intention was that the framework would modify or adapt the current rules. The concern about duplication was also expressed by the Australasian Compliance Institute since it felt that a 'significant body or work already exists in terms of the responsibilities of Company Directors as outlined in the *Corporations Act*.'

The Project also expressed doubt about the capacity for the model decision making and accountability frameworks to 'cater adequately for the diversity of the sector.' This concern was also expressed by respondents who supported the core rules, such as the Federation of Ethnic Communities Councils of Australia, who suggested that the rules should 'allow flexibility and recognise the diversity within the culturally and linguistically diverse NFP sector.'

Regarding the question on the powers required to improve governance and regulatory oversight, most respondents did not answer the question. Some respondents were cautious of an over-zealous regulator, as expressed in PilchConnect's submission:

*while PilchConnect supports the creation of a national regulator with real enforcement powers and a presence and influence in the sector, it cautions against the creation of a regulator focused on a deterrence model of regulation that seeks to 'police' the sector.*

The Australian Catholic Bishops conference feared that over-regulation may stifle the growth of the sector.

## Issues

The diversity of the sector should drive consideration of suitable governance arrangements. Anecdotal evidence suggests that some organisations need no additional assistance in this area, whilst others need significant guidance since they may have minimal governance arrangements in place.

The arrangements would need to balance the flexibility that a principles-based approach offers with the certainty that a prescriptive approach offers. Principles-based governance arrangements may be appropriate for organisations with a sophisticated understanding of good governance outcomes, but may be inappropriate for organisations that lack the resources to devise rules specific to their particular organisation. On the other hand, a prescriptive approach may disadvantage organisations with already suitable governance arrangements in place and may add to compliance costs.

Regarding the powers of any regulator, a balance needs to be struck between rules to deter malfeasance with a culture which promotes compliance and self-regulation.

In the terrorism-financing space, Australia has an international obligation to combat terrorism financing as a party to the *International Convention for the Suppression of the Financing of Terrorism* and pursuant to UN Security Council resolutions on terrorism. As other countries put systems in place to protect NFP entities, terrorists are likely to look to those countries where lack of awareness means that the NFP sector is more vulnerable to misuse. It is therefore important that Australia improves its governance standards so as to contribute to reducing opportunities for terrorism financing globally.

## Findings

Whilst the submissions were generally supportive of improved governance arrangements, respondents were cautious of an overly prescriptive approach. A principles-based approach would however be largely welcomed by the sector, particularly for smaller NFPs who often lack the resources to develop adequate governance policies.

Any governance rules developed should be principles-based and take into account the size of the organisation, the risks it presents by virtue of its activities and turnover as well as the level of government support an organisation receives. Where possible any regulator should consider the existing frameworks applied by ASIC and the ATO and the rules governing trusts.

To effectively regulate the sector, over the long term, any regulator should be given powers of asset protection (which would enable the regulator to protect an NFP's assets if malfeasance were detected), suspension and/or replacement powers (in the case of a serious breach by a responsible individual), powers to register and deregister any NFP, enforce governance rules and commence investigate processes, powers to implement proportional compliance activities (such as the power to issue warnings and penalties and provide information to non-compliant NFPs) and powers to undertake dispute resolution processes, which would permit the regulator to intervene in any dispute of which an NFP is a party, both within the NFP and between the NFP and another entity. Finally, any regulator should be given appropriate enforcement powers including the imposition of fines and civil penalties, information gathering powers and general supervisory powers.

Regarding terrorism financing issues, NFPs should have procedures in place to know who they are dealing with, who their beneficiaries are, and to take seriously the risk that they could inadvertently be participating in terrorism financing. The Attorney-General's Department has published detailed guidance which is online from the Department's website.<sup>22</sup>

The powers of any regulator should include information sharing with enforcement agencies like the Australian Federal Police, the ATO and ASIC. It should also be easy for members of the public, volunteers and NFP staff and directors to report suspected malfeasance to the authorities. Telephone hotlines are an important mechanism for many Australian Government agencies.

Governance principles for NFP entities that work overseas should include consideration of which members of the entity are responsible for the entity's financial records, volunteer credentials, overseas activities and associations with other charities and beneficiaries. Governance should consider any possible conflicts of interest or opportunities for corruption, for example, an entity's income received and moneys spent should ideally be accounted for by different individuals within an entity. Given the low resourcing available to many NFPs, there may not be adequate scope to do this which increases the importance of financial disclosure, and the role of the regulator in providing training, assisting officers with their compliance responsibilities, and regular risk based monitoring.

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22 [http://www.nationalsecurity.gov.au/agd/WWW/nationalsecurity.nsf/Page/What\\_Governments\\_are\\_doing\\_Risk\\_of\\_Misuse\\_-\\_Terrorism\\_Financing](http://www.nationalsecurity.gov.au/agd/WWW/nationalsecurity.nsf/Page/What_Governments_are_doing_Risk_of_Misuse_-_Terrorism_Financing).

## **Recommendations**

35. Organisational governance rules should be proportional to the size of entities, risk factors and receipt of public and government assistance.
36. The regulation of service provision should remain with existing entities.
37. Government contracts should no longer mandate organisational governance requirements for NFPs.
38. Treasury should undertake a review to determine what, if any, should be the core organisational governance principles applying to registered NFPs.
39. Over the long term, the regulator should be provided with powers regarding asset protection, the suspension and/or removal of responsible persons, registration and deregistration, the enforcement of governance rules, investigative processes; enforcement powers, including civil penalties and the imposition of fines, proportional compliance activities, and, dispute resolution processes.

# Chapter 11

## The form of the national regulator

### Introduction

#### Current regulation

Regulation of the NFP sector is currently a shared responsibility between the Commonwealth and the states and territories. The current regulation of the sector by numerous bodies at the Commonwealth, state and territory levels results in the imposition of an unnecessarily high regulatory burden on some entities while other entities are inadequately regulated.

Commonwealth regulation of the NFP sector is primarily through the tax system and the corporate regulatory framework. The Commonwealth also places requirements on NFP entities which access Commonwealth grants or enter into contracts with the Commonwealth.

Regulation at the state and territory level can include regulation of incorporated associations, and charitable trustees. Additionally, states and territories regulate for consumer protection purposes (related to fundraising by NFPs), and for access to state grants and contracts.

In addition, governments undertake ad hoc regulation of certain activities, for example, to regulate the quality of services provided by NFPs, such as the provision of aged care, child care and health services.

The complex interrelationship between state and territory regulation in the NFP sector will necessarily influence the form which the national regulator would ultimately take. The extent of a national regulator's powers will depend on the cooperation of the Commonwealth, state and territory governments.

The ATO is currently the default charity regulator at the Commonwealth level, as a result of its role to determine charitable status and administer charitable tax concessions. Consequently the ATO has the highest degree of expertise in the NFP sector.

#### Legislation

For a new body to be established, it needs to be considered whether it should be established as a separate body and the appropriate legislation under which it would be established, or if it should be established as a separate statutory office within an existing body.

The Department of Finance's guidelines for the structure and governance of new bodies states that it is generally preferable that bodies operate under *the Financial Management and Accountability Act 1997* (the FMA Act).<sup>23</sup> These bodies are considered to be financially part of the Commonwealth. Government bodies established under the FMA Act hold public money which can only be spent under the authority of an appropriation from the Australian

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23 Department of Finance, *Governance Arrangements for Australian Government Bodies*, 2005, p. x.

Parliament. The FMA Act should especially apply to primarily budget-funded bodies, regulators and bodies that raise public money under a Commonwealth law.

Regulators with similar roles and functions to those envisaged for the NFP regulator, including ASIC, the ATO and the Australian Competition and Consumer Commission, are established as agencies under the FMA Act within the Treasury portfolio.

In cases where a governing board appears to be essential for the effective governance of a body, it is considered appropriate for the body to operate under the *Commonwealth Authorities and Companies Act 1997* (CAC Act). Bodies established under this Act are both legally and financially separate from the Commonwealth. The extent of government control over a CAC body depends on its establishing legislation. However, ministers retain responsibility for legislation in their portfolio and this will, typically, include the right to access information that helps with the oversight of this legislation. Ministers are also entitled to expect advice and assistance from their departments in this role.

A separate statutory office could also be established within an existing body. The establishment of a statutory office within either the ATO or ASIC could allow for a completely separated body within that organisation, while utilising existing resources.

## Reviews

Several recent reviews and inquiries have recommended a NFP regulator be established. However there were divergent views on the location of the regulator. The AFTS Report recommended the establishment of a national charities commission, whereas the PC Report recommended the establishment of a regulator within ASIC.

## Summary of consultation

The consultation paper presented a number of options, including an interim regulator. The development and establishment of a fully functioning national regulator will take time, and an interim regulator would allow reform to begin during the development phase, allowing some reforms to be undertaken now.

Of the submissions 44 opposed an interim regulator, especially if it was located in the ATO, while 14 submissions were supportive of an interim regulator, including if it was in the ATO. Most of the remaining submissions did not comment on this issue. This may also relate to one of the key concerns raised by stakeholders throughout the consultation process to avoid additional duplication of regulation or increase of regulatory burden.

Related to these issues were concerns about the best process for advancing reform. For example, the Asylum Seeker Resource Centre stated in reference to both an interim regulator and the reform process that:

*No — an interim regulator should not be used. Instead, a set of regulations and guidelines for compliance should be developed and issued to NFPs with a grace period of 12 to 18 months to help them develop systems to meet regulatory requirements. This period should allow for feedback and training opportunities. This information should then be used to create the full scale regulatory system within 12 to 18 months.*

## Issues

### National NFP Regulator

A new national regulator would be in line with community expectations for regulatory reform of the NFP sector, given the many reviews and inquiries which have recommended a regulator in this form as well as overseas developments.

The Commonwealth does not have the necessary constitutional power to establish a truly national regulator without the support of the states and territories.

There are three alternatives for the establishment of a national NFP regulator and regulatory framework, namely, a referral of powers by the states to the Commonwealth, a cooperative legislative regime based on model Commonwealth legislation or a cooperative legislative regime based on model state legislation. The final form of the regulator would be determined following negotiations with the states and territories.

Owing to the requirement to gain the agreement of the states and territories to establish a national regulator with full powers, the Commonwealth could immediately begin to progress the development of a national regulator through COAG.

COAG negotiations could provide a forum for consultation on areas such as the regulation of incorporated associations and charitable trusts, as well as areas of high regulatory burden for the NFP sector such as reporting and grant acquittals.

In addition, negotiations through COAG may be perceived as not delivering adequate regulatory improvements in the short term. However, progressing these negotiations in tandem with immediate reforms will ameliorate these concerns.

### Commonwealth NFP Regulator

Given the complexity of issues involved, it may take some time for agreement to be reached on a national regulator. It may take some time for measures such as harmonisation of legislation to be achieved. If no intermediate steps are taken, there may be long delays before any regulatory improvements are delivered for the NFP sector.

A Commonwealth NFP regulator can deliver significant benefits to the sector in the short to medium term. A Commonwealth regulator can centralise the Commonwealth's regulatory interaction with NFPs, providing significant simplification and streamlining of these regulatory arrangements.

A Commonwealth regulator can also provide the foundations of further reforms for the NFP sector as its functions and powers could be expanded over time to further reduce red-tape.

A balance needs to be struck between providing the sector with a fully separate and independent NFP regulator, the cost of such a regulator, the need to avoid a new layer of bureaucracy and the need to avoid pre-empting any model that COAG may agree to.

## An interim regulator within either ASIC or the ATO

### ASIC

ASIC regulates approximately 11,000 NFP entities incorporated as companies limited by guarantee under the Corporations Act. Additionally, ASIC has responsibility for the registration of incorporated associations and cooperatives if they wish to operate outside of their home jurisdiction.

There are several arguments in favour of ASIC acting as a NFP regulator, ASIC registers and regulates a number of NFP entities and is the national portal for the collection of corporate and financial public record information entities under the Corporations Act. There would also be synergies associated with ASIC's IT services, corporate governance education support and national presence. In this context, the PC Report recommended that a 'one-stop shop' for Commonwealth regulation of NFPs should be established as a statutory body or organ within ASIC.

However, ASIC's focus as a corporate regulator, that is strongly focussed on corporate and financial market matters, means it is unlikely to be considered as an appropriate body to accommodate a statutory office that is committed to the regulation of the NFP sector.

In addition, all NFPs would need to be incorporated entities which would reduce the current flexibility of legal structures and be highly burdensome for NFPs.

Furthermore, ASIC provides some guidance material on registering charities and NFP companies under the Corporations Act, which is general in nature and concerned primarily with compliance obligations.

A new statutory office within ASIC would be able to provide regulation for limited additional costs to the Commonwealth compared to a new Commonwealth body. It could also be established in a shorter timeframe than a new body. A separate statutory body would also be able to address some of the concerns in relation to ASIC's corporate focus.

However, ASIC would not have the systems and technical knowledge of the sector that the ATO has that would allow a knowledge transfer of NFP expertise.

### The ATO

In many ways the ATO already acts as the default regulator of the NFP sector through its role in processing access to tax concessions for which the sector is eligible. As a result the ATO has the greatest interaction with and knowledge and expertise of the sector. Additionally, initially establishing a national NFP regulator within the ATO would have the benefit of taking advantage of the ATO's presence in all states and territories.

There is a perceived conflict of interest within the NFP sector between the Commissioner of Taxation's revenue collection focus and his role as default NFP regulator. However, structural separation and branding would help to address the risk of a perceived conflict of interest.

This approach would be similar to the approach adopted in Canada and the United States (which are federations like Australia with set powers given to the national government). Both countries use their relevant tax authority to regulate charities, with an explicit 'Charities Directorate' established within Canada's tax authority.

An independent statutory office could be established that was structurally separated from the ATO. This would limit additional costs to the Commonwealth of establishment and minimise the time of establishment. In addition a separate statutory office would ensure that the expertise of the ATO in charitable and NFP law is retained and that knowledge is transferred. However, it would also allow a NFP regulator to be completely independent and to have a different organisational culture.

### Advisory board

An advisory board of professional NFP sector experts could be appointed, in order to provide the regulator with guidance on decisions and guidelines. An advisory board would also help to ensure sector confidence in decisions of the regulator, and would demonstrate the independence and new organisational culture of the NFP regulator.

### Independence

The independence of the regulator is important for the NFP sector to have confidence in its decision making processes and for a new culture that is focussed on the NFP sector to be established.

An independent regulator can be achieved through a variety of mechanisms, such as the establishment of a new body, or the establishment of a separate and independent statutory office within an existing body. The independence of a separate statutory office would also be ensured as it would report directly to parliament via the Assistant Treasurer. In any of these models an advisory board will help ensure independence and an organisational focus on the NFP sector.

### Findings

A new national NFP regulator would provide the greatest benefits to the public, the sector and governments, in terms of providing a 'one-stop shop' for NFPs, reducing red-tape and simplifying and streamlining reporting arrangements.

However, due to the need for Commonwealth, state and territory cooperation to achieve a national NFP Regulator, this may involve long timeframes before significant reform is delivered for the sector.

In the interim the Commonwealth can establish a NFP regulator for the purposes of Commonwealth regulation.

A NFP regulator established as a separate statutory office within the ATO would provide the greatest benefits, as it would allow for a quick and cost effective establishment of an independent regulator with a new organisational culture, while retaining the sector expertise of the ATO. A separate statutory office would report directly to parliament through the Assistant Treasurer.

## **Recommendations**

40. The Commonwealth should pursue the long-term objective of a single national regulator and regulation for the NFP sector, noting that the Commonwealth does not have the constitutional power to implement this alone.
41. The Australian Government should seek agreement with the states and territories on a single national regulator through COAG.
42. As setting up a national regulator will take time, the Government should improve Commonwealth regulation for the sector in the interim, ensuring that regulatory overlap at a Commonwealth level is removed.

# Chapter 12

## Funding of a national NFP regulator

### Introduction

Most regulated entities in Australia currently incur fees or charges for the cost of regulation.

Currently NFPs pay fees to several different regulators. NFPs regulated by ASIC are required to pay incorporation fees and annual fees. Fees may also be required by state and territory fundraising regulators where NFPs undertake fundraising activities.

NFPs that are incorporated under state and territory legislation also pay regulatory fees. These fees are applicable to incorporated associations for a number of purposes, including incorporation, filing annual returns, modifying an association's rules and inspections of documents kept in the register. The fees vary widely across jurisdictions. For example, incorporation fees in the Northern Territory are \$65, compared to \$161 in South Australia. A number of jurisdictions have also introduced late fees if documents are lodged after the date specified.

### Funding NFP regulators in comparable jurisdictions

Administrative fees are collected from regulated charities and NFPs in several comparable jurisdictions.

#### ***United States***

In the United States applications to the IRS for tax exempt status require a filing fee. This fee is US\$400 for organisations with annual gross receipts of less than US\$10,000 during the preceding four years and US\$850 for organisations with annual gross receipts of US\$10,000 or more during the preceding four years.

In order to determine the level of the fee, the IRS considers the number of cases and the actual time and costs of reviewing applications.

#### ***New Zealand***

Application for registration with the New Zealand Charities Commission is free of charge. However, annual returns must be provided at a cost of NZ\$76.67 for paper based annual returns and NZ\$51.11 for online returns. Charities with a gross annual income below NZ\$10,000 are not required to pay an annual return fee.

#### ***Other***

Regulators of the NFP sector in other jurisdictions, such as England, Wales, Scotland and Ireland do not charge regulatory fees.

## Funding other Australian regulatory regimes

Other Australian regulatory regimes are funded, or partly funded, by the sector that is regulated. For example, the APRA imposes a supervisory levy, on regulated entities such as banks, insurers and superannuation fund trustees. The ATO imposes a regulatory levy on self managed superannuation funds. Additionally NFPs that are regulated by ASIC pay annual fees.

## Funding model options

There are two main options for the funding of the regulator, it could be entirely funded by the Australian Government or alternatively a contribution towards the costs of regulation could be collected from regulated NFP entities. The scope of the regulatory activities may be more limited if funding alternatives are not considered.

Regimes which collect fees or contributions from regulated entities are currently in place both in Australia and overseas.

### ***Option (a) — Fully funded***

The regulator could be fully funded by the Australian Government.

### ***Option (b) — Supervisory co-contribution***

Alternatively, the regulator could be partly funded by a co-contribution from the NFP sector. A small contribution towards regulation of the sector could be collected along with the lodgement of annual reports by regulated NFP entities.

- The supervisory co-contribution could take the form of a small flat fee or could be tiered to reflect entity size and complexity.
  - Small NFP entities, such as those under a minimum gross annual income, could be exempted from paying the regulatory contribution, which would address concerns within the sector regarding the ability of smaller organisations to pay the contribution.
  - The amount of the contribution could be reviewed annually by the Treasurer. Annual review is required as there is currently very little information concerning the character or distributional structure of the sector.
- A differential fee for paper and electronic returns, such as that charged by the New Zealand Charities Commission could also be adopted. However, this may be seen to unfairly discriminate against smaller, less technologically equipped organisations.
- A supervisory co-contribution to a NFP regulator could replace the current fees and charges paid by NFPs to various agencies, such as annual ASIC fees and annual state regulatory fees.
  - Consequently NFPs would incur only one fee under a national NFP regulator. For example, NFP corporations which currently pay an annual fee of \$40 to ASIC would no longer be required to pay that fee.

## Summary of consultation

The responses to the consultation paper highlighted a diversity of views within the sector in relation to the best model for the funding of the NFP regulator. The majority of submissions did not address this issue, indicating that many NFPs did not view this as a key issue for their organisations.

Of the submissions which addressed the issue, a small number supported the co-contribution, a significant number opposed the co-contribution, and the greatest number of submissions that addressed the issue expressed general support for NFPs to contribute to the costs of regulation, provided that the level of the contribution was reasonable and was not unfairly burdensome for new or small NFPs.

Most submissions did not address the structure of a supervisory co-contribution. However, of the responses that did address this question, a clear majority supported a fee structure which allowed for differential treatment for smaller entities. It should be noted that many submissions that expressed reservations about a supervisory co-contribution supported a differential fee structure if a co-contribution is adopted.

Consultation on this matter highlighted the complexity of this issue and the diversity of views within the NFP sector. The large number of responses that expressed qualified views on whether a supervisory co-contribution should be adopted may also indicate that whether a co-contribution is appropriate will be influenced by the form and the broader resourcing considerations of a NFP regulator.

## Issues

In considering whether or not a regulatory co-contribution is appropriate, arguments in relation to user charge systems should be considered. User charge systems can ensure that public goods are efficiently allocated, whereas a free service may be over-utilised. On this issue, the AFTS Report noted that,

*User charging can be an efficient means of financing some government provided goods and services and of rationing individual access to community services.<sup>24</sup>*

It may be appropriate to consider whether a co-contribution is needed to discourage frivolous demands for assessment of charitable or NFP status and to signal to organisations the costs of the resources involved.

The regulatory fees and charges that are currently imposed by ASIC and the state and territory regulators do not appear to cause restrictions for the sector. As these fees could be removed when organisations are regulated by a NFP regulator, there would be no additional burden on the sector.

In order for a regulatory co-contribution to be most efficiently designed, it will be necessary to identify a base for imposing the levy that reflects the cost of regulation and targets the firms creating the need for the regulatory activity. For example, it will need to be considered if it is appropriate to levy the whole sector if only a small group of organisations creates the need for the regulation, and this group cannot be individually charged. In this event, a levy would have few advantages over general taxation.

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<sup>24</sup> 2010 *Review into Australia's Future Tax System*, p325.

The basis for a regulatory co-contribution would also need to be reflected in the structure of a co-contribution. A tiered system based on organisational size and complexity would reflect the resourcing constraints of smaller NFPs. A risk-based approach however may also be appropriate for the sector. This could take into consideration the risks posed by NFPs of different size and complexity. It would also need to consider the different risks posed by member-based NFPs and the accountability of these organisations to their members in comparison to charities and the accountability of these organisations to their donors.

The cost and complexity of collecting a supervisory co-contribution may be a factor which would count against collecting a co-contribution.

A co-contribution may also reflect the method of lodgement of the reports by NFPs. For example, New Zealand charges higher fees for the paper lodgement of reports. A structure such as this may be seen to unfairly discriminate against small NFP entities with limited resources. This may change over time as lodgement is increasingly electronic. In the long term, a goal of electronic lodgement for all NFPs could be achieved.

### **Recommendations**

43. The Government should consider whether or not to collect a supervisory co-contribution, as NFP entities are brought within the new regulatory framework and once it is possible to replace existing fees.
44. If a supervisory co-contribution is adopted, it should be tiered to reflect the resourcing constraints of smaller NFP entities.

## Appendix A — International regulatory models

### NFP regulation in England and Wales

The Charity Commission is the independent regulator of charities in England and Wales. It is a body corporate managed by an executive board. Its role is to provide advice and guidance to registered charities, ensure that they are accountable and meet their legal obligations, and to identify and investigate abuse and mismanagement through compliance activities.

Once a charity is registered it can make an application to HM Revenue and Customs (HMRC) for recognition as a charity for tax purposes.

- A recognised charity may qualify for a number of tax exemptions and reliefs on income and gains and on profits for some activities.
- Charities and community amateur sports associations can also benefit from the gift aid scheme.

Like all organisations, charities are subject to the laws of England and Wales and may be regulated by other government bodies. For companies, the law of England and Wales will normally apply if the company itself is registered in England and Wales.

Charitable organisations that have an income of more than £5,000 must register with the Commission.

- If an organisation's income does not exceed £5,000 it is not mandatory to register as a charity with the Commission. It can, however, register as a charity with HMRC for tax purposes only. However, many choose to be regulated as this increases public confidence in them.

The information a charity is required to prepare or send to the Charities Commission (as well as audit requirements) is determined by whether the charity is incorporated or not and its annual income. In general, charities with an income over £10,000 must submit an annual return to the Commission with the charity's accounts and annual reports. If a charity's income is £10,000 or less, the charity must prepare accounts and advise of changes to the charity's details including income and expenditure each year.

The Commission maintains an online register of charities which records details of registered charities in England and Wales with information provided from the annual return or update.

- The register provides information about the activities and finances of each charity. It shows details of trustees and whether they have complied with their reporting and accounting responsibilities.
- The entries for larger charities with income in excess of £500,000 include a financial profile. The register is maintained from information provided by charities in their annual return or update.

Guidestar UK also provides information on charities in England and Wales and contains a search engine. Charities can edit and add to their entries online. The Charities Commission provides Guidestar with existing public data on charities as well as electronic copies of annual reports and accounts. The resource is free to charities and users.

## NFP regulation in Northern Ireland

The Charity Commission for Northern Ireland was created under the Charities Act (Northern Ireland) 2008 and is the new independent regulator of charities in Northern Ireland. It has a board comprising a chief commissioner, a deputy chief commissioner and up to five charity commissioners, all on a part-time basis.

Before the introduction of the new charity legislation, there was no local registration of charities and only limited control of how charities were run. Usually charities had applied to HMRC for tax benefits and received a reference number.

The general functions of the Commission are to:

- determine whether institutions are or are not charities;
- identify and investigate apparent misconduct or mismanagement in the administration of charities and take remedial action;
- encourage and facilitate the better administration of charities;
- determine whether public collection certificates should be issued;
- obtain, evaluate and disseminate information in connection with the performance of any of the Commission's functions or meeting any of its objectives (including the establishment and maintenance of an up-to-date register of charities); and
- give information or advice, or make proposals, on matters relating to any of the Commission's functions or its objectives.

## NFP regulation in Scotland

The Office of the Scottish Charity Regulator (OSCR), established under the Charities and Trustee Investment (Scotland) Act 2005, is the independent regulator and registrar of charities in Scotland. There is no fee for registration of a charity.

An organisation registered with OSCR can make an application to HMRC for recognition as a charity for tax purposes.

Charities also have to comply with other relevant legislation, for example charitable companies must also comply with company law.

The roles of the OSCR are to:

- determine whether bodies are charitable;
- keep a public register of charities (the Scottish Charity Register) and review these entries;

- encourage, facilitate and monitor compliance by charities;
- identify and investigate misconduct of charities and take remedial action; and
- give information and advice or make proposals to Scottish ministers of matters relating to OSCR's functions.

The OSCR publishes a range of guidance materials to assist charities and their professional advisers to meet their responsibilities under the 2005 Act.

The public register must contain the following information for each charity:

- the name of the charity;
- the principal office or the name and address of one of the charity trustees (unless, it is necessary to protect an individual or the charity's premises);
- the charity's purposes; and
- certain other information (including whether it is a designated religious charity or national collector).

Registered charities must provide the OSCR with certain annual information about the way in which they operate and how they use their resources. Charities are required to submit:

- an annual return;
- a supplementary monitoring return (for charities with a gross income of £25,000 or more); and
- a signed copy of annual accounts.

Most charities can prepare simple accounts but where their gross income is £100,000 or more, or the charity is a company, it must prepare more detailed accounts.

## NFP regulation in New Zealand

The New Zealand charities regulator is the Charities Commission which was established by the *Charities Act 2005*. It is an Autonomous Crown Entity (ACE) which came into existence on 1 July 2005.

- Autonomous Crown Entities are established by, or under, an Act and must have regard to government policy when directed by the responsible Minister.

The role of the Commission is to:

- receive and process applications for registration as charitable entities and monitor entities to ensure they continue to be qualified for registration;
- educate and assist charities in relation to matters of good governance and management;
- maintain and compile a public register of charities;

- receive and process annual returns submitted by charitable entities;
- supply information and documents in appropriate circumstances for the purposes of the Inland Revenue Acts;
- inquire into charitable entities which may have breached the requirements of a charitable entity; and
- consider and make recommendations and carry out research on any matter relating to charities.

Registering with the Commission is voluntary. A charity that chooses not to register can still call itself a charity and solicit funds from the public. However, it is not eligible for tax concessions.

In many cases, these organisations also have to comply with other legal requirements relating to their rules. This will be the case if they are registered under the *Incorporated Societies Act 1908*, the *Charitable Trusts Act 1957* or the *Companies Act 1993*.

Application for registration is free of charge. However charities are to furnish an annual return each year at a cost of NZ\$76.67 for paper based annual returns and NZ\$51.11 for online returns. Charities with a gross annual income below NZ\$10,000 do not pay an annual return fee.

Inland Revenue New Zealand administers charitable tax exemptions. Generally, registration by the Commission is accepted by Inland Revenue so that registration will, in most cases, lead to tax exemption. Inland Revenue continues to administer donee status. Organisations do not need to be registered with the Commission to get donee status. Individuals can claim a tax rebate for a donation they make to an organisation that has donee status.

The charities register includes the following information:

- the name, address and registration number of the charity;
- names of all past and present officers since the organisation was first registered;
- a copy of its rules;
- the application for registration as a charitable entity (including all accompanying information and documents); and
- annual returns.

Charitable organisations are required to notify the Commission if certain core information has changed during the year. This ensures that all information that is held on the charities register is as up to date as possible.

## NFP regulation in Ireland

In Ireland, the Charities Act of 2009 establishes a Charities Regulatory Authority with the aim of securing compliance by charities with their legal obligations and to encourage better administration of charities.

The establishment of the Authority means that functions will be transferred from other institutions to the Authority such as functions of the Attorney-General that relate to charities. The Act has commenced with individual provisions.

The intention of the Act is that an integrated system of mandatory registration and proportionate regulation and supervision of the charities sector will be introduced for the first time in Ireland.

The Authority's role will principally be to increase public confidence in the charities sector through effective oversight, promotion of compliance, better administration and providing guidance to charitable organisations.

The Act provides for a register of charities on which all charities operating in the jurisdiction must be entered and that will be accessible to the general public.

The Revenue Commissioners alone determine whether a body is entitled to charitable tax exemption under the Taxes Consolidation Act 1997. Any organisation in receipt of charitable tax exemptions from the Revenue Commissioners on the establishment day is to be automatically deemed to be registered with the Authority.

The Act provides for proportionate regulation in recognition that many charitable organisations are small with limited resources. There are varying reporting and audit requirements depending on whether a charity's income or expenditure is above or below a prescribed level.

All charitable organisations will be required to make annual reports on their activities to the Authority which will generally be accessible to the public.

### NFP regulation in the United States

In the US, all federal and state laws pertain, directly or indirectly, to tax-exempt organisations. Most of the laws that pertain to the concept and creation of these organisations originate at the state level, while most laws concerning tax exemption are generated at the federal level.

- Federal tax-exempt status does not guarantee exemption from state and local taxes and vice versa.

At the federal level, the IRS is responsible for the administration of tax-exempt organisations.

- Charitable organisations are eligible to attract deductible charitable contributions (but not including charitable organisations that test for public safety).

The role of the IRS is to consider whether an organisation meets the requirements for tax exemption, assist tax-exempt organisations with their tax law responsibilities and improve compliance.

To obtain tax-exempt status an organisation must apply for recognition for exemption. The application must be accompanied by a user fee (currently US\$400 which increases to US\$850 if the gross receipts for the organisation are expected to average US\$10,000 or more over the preceding four years).

- Churches and public charities whose gross receipts are not more than US\$5,000 are exempt from this requirement.

Most tax-exempt organisations (other than churches) must file a yearly return or notice and a tax return where there is unrelated business income exceeding US\$1,000 with the IRS. Since 2008, small tax-exempt organisations (annual gross receipts of US\$25,000 or less) are required to lodge an e-postcard to the IRS.

In general, a tax-exempt organisation must make available for public inspection and on request its exemption application with all supporting documents and its annual information return and annual returns. The IRS must also make this same information available to the general public.

- Charitable organisations must also make available its annual business income returns for public inspection which includes disclosure of unrelated business income.
- GuideStar is also a source of information about US NFPs.

## NFP regulation in Canada

In Canada, like Australia, the laws relating to charities are primarily the responsibility of sub-national governments, while income tax laws are generally the responsibility of the national government. The national government's control over charities is mostly achieved through provisions relating to taxation.

The CRA is Canada's federal agency responsible for administering the Income Tax Act (the Act). The Charities Directorate of the CRA, is responsible for administering the Act in relation to registered charities and certain other 'qualified donees.'

The role of the Charities Directorate is to review applications for registration, provide guidance on maintaining registered status, ensure registered organisations comply with registration requirements, develop policy; and provide information and education programs for the charitable sector and for donors.

Registered charities are required to file an annual information return with the CRA and must meet certain requirements of the Act concerning their expenditures and activities. The CRA maintains a list of charities where the following information is publicly available:

- whether a charity is registered under the tax legislation and is therefore eligible to issue official donation receipts for income tax purposes;
- a charity's information return;
- a charity's financial information (assets, liabilities, income, and expenditures);
- the activities of a registered charity; and
- how to contact a charity.

Within the federal government, there are other government agencies with a regulatory role for specialised entities, for example, Industry Canada which has responsibility for federal incorporation.

The regulation of charities outside income tax is constitutionally under the jurisdiction of the provinces and territories. The responsibility of provincial and territorial governments relates to fundraising, corporation registry, gaming and lotteries, and other activities.

In 2009, the Canadian Government enacted the Not-for-Profit Corporations Act 2009 which aims to promote accountability, transparency and good corporate governance for the NFP sector in the same way as the for-profit sector.

A NFP organisation is broadly a club, society or association that is not a charity and is organised and operates exclusively for social welfare, civic improvement, pleasure or recreation or for any other purpose except profit.

Even though most of these organisations are exempt from income tax, they are still required to complete an income tax return each year to the CRA. Some NFP organisations may be required to pay tax on income from property.



## Public submissions received:

Aged and Community Services  
Alan R Ovenden  
Alcohol and other Drugs Council of Australia  
Anglican Church Diocese of Sydney  
Anglicare Australia  
Anglicare Diocese of Sydney  
Artsource WA  
Association of Independent Schools of Western Australia  
Association of Mining and Exploration Companies  
Asthma Australia  
Asylum Seeker Resource Centre  
ATNS University of Melbourne  
Australasian Compliance Institute  
Australasian Society for HIV Medicine  
Australia Council  
Australian Accounting Standards Board  
Australian Baha'I Community  
Australian Catholic Bishops Conference  
Australian Catholic University  
Australian Catholic University Public Policy Institute  
Australian Chamber of Commerce and Industry  
Australian Community Support Organisation  
Australian Conservation Foundation  
Australian Council of Social Services  
Australian Environment Grantmakers Network  
Australian Friendly Societies Pharmacies Association  
Australian General Practice Network  
Australian Hotels Association  
Australian Institute of Company Directors  
Australian Lawyers for Human Rights  
Australian Major Performing Arts Group  
Australian Medical Council Limited  
Australian Neighbourhood Houses & Centres Association  
Australian Racing Board  
Australian Red Cross  
Australian Society for Association Executives  
Australian Sports Commission

## Final Report: Scoping study for a national not-for-profit regulator

Baptistcare  
Beyond Blue  
Blake Dawson  
Boystown  
Cancer Council Australia  
Cancer Council of Queensland  
Cat Protection Society of NSW  
Cerebral Palsy League  
Chamber of Arts and Culture WA  
Chamber of Commerce and Industry WA  
Changemakers Australia  
Chartered Secretaries Australia  
Church of Scientology  
Church of Scientology — Canberra  
Colin Ball  
Commonwealth Ombudsman  
Community Compass Inc  
Community Council for Australia  
Community Employers WA  
Community Southwest  
Complementary Medicine Association  
Consumers Health Forum  
CPA Australia  
CPA Australia Third Age Network Committee  
Curtin University  
David Morrison and Maria Nicolae  
Dietitians Association of Australia  
Dr Matthew Turnour  
Epilepsy ACT  
Evelyn O'Loughlin  
Every Day Hero  
Family Care  
Federation of Ethnic Communities' Council of Australia  
Financial Ombudsman Service Limited  
Foley, Joe  
Fundraising Institute Australia  
GAAP Consulting  
Global Philanthropic  
Good Beginnings Australia  
Grant Thornton  
Griffiths, David R  
Health Insurance Restricted Membership Association of Australia

Holman Webb  
Human Rights & Responsibilities Australia  
Independent Schools Council of Australia  
Institute of Chartered Accountants  
John Church  
Legacy  
Life Without Barriers  
Live Performance Australia  
Markwell, Andrew  
Masonic Homes Ltd  
Master Builders Association  
McCullough Robertson  
McGrath Foundation  
Meals on Wheels  
Melbourne Community Foundation  
Melbourne Fringe  
Mission Australia  
Monash University  
Moore Stephens Accountants & Advisors  
Moores Legal  
Murdoch Childrens Research Institute  
Myer Family Company  
National Institute of Accountants  
National Pro Bono Resource Centre  
National Roundtable of Nonprofit Organisations  
NF Australia  
North Queensland Land Council  
Not-for-profit project University of Melbourne Law School  
NTSCORP  
Optimum NFP  
Oxley, John  
Parkinson's Australia  
Peninsula Community Legal Centre  
Performance Partners  
Pharmaceutical Society of Australia  
Philanthropy Australia  
Physical Disability Australia  
PilchConnect  
Presbyterian Church NSW  
Pricewaterhouse Coopers  
Prolegis Lawyers  
Prudential Partners Chartered Accountants

## Final Report: Scoping study for a national not-for-profit regulator

Queensland Councils for Parents and Citizens' Associations

Queensland University of Technology

Rotary Australia World Community Service

Rowing Australia

Royal Australasian College of Physicians

Royal Automobile Club of WA

Royal College of Pathologists Australasia

Royal Flying Doctor Service

RSPCA Australia

Sei Kato

Social Traders

Southern Youth and Family Services

St John Ambulance Australia

St Vincent de Paul Society

Surf Life Saving Australia

Tasmanian Government

The Benevolent Society

Trustee Corporations of Australia

Uniting Care NSW & ACT

Uniting Church in Australia

UnitingCare Australia

Vicsport

Victorian Council of Social Service

Victorian Government

Vincent Fairfax Family Foundation

Vision Australia

Volunteering Australia

WA Peaks Forum

Wanslea

Wesley Mission

White Lion Inc

Wilk, Jason

World Vision Australia

Wright, Robert

YMCA Australia