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Tuesday, 3 November 2009

Simplifying disclosure regimes for charities and not-for-profits

The Productivity Commission has released its draft Research Report which examines, amongst other things, the introduction of a single legal entity, a national regulator for not-for-profit organisations, and national fundraising legislation.

The Senate Standing Committee on Economics made 15 separate recommendations in its December 2008 report on how the disclosure regimes for charities and not-for-profit organisations could be improved upon. Disappointingly, the Commonwealth Government's response was surprisingly brief. With a number of the recommendations put forward by the Senate Standing Committee, the Commonwealth Government responded by advising that the issues raised in the particular recommendation would be investigated by the Productivity Commission. The Productivity Commission finally issued its draft Research Report in October 2009, inviting written comments on that draft Report by 24 November 2009.

We have previously written on the legal issues arising from the report prepared by the Senate Standing Committee in December 2008. Our comments can be found in our December 2008 issue of *Balancing Act*. In particular, we commented on three specific legal issues, being the introduction of a single legal entity, the creation of a national regulator for not-for-profit organisations and the introduction of national fundraising legislation.



MAKINSON & d'APICE
LAWYERS

Level 12 135 King Street Sydney NSW 2000 • GPO Box 495 Sydney 2001 • DX 296 Sydney
Telephone 02 9233 7788 • Facsimile 02 9233 1550 • Email mail@makdap.com.au • www.makdap.com.au

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All three of these legal issues are discussed at length in the draft Research Report prepared by the Productivity Commission. This Bulletin will discuss how each of these three issues has been treated by the draft Research Report.

General Introduction

By way of a general introduction to the draft Research Report, the writer found the report to be highly informative with interesting data and helpful explanations as to the current state of the confusing non-profit sector in Australia. The writer highly advises any person interested in the issues facing the non-profit sector in Australia to read the report.

Not surprisingly, the draft Research Report found that the current regulatory architecture does not serve the non-profit sector well and that, consequentially, reforms are necessary. As mentioned, this Bulletin focuses on the legal issues facing the non-profit sector, and those are discussed by the Report in the second of three different sections in the Report. More specifically, these issues are discussed in Chapter 6 of the Report. (Chapter 7, however, is also extremely interesting. It studies the various tax concessions available to the not-for-profit sector and whether or not they require any revision. The Report states that it is widely acknowledged by governments and the sector that the current eligibility requirements and endorsement processes for organisations to access tax concessions are complex, inefficient and inequitable. Of particular interest is the recommendation by the Report that relocating the endorsement process to a national

registration body – such as a national regulator – may increase the transparency of the process and reduce any perceived bias. It is argued that there should also be an appeal process for not-for-profit organisations which have been denied DGR status, and for the Australian Taxation Office (**ATO**) where the ATO believes that an organisation should not have been granted DGR status. Chapter 7 also analyses how changing tax incentives could impact upon philanthropy as a whole in Australia.)

1. Single Legal Entity

The Senate Standing Committee on Economics last year recommended that all not-for-profit organisations should use the same legal structure in order to ensure more solid regulation of the sector. This would have resulted in all existing organisations migrating to the new structure once it had been developed. The Committee also recommended that this legal structure should be compulsory for all organisations.



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The draft Research Report by the Productivity Commission states that this idea of a new single legal form continues to find support, and that such a legal form could cover different sized agencies through layered reporting and other requirements. The Commission, however, acknowledges that the attractiveness of a single legal form depends crucially on the degree of complexity and burden imposed by such a structure relative to the burden it relieves, and concedes that there could be simpler alternatives. The Productivity Commission acknowledges that some have argued that the current forms are adequate, and that it is the administration that is the issue. Further, a new form replacing existing structures would create legal uncertainty and risk. There would also be high transaction costs associated with adopting a new legal form and it would inhibit diversity. The Commission has found, on balance, that although there is merit in the proposal of a single legal entity, it could be argued that a variety of legal forms offer scope for best fit, just as in the “for profit” area where legal forms range from sole traders through to public corporations. The Commission also concedes that the transition costs in moving all not-for-profit organisations to a single legal entity would be significant.

The Commission has found that the problem of inappropriate legal form could be mitigated if not-for-profit organisations were able to easily migrate to a more appropriate form. There was also the issue faced by not-for-profits which operate across State boundaries. For these not-for-profit organisations, it is the inconsistencies between similar legal forms and the

costs of complying with different legislation that causes the greatest amount of concern.

After studying various alternatives, the Commission has found that there is a case for the Commonwealth Government to offer, but not mandate, an alternative incorporated association framework to aid not-for-profit organisations operating across State boundaries. This alternative incorporated association could be based on best practice State law; allow for tiered reporting requirements; and also accommodate any not-for-profit organisations, particularly those aspiring to operate in more than one jurisdiction. Some participants suggested that State/Territory incorporation responsibility should be restricted to smaller agencies, perhaps those with annual revenues below \$150,000. The Commission is seeking further input on this particular proposition.

Notwithstanding the possibility of creating an alternative incorporated association that could operate nationally, most State/Territory based associations incorporation laws needed to be amended to allow easier migration from one legal form to another and from one jurisdiction to another. The Commission recognises a greater regulatory consistency across jurisdictions is also likely to provide benefits.

Chapter 6 proceeds to discuss the reporting requirements for not-for-profit organisations. It recognises that there are significant inconsistencies in reporting and other requirements imposed in different States and Territories pursuant to the very different associations incorporation laws operating in each

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jurisdiction. This is therefore a compelling argument for reform of accounting and reporting requirements. The Commission admits that there is scope for increased consistency amongst the jurisdictions as to both disclosure requirements (based on size) and the enforcement of financial reporting regulations. The Commission considers that the application of a Standard Business Reporting Initiative and the national adoption of a Standard Chart of Accounts to NFP financial reporting will assist in achieving this goal. The Standard Chart of Accounts has already been adopted by government agencies in Queensland, New South Wales and Western Australia, and is currently awaiting sign-off in Victoria.

The Report discusses that there is scope to develop a national portal for key corporate financial data for both public and government access. Not-for-profit organisations that are incorporated at a federal level could be required to lodge this information once only, and this information could then be accessed for multiple purposes. Other not-for-profits which are not incorporated at federal level could also lodge such information. Eventually, this sort of portal could link to State-based information systems. The Commission is of the opinion that the principle of “*report once, use often*” could be entrenched in this sort of process and would be consistent with the direction of the Standard Business Reporting Initiative.



2. National Fundraising Legislation

The December 2008 report by the Senate Standing Committee on Economics recommended that national legislation be introduced governing fundraising in Australia. Although this recommendation was highly supported, it faced the inherent difficulty of arranging for the States and Territories to refer their powers in this regard to the Commonwealth, which is never a simple and expeditious task, and usually takes some years.

The Commission also agrees that a nationally consistent approach to fundraising would resolve the regulatory burden faced by non-profit organisations operating across the jurisdictions, and would deliver net benefits to the community. Apparently this issue is already being investigated and is being progressed by the Council of Australian Governments (**COAG**). A number of approaches and combination of approaches are possible to achieve this, including:

- mutual recognition;
- harmonisation of existing State and Territory legislation or the introduction of new harmonised legislation; and

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- national legislation.

Of these three options, the Productivity Commission favours the harmonisation of existing State and Territory legislation as the most appropriate solution. Mutual recognition would possibly result in some “*forum shopping*”, whereby fundraisers would register in that jurisdiction with the least onerous requirements for those regulations affecting them. With regard to national legislation, whilst the Commission is attracted to this idea, it is reluctant to recommend this at present. This is due to the fact that States would be understandably reluctant to cede this power to the Commonwealth without knowing what form that legislation might take. Therefore, the Commission suggests that Commonwealth, State and Territory governments proceed to a nationally consistent approach to fundraising in a staged manner. This would involve:

- a first stage where the States and Territories developed harmonised fundraising legislation under the existing COAG initiative;
- a second stage where the States and Territories would mutually recognise (in conjunction with the Commonwealth) the fundraising approval granted in other jurisdictions; and
- a final stage where if sufficient confidence in the new fundraising regime was engendered, the States and Territories could consider referring their powers to the Commonwealth so that a national fundraising law could be enacted based on the harmonised legislation agreed by the State and

Territory governments, and regulated by the proposed national registrar.

The harmonised legislation should include the following features according to the Commission:

- a complete definition of fundraising activities;
- it should apply to all organisations undertaking fundraising activities;
- reporting requirements should be commensurate with the size of the organisation and the amount being raised; and
- the legislation should encompass contemporary fundraising activities such as Internet fundraising or interactive television.

This harmonisation option is already being investigated by the COAG as part of its Business Regulation and Competition Working Groups 2009 Work Plan.

3. Regulator for Not-for-Profit Organisations

The draft Research Report discusses the various problems and difficulties arising out of the current system of determining charitable and other tax concessional statuses. There are a multitude of agencies involved in determining concessional tax statuses of not-for-profit organisations at the Commonwealth, State and Territory government level. In 2007, the National Roundtable of Non-Profit Organisations found that some 19 Commonwealth, State and Territory government entities are regularly involved in determining the charitable status of

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organisations, and a further 74 entities may be called on to make such determinations. The Productivity Commission considers therefore that, at a minimum, endorsement for Commonwealth tax concessions should be undertaken by a single Commonwealth organisation outside of the ATO. States and Territories would recognise those endorsements. The Commission does concede, however, that State and Territories would be free to determine the nature and extent of any taxation concessions applicable to non-profit organisations holding a particular taxation status in their jurisdictions.

To facilitate the implementation of all of the “*legal*” recommendations being made by the Productivity Commission, the Commission is proposing a new Commonwealth organisation, such as the Registrar for Charitable and Community Purpose Organisations, to be the “*one-stop-shop*” for non-profit organisations for the consolidation of all Commonwealth regulatory arrangements. This would apparently offer non-profit organisations the advantage of:

- a one-stop-shop for tax endorsements;
- distribution of corporate financial information;
- possibly also registration for national fundraising activities;
- registering and regulating Commonwealth incorporated associations (being the new legal entity being proposed by the Productivity Commission), companies limited by guarantee and indigenous corporations;
- promoting confidence and informed participation in the non-profit sector through appropriate education and complaints handling.

This national registrar could be a separate agency under the *Financial Management and Accountability Act* 1997, or it could be an additional function required of ASIC. The Commission is welcoming participants’ views on which would be preferable.

Next Steps

The draft Research Report prepared by the Productivity Commission is, in the writer’s opinion, a more practical and palatable approach to addressing the many regulatory issues being faced by the non-profit sector. The writer highly encourages all participants in the sector to prepare and lodge a submission by 24 November 2009 in relation to these legal issues and any other issues raised in the Report. This is a unique opportunity for the non-profit sector in Australia to both drive and participate in the much needed reform of the third sector. ■