

## **Report on the Implementation of the Government's Charities and Not-for-Profit Sector Reform**

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Canberra, April 2012

### **Objective of the Report**

The objective of this report is to help our clients understand:

- The broad aims of the Australian Government's Reform Agenda for the Not-for-Profit Sector.
- What the Office of the Not-for-Profit Sector and the Australian Charities and Not-For-Profit Commission plan to do in the early stages of their implementation of the Reform Agenda.
- What the import of this might be for our clients.

### **Sources**

This Report is based on publicly available information on the various web sites quoted, plus conversations with senior officials.

## Executive Summary

1. Improving the quality of governance in the Charities and Not-for-Profit (NFP) sector is badly needed and long overdue. The Australian Government has now moved to do that with its Charities and NFP Sector Reform Agenda.
2. The intent of the Reform Agenda is to establish a separate regulatory regime for the sector that is very different in its culture and relationship from the regulators that have gone before it.
3. The basic orientation is to establish a co-operative relationship between the regulator and the charities and NFPs subject to it that encourages the practice of good governance by NFPs, because that is in the best interests of their members and their objectives of providing service.
4. In establishing the Australian Charities and Not-for Profits Commission (ACNC) as a “one stop shop” regulator for the sector, separate and parallel to the Australian Securities and Investment Commission (ASIC), careful attention is being given to attune it to the needs and working realities of organisations in the sector.
5. Included in this is a role to educate and support. Careful attention is being given to being helpful and to avoid being coercive.
6. **We are most impressed at the innovative way an open and practical culture is being deliberately created by recruiting people with serious career experience in the NFP sector and key people from similar overseas regulators to form the initial staff of the ACNC.**
7. **In all our forty years’ involvement with the Australian Government, we have never seen such a creative approach to establishing a new regulatory authority.**
8. The need for significant reform has been recognised for a long period of time:
  - By two Productivity Commission reports spanning sixteen years;
  - From widespread experience from across the governance community; and
  - By our own experience as volunteers and consultants;
  - As well as from input from many colleagues

All the above point to an acceptably low standard of governance prevalent within the sector.

9. There are no effective internal governance disciplines on the NFP sector to encourage it to be cost effective. In contrast to the disciplines of the profit motive, shareholdings and regulatory oversight in the corporate sector and the budgetary constraints and accountability provisions of the Parliament and government in the public sector, the NFP sector is driven by a high sense of noble purpose and emotional commitment that too often rejects attention to the practice of good governance as a distraction.
10. The NFP sector is a largely unregulated market. Neither the state/territory authorities, which register incorporated associations, nor ASIC, which is responsible for companies limited by guarantee, provide a level of compliance management that is any way near commensurate with the economic weight of entities in the NFP sector.
11. Establishment of new regulatory structures, with adequate resources, is therefore appropriate and overdue in the best interests of the members and investors in Charities and NFP sector, which is a serious part of the Australian economy.
12. There is an urgent need for stronger imperatives to drive greater rigour in the governance practices of the majority of NFPs.
13. Attitudinal change among leaders in the NFP sector to adopt greater rigour in the way they govern themselves is essential, because this is the best way to serve the interests of their members and to achieve the service objectives of their organisation.
14. **Our assessment is that the Government's initiative for Not-for-Profit Sector Reform will bring long overdue and effective change to the governance landscape of the sector for the better.**
15. **Our assessment is that the timeframe for the NFP Reform initiative of:**
  - **establishment of the ACNC as a "one stop shop" regulator for the sector, separate from and parallel to the Australian Securities and Investment Commission (ASIC); now deferred to 1 October 2012 to allow for longer consultation;**
  - **establishment of the Public Information Portal by 1 July 2012 ; and**
  - **the statutory definition of a "Charity" by 1 July 2013****is realistic and achievable.**
16. The reform initiative is being developed incrementally. The first stage of the work to mid 2014 will engage those 56,000 NFPs which claim status as a "charity" and seek exemption from income and other taxes in consequence. This includes the (entirely reasonable) objective of placing greater discipline on the administration of NFP income that is exempt from tax.

17. For the first tranche of organisations required to be registered with the new regulator, change will be forced by the external imperative of greater visibility about their performance provided by the Public Information Portal. This will drive a heightened importance to serving their member's interests well in a highly competitive environment for philanthropic funding.
18. For the first time, donors and volunteers will have information about the performance of various charities and NFPs that will allow them to judge which they wish to support and which they do not.
19. For private schools, this will add to the information already available on the "My School" web site and create even greater transparency and pressure to operate at the level of best governance practice.
20. Decisions have yet to be made about how to deal with more effective regulation of other bodies in the NFP sector such as industry bodies, professional organisations, issue-related lobby groups, service clubs, private schools and the like. Most of these bodies are already incorporated as associations under state/territory jurisdiction, or as companies limited by guarantee under the *Corporations Act (C'wealth)*, 2001 and presently regulated by ASIC. It has yet to be decided when/whether companies limited by guarantee will be transferred from ASIC to the ACNC.
21. However, there is no reason why Directors and Board teams of NFPs not immediately included in the first tranche of participants should not give attention to their quality of governance for the good of their members. We note that "opt-in" provisions for NFPs in this category are being considered in the design of the Public Information Portal.

## Report

### Section 1. The Government's Reform Agenda

#### Situation

The three broad aims of the Government's stated reform agenda are to:

1. Improve the way government and the NFP sector work together, through
  - the National Compact
  - streamlined funding arrangements; and
  - reduction of red tape.
2. Streamline and simplify regulation by
  - establishing the Australian Charities and Not-for Profit Commission (ACNC); and
  - tax reform.
3. Promote long-term sustainability of the NFP sector by assisting with
  - workforce planning;
  - measurement of the sector;
  - a national volunteering strategy; and
  - social investment and philanthropy.

The initiative is set in the context of the Australian economy where the NFP sector:

- consists of around 600,000 organisations (of which AICD estimates possibly 200,000 are substantial enough to be worth regulating);

- involves over 6 million Australians, who volunteer for service to the community each year with a wage equivalent of \$ 15 billion;
- makes a contribution of more than \$14.6 billion to the Australian economy, by donations and in kind, which relates to national productivity and constitutes a saving to the public purse;
- employs about 8 % of the national workforce; and
- contributes \$43 billion to Australia's GDP.

Review of this substantial part of the Australian economy and our community was last undertaken in the 2010 - Productivity Commission Research Report, *Contribution of the Not-for-Profit Sector*. This followed up on the findings of the 1995 - Industry Commission Inquiry Report, *Charitable Organisations in Australia*.

Other work by the Productivity Commission and in Treasury in the interim has focussed on the definitional issues of "charity".

For the Government's recent starting point in focussing on how best to support the organisations and people who volunteer and operate in the sector, see the *Final Report of the Scoping Study for a National Not-for-Profit Regulator*, which highlighted the concerns of the NFP sector about duplicative, burdensome and unclear governance requirements across all Australian jurisdictions. The report also made several recommendations concerning governance arrangements applying to the sector. See the Treasury website [www.treasury.gov.au](http://www.treasury.gov.au).

For the orientation of the Government's reform pathway, see *Consultation Paper - Review of Not-For-Profit Governance Arrangements* at [http://www.treasury.gov.au/content/not\\_for\\_profit.asp?ContentID=2188](http://www.treasury.gov.au/content/not_for_profit.asp?ContentID=2188)

### Analysis of the Reform Agenda

Although a proportion of NFPs is managed efficiently within their limited budgets and skill sets, the sector as a whole is renowned for inadequate attention to its governance practices. There are no effective internal imperatives in the NFP sector to be cost effective.

In contrast to the disciplines of the profit motive, shareholdings and regulatory oversight in the corporate sector and the budgetary constraints and accountability provisions of the Parliament and government in the public sector, the NFP sector is driven by a high sense of noble purpose and emotional commitment that too often rejects attention to the practice of good governance as a distraction.

Poor knowledge about governance, along with complacency (even active rejection of the practice of good governance), is endemic in the sector. The claim that

*“... we’re not BHP, we’re not Telstra - we’re a grass roots voluntary organisation - we don’t need to waste our time with that kind of stuff”*

remains all too familiar.

The result is often a significant waste of time and effort of employed staff as well as volunteers, together with a squandering of resources donated by the public and time invested by volunteers.

The NFP sector is a largely unregulated market. Neither the state/territory authorities, which register incorporated associations, nor ASIC, which is responsible for companies limited by guarantee, provide a level of compliance management that is any way near commensurate with the economic weight of entities in the NFP sector.

ASIC’s administrative processes are too bureaucratic and rigid for the effective regulation of NFPs.

Competition for funding brings some reality check to larger Charities and NFPs and the scrutiny of professional advisors does have some effect on the choices of larger benefactors, but below the top echelon of charities there is little direct causal link made between the performance of boards and their managements and the performance of their organisations.

There is the widespread view that those who engage in the governance of the sector do so for noble reasons. It therefore is too often assumed that their actions are not only noble, but also unquestioningly efficient.

While performance management does appear to be practised, variously, at the level of upper management across the sector— reflecting the general trends of management practice - there is little evidence of performance evaluation at the board level that might be a substitute for the lack of other governance discipline.

The investment that people make at all levels throughout the sector is characterised by a high level of emotional commitment. While this is exemplary and creates great energy for the cause, it is not well counterbalanced by an offsetting discipline of evaluating how well the leaders in the sector work together in governing their entities. Investment in applying the practice of good governance is not generally regarded as a high priority in the sector.

Broadly, the legal status by which the many bodies in the NFP sector are established is provided by an uncoordinated matrix of provisions, including:

- Incorporated associations – state/territory legislation;
- companies limited by guarantee under the *Corporations Act (Aust), 2001*;
- industrial representatives under *Fair Work Act (Aust), 2009*.

There is a widely held need for:

- an external imperative to encourage more rigorous attention by NFP Boards / Committees about how to work effectively in the use of the resources that are contributed to them by such a large proportion of the Australian population.;
- greater transparency about the resources that are tied up in the sector and how efficiently they are used by individual NFPs, including by some form of benchmarking; and
- harmonisation and simplification of the existing regulatory provisions for the sector, which are covered, variously by state/territory as well as national legislation.

The policy drivers of the Government's NFP reform initiative appear to be relevant, timely and in the interests of the NFP sector bodies and their members.

## Section 2. A Contrary View about the Quality of Governance in the Sector

### Situation

The *Directors Social Impact Study 2011* was conducted by the Centre for Social Impact on behalf of the Australian Institute for Company Directors (AICD) and its partner in this project, the Commonwealth Bank of Australia.

It attracted 1,912 respondents across Australia, all of whom were AICD members, and is the expansion of the inaugural *Directors Social Impact Study*, released in 2010.

The *Company Director* article reporting the outcomes notes:

“Study respondents were found to have extensive involvement in the NFP sector. Indeed, 58 per cent currently served on NFP boards and half of those held multiple directorships. Together, they sat on 1,996 NFP boards ...”



*Company Director* bridled at the widespread view that the NFP sector has failed to keep pace with the evolution of good governance. It claimed "... this view is not shared by the *Directors Social Impact Study's* findings that:

"Directors were evenly split in their views when comparing sector governance practices. Half of the respondents with experience in both NFP and for profit organisations felt the quality of governance in NFP organisations was equal to or better than in for profit organisations."

*Company Director* noted that:

"... in many areas, the experience of directors was comparable across both sectors and the evidence suggests that , due to the sheer volume of directors who are now operating across both sectors, an improvement in governance has followed accordingly."

Source: *Company Director*, Volume 27, Issue 09 | October 2011, pp 40 – 42.

#### *Analysis of the Company Director coverage of the Social Impact Study*

Even if the survey were limited to the 200,000 or so Charities and NFPs that AICD regards as worth regulating, the small return to the AICD study from only 1,912 respondents is statistically insignificant as an assurance of the quality of governance across the whole sector.

It is likely that what is happening in the *Directors Social Impact Study* is that the respondents, being interested enough in governance to be members of AICD and to respond to the study, self selected as among the best quality of NFP leaders.

A more logical outcome of the Study is that the best of NFP organisations in the sector are as good as their private sector counterparts, especially those with cross-directorships between the two sectors.

However, although the best of leaders in the sector should be commended, it would-be foolish in the extreme to assume they reflect the attitudes of the bulk of NFPs, who have been studied over a lengthy period of time and are the stuff of widespread anecdotal evidence of bad practice.

The AICD's *Directors Social Impact Study* 2011 does not negate the many assessments about the widespread apathy/disdain for effective attention by NFP boards in their governance practices.

## Section 3. The Architecture of the Reform Arrangements

### Situation

Political leadership of the Reform Agenda involves:

- Prime Minister Julia Gillard MP
- Deputy Prime Minister and Treasurer Wayne Swan MP
- Minister for Employment and Workplace Relations and Minister for Financial Services and Superannuation Bill Shorten MP
- Minister for Social Inclusion Mark Butler MP
- Assistant Treasurer David Bradbury MP

The coordinating authority for the reform agenda is the Office of the Not-for-Profit Sector in PM&C.

Regulation of the sector will be undertaken by the ACNC, which is being established as a separate regulator to ASIC within the Treasury Portfolio.

Residual social inclusion and policy delivery work will remain with FAHSCIA.

Widespread consultation is being undertaken with relevant peak bodies and industry groups, as well as with the states/territories. See the National Compact Map at Attachment 2.

### Analysis of the Architecture of the Reform Arrangements

Although the architecture of the reform arrangements may seem complex to people outside of government, it is normal and appropriate to the span of the required policy and operational work across the three portfolios. It is entirely consistent with the emphasis on integration and coherence of decision-making in the modern Australian Public Service (APS).

The Department of the Prime Minister and Cabinet (PM&C), as the lead co-coordinating body for whole-of government policy work, is well across this task. It is well skilled for the task and is respected for its track record.

Regular contact between the staff of the various agencies involved in the Not-for-Profit Reforms occurs at a range of levels from formal processes to daily contact between officers.

## Section 4. The Office of the Not-for-Profit Sector

### Situation

The Office was established in PM&C in October 2010 to drive and coordinate the not-for-profit sector reform agenda. The Office provides secretariat support to the Not-for-Profit Sector Reform Council and an Interdepartmental Committee on Not-For-Profit Reform.

It is also responsible for some functions that were transferred from the Department of Families, Housing, Community Services and Indigenous Affairs (FaHCSIA), including:

- volunteering policy
- some volunteering program funding (does not include funding for volunteer grants)
- implementation of the National Compact: *working together*.

The Office is led by a Band 1 SES Officer and has two Sections, led by EL2s, comprising:

### *Regulation and Tax*

This Section is responsible for oversight of not-for-profit reform; convening an interdepartmental committee to advance the not-for-profit reforms and coordinate the implementation of the National Compact across government; providing secretariat support to the Not-for-Profit Sector Reform Council and working groups; and coordinating efforts to reduce red tape.

### *Social Investment, Philanthropy and Volunteering*

This Section develops and implements policy that is integrated with not-for-profit sector reform and improves the environment for social investment and philanthropy. The Section is also responsible for the National Volunteering Strategy and its implementation, as well as the International Year of the Volunteer Plus 10 Advisory Group and activities to promote participation in volunteering. This section manages funding provided for volunteer support organisations including Volunteering Australia and state and regional Volunteer Resource Centres.

### Analysis of the Office of the Not-for-Profit Sector

The Office is well resourced for its responsibilities and has been deliberately staffed with people who are deeply knowledgeable about the NFP sector.

It is noted that the Division Head, the Head of the Office, both EL2s and other staff have been recruited from careers in the management of NFPs. It is also noted that several of these staff have had experience of serving on or reporting to NFP Boards.

This has provided the Office with critical insights about the wide range of situations and needs of NFPs and close links with the sector.

The recruiting of this awareness is a very welcome initiative in establishing the policy perspective of the co-ordinating agency.

Beyond its responsibility to “drive and coordinate the not-for-profit sector reform agenda,” there is an important role for the policy co-ordinator to ensure that this significant sector of the Australian economy is included in the debate about improving Australia’s productivity.

Poor performance from the NFP sector must have an impact on Australia’s overall productivity, which has been in decline for some years.

There is a strong case that the productivity of the NFP sector in the employment of its people, resources and capital and in providing services in lieu of what might be provided by other means (private or public) should be included in the emerging policy debate about improving national productivity.

The NFP sector is too important a part of the national economy to be omitted from that debate.

Moreover, inclusion in the national policy debate will assist in helping NFP boards to see the need to improve their productivity, not only for their members, but also for the benefit of the wider community.

## **Not-for Profit Reform Council**

### Situation

The Council was established on 14 December 2010 to help drive sector reform, advise on the implementation of the ACNC, streamlining tendering and contracting processes for government funded NFPs, a nationally consistent approach to fundraising and other Commonwealth, state and territory laws, as well as the implementation of the National Compact: *working together*.

The Council is chaired by Linda Lavarch from the Australian Centre of Philanthropic and Nonprofit Studies. For the membership of the Council, see Attachment 1.

The Reform Council is expected to meet in February, June, August and November 2012.

### Analysis of the Not-for Profit Reform Council

The Not-for-Profit Reform Council is comprised of respected leaders from across the sector and is well resourced.

We note that, as well as being career managers in the NFP sector; members also serve on boards or report to boards and are familiar with that dimension of governance work as well.

## Section 5. Separate Not-for-Profit Regulator

### a. The size and establishment of the new Regulator

#### Situation

The Government committed \$53.6 million over four years in the 2011-12 Federal Budget, to establish the ACNC, and related structural changes required to the Australian Taxation Office (ATO), to enable significant improvements in processes for and oversight of financial and compliance reporting for NFPs claiming exemption from tax as “charities”.

The ACNC is being established as an independent statutory office responsible for determining charitable, public benevolent institution and other not-for-profit status for all Commonwealth purposes.

The ACNC will:

- report to Parliament through the Treasurer;
- be staffed by around 90 officers, with potential for growth if additional functions are added; and
- be supported by the ATO in the provision of back-office services.

Its starting date has been deferred to 1 October 2012 in order to provide more time for the sector and Government to continue to work closely together to finalise the legislation, in the spirit of the National Compact.

Once established, the ACNC will liaise with the ATO regarding the status of NFPs and the ATO will administer “charitable” and all other NFP tax concessions.

The ACNC will be restricted, until 2014, to regulating the 56,000 or so NFPs that claim any of the various forms of exemption from tax on the moneys they raise – the so called “charities”.

However, as noted below, NFPs not in the first tranche, will still be able to relate to the ACNC, if they wish to, through its provision of:

- education and support to the sector;

- implementing and managing the Public Information Portal to be established by 1 July 2012; and
- introduction of a 'report once, use often' general reporting framework for charities.

The ACNC will be supported by an Advisory Board headed by Robert Fitzgerald, the author of the 2010 Productivity Commission research report, *Contribution of the Not-for-Profit Sector*.

To prepare for the launch of the ACNC, the Government set up an Implementation Taskforce based in the Treasury from 1 July 2011. The Taskforce is actively consulting with the public, the NFP sector and across the Federal and State / Territory governments on general reporting and public information portal requirements.

### Analysis of arrangements for the new regulator

The biggest advantage the new regulator has is that it can be different from ASIC.

Apart from its important role in supporting good practice at the macro-level in the corporate sector, ASIC is widely regarded by those who have to deal with it at the micro level, as insufficiently aware of the unnecessary demands it makes with process and returns, compared to the value of those demands in supporting good governance.

ASIC is typical of the usual response of public administrators who respond to emerging problems by adding regulation without effectively evaluating it or making offsetting reductions.

This is a combination of organisational culture, allocation of resource priorities and the low level of awareness among public servants about the practical realities of the market they regulate.

Normal practice in public administration gives little value to relieving the regulatory burden. Because it is undertaken by junior employees, is time-consuming and runs risk of criticism, it is easier for junior staff to just demand for more information because they have the power to command. Regulation becomes a rolling accretion of required minutiae to be provided without evaluation of its value in managing compliance with the regulatory requirements.

ASIC has no track record of taking any initiative to reduce red tape and to streamline regulation, despite calls to do so for decades from the business community and despite platitudes from successive governments about the importance of this work.

As with the inclusion of the present level of NFP productivity in the national debate about improving national productivity, the potential contribution of reduction of red tape and the streamlining of regulation in the NFP sector should also be included in the national debate

A new and different approach to regulation of the NFP sector is entirely appropriate to the nature of the sector, where there are few external imperatives to observe good governance practice.

Decisions have yet to be made about how to deal with more effective regulation of other bodies in the NFP sector such as industry bodies, professional organisations, issue-related lobby groups, service clubs, private schools and the like. Most of these bodies are already incorporated as associations under state/territory jurisdiction or as companies limited by guarantee under the *Corporations Act, 2001* and presently regulated by ASIC.

We note the possibility of their using the Portal, as well as their own web sites, for marketing themselves to their stakeholders and potential donors.

b.. **New culture for the regulator to strongly influence and support the quality of governance across the NFP sector,**

**Situation**

The intent of the Reform Agenda is to establish as a separate regulatory regime for the Charities and NFP sector that is very different in its culture and relationship with the entities it regulates than we have seen anywhere else in our forty years of involvement with the APS and national-level Government leadership.

The ACNC is being deliberately developed with a different approach to regulating the sector, compared to the present approach of ASIC.

In establishing the ACNC, careful attention is being given to attune it to the particular cultures, needs and working realities of organisations in the sector.

Recruitment is focussed on appointing staff with experience in the NFP sector. Leaders experience in similar NFP reform in the United Kingdom, Canada and New Zealand have already been appointed. Staff at senior levels have also been recruited from roles at the highest levels within leading charities and the NFP sector.

A lot of work is being done to ensure an independent culture and an orientation of transparency and co-operation with the sector.

### Analysis of the new culture

Because of the very different culture of governance and accountability in the NFP sector, compared to the private and public sectors, it is essential and entirely appropriate that the Government's approach to bringing in newfound legislation and regulation should be very different from that which pertains for the other two sectors. A separate regulator for the sector is the best way of relating to the organisations in it.

We are most impressed at the innovative way an open and practical culture is being deliberately created by the experience and background from which the staff of the ACNC have been recruited. It has a high chance of success in managing compliance by a regulatory framework that will be effective in lifting the standard of governance and creating competition for excellence in the Charities and the NFP sector.

If the ACNC is able to build and sustain a different regulatory culture based on awareness and sufficiency of effect, the NFP Reforms will have an effect far beyond the NFP sector.

### **c. Education and support role**

#### Situation

Included in this is a role to educate and provide support to the sector. Careful attention is being given to being helpful and to avoid being coercive.

### Analysis of the Education and support role

The involvement of the ACNC (and the Office of the Not-for-Profit Sector) providing education and support to the sector in support of the continually evolving understandings about "how to do" good governance – and then to apply them -will be critically important in strengthening the incentives for NFP boards to apply themselves to this task.

In welcoming the role of providing education and support to the practice of good governance, we caution that it is essential that the Implementation Task Force and the Office of the Not-for-Profit Sector make full use of:

- the long standing professional bodies;
- the extensive body of knowledge that has grown up over an extended period of time with real time experience about what works and what does not work;
- the principles of good governance; and



- the precedents of the Courts.

We note the well established and central role of the AICD, as well as other professional governance support and advisory bodies, and the many and varied sources of expertise that exist in the governance community, including this Practice, which provide detailed support to NFPs in how to serve their members to the best of their ability. There are powerful synergies among all the parties concerned to be used in implementing the Government's reform agenda.

We note the culture of consultation that has been established from the outset of this reform initiative and that the consultative groups contain high calibre people, who are aware of what expertise is already "out there". We found there is a basis for a constructive development of complementary roles in education and support and that there is a willingness to explore the synergies between the roles of the ACNC and the corporate governance community

## **Section 6. ACNC Implementation Task Force**

### *Situation*

To prepare for the launch of the ACNC, the Government set up an Implementation Task Force on 1 July 2011, based in the Treasury. The Task Force is consulting with the public, the not-for-profit sector and across the Commonwealth and state and territory governments on general reporting and public information portal requirements.

For the members of the Task Force, see [Taskforce members](#)

The immediate focus of the Task Force is on charities with an annual turnover of more than \$60,000.

In order to create a true one-stop-shop regulator, the Australian Government will work with state / territory governments to increase the priority for the Council of Australian Governments (COAG) to bring forward arrangements to clarify the transition from incorporated associations to companies limited by guarantee as NFPs grow in financial stature and their significance in the sector.

Widespread consultation has been undertaken and is continuing. This has made innovative use of social media and other forms of communication, beyond the traditional circulation of formal position papers and internal assessment of the responses. Responses from across the sector have paid tribute to the quality of the consultative processes. This is continuing.

### Analysis of the arrangements for the Implementation Task Force

The Implementation Task Force is well resourced, contains the right mix of skills and is well capable of creating the new culture for the regulator

- with the exception of the comment which follows.

#### **a. Concern about over-selling reduction of red tape and the streamlining of regulation**

##### Situation

Among the central aims of the Government's stated reform agenda is:

- the reduction of red tape; and
- the streamlining and simplification of regulation

We understand that some concern has been expressed that the Government may have oversold those aspects of the reform agenda.

The fear seems to be that these broad aims may be ultimately unachievable and it would be better to avoid becoming hostage to them.

### Analysis of over selling reduction of red tape and the streamlining of regulation

It is these very aims that will allow the ACNC to stand out as different from ASIC

- and indeed from the general run of government regulators.

If the Australian Government resiles from these centrally important aims, it can “kiss goodbye” to any aspiration for a co-operative relationship between the Charities and NFP sector and the new regulator that was launched with such high ideals.

The sector will return to “business as usual” and a once-in-a-generation chance to make a difference will be lost.

That comment does not underestimate the extreme difficulty of the task ahead

- it argues for the highest priority to be given to achieving it.

In doing so, and consistent with the overall approach of the reform agenda to recruit people with the skills needed to establish a new culture, there would seem to be wisdom in connecting with the skills of people who have established and/or led regulatory agencies, to ensure the ACNC has:

- the right strategic directions and policy orientation upon which to plan its work;

- the management structures appropriate to the new culture;
- the right abilities in staff;
- on-going training and “attitude checks”;
- reporting and audit arrangements oriented to ensuring the reduction of red tape and that the streamlining and simplifying of regulation actually happens; and
- an effective feedback loop from the sector as a reality check that red tape really is being reduced.

See our suggestions about the conceptual basis for achieving the Government’s stated aims for the Reform Agenda at Section 7. below.

## **Section 7. Opportunities to establish central new regulatory concepts and responsibilities**

Establishing the separate regulator with its own culture oriented to serving the NFP sector brings the opportunity to look afresh at the conceptual basis upon which the policy, legislation and regulations that implement the Reform Agenda will be based.

We note the following areas for consideration.

### **7.1 Enshrine the twin concepts of regulatory “awareness” and “sufficiency”.**

#### **“Awareness”**

It is essential that the regulator is knowledgeable about the situation, needs and performance of the bodies being regulated

- and the effect of its administration upon their achievement of the objective for which each NFPs exists.

#### **“Sufficiency”**

In regulating the NFP sector, the concept of “sufficiency”, applied with the awareness of the situation of each body, should be the central tenet of the regulatory framework

- and all the elements of its administration.

It is essential that the regulator is held responsible for working under the discipline of “sufficiency”

- and that, as regulatory provisions are developed to cover evolving circumstances, equal priority is given to ensuring that offsetting provisions be removed from the regulatory framework that are no longer required for “sufficient” regulation.

It is essential that the regulator’s performance in its exercise of the discipline of “awareness” and “sufficiency” should be subject to external audit by an arrangement that includes the integral and continuing involvement of knowledgeable persons with relevant experience and good reputation in the NFP sector.

Note:

1. The effect of the introduction of the concept of “sufficiency” to the legal requirement for the recording of the minutes of a meeting. What was traditionally lengthy and detailed is now significantly simpler.
2. The long-standing request from the business community for regulatory impact statements to be included as an effective discipline upon all proposed legislation and regulation.

7.2 Develop the concept that the grant of charitable status, giving exemption from tax and other concessions granted to the business of generating income, is allocating a public resource that should be valued and its use should include explicit obligations on the recipient to show how it plans to use the resource effectively.

7.3 Develop the concept that it is a fundamental compact between the organisation and the concessional funding it receives that the way the resource will be used by each NFP should be planned before the resource is used and the plan should be subject to a level of external scrutiny commensurate with the value of the resource to be used.

Clear understanding should be established in the minds of boards and managements across the NFP sector that any concession to the payment of tax is a cost to consolidated revenue of the nation. The value of that contribution should be transparent and should be subject to audit as a matter of course.

Its use should be well justified as making a superior contribution to the national good than the tax that has been forgone.

Note:

1. The Commonwealth Industry portfolio, from the mid 1980s, imposed on all applications for its industry assistance grants the requirement for a business plan, which was assessed by experts and used as the primary determinant in the decision about a grant.

There was, then, a follow-up audit to assess the effectiveness with which the grant was being used

- and, in the larger grants, active dialogue with the recipient about the efficiency of usage and the outcomes being achieved for the national good.

2. The banks do likewise in their processes for assessing business loans.

- 7.4 Develop the concept that boards have a role to ensure the organisation undertakes its “corporate social responsibility”, which means that, although they are not overseeing businesses that return a profit to their shareholders, they have a duty to their members and to the wider community to “work in a business-like manner.”

Use the opportunity to strongly influence and support the culture of best governance across the NFP sector, especially by

- 7.4.1 Establishing a strong culture of multi-level board performance evaluation as part of expected normal practice, based on further research and clear evidence of the causal link between good performance by the board cascading through the organisation to good performance in the provision of service and other objectives of the organisation, as well as to the wider community.

In our experience, suggestions about instituting some carefully tailored form of board performance evaluation are met with varying degrees of evasion. Performance evaluation tends to be regarded as somehow indecent in an NFP and to be out of keeping with the ethos of volunteers.

Having said that, however, we have noticed a tentative acceptance of the concept that NFPs do owe it to their members to work in a “business like” way.

Developing a culture of multi-level board performance evaluation could become a powerful driver of that blossoming of awareness.

- 7.4.2 Establishing as normal expectation that directors be personally familiar with the principles of good governance and that boards allocate time to deciding how those principles are to be implemented in their particular situation.
- 7.5 Develop the concept that boards should give appropriate priority in their work to the processes and application of good governance for the benefit of their members and the quality of service they provide (especially with funds that are exempt from taxes and therefore a loss to the tax base).
- 7.6 Develop the concept of sector responsibility to actively test for greater efficiency in the provision of agreed services to the community by volunteers or otherwise by charities and NFPs than can be provided by the corporate or the public sectors.

## Section 8. New legislation / regulation

### Situation

As noted above, there has been a lot of work done by the Reform Council and the Implementation Task Force on ensuring a culture that is independent of, yet co-operative with, the NFP sector.

The focus has been to find the right balance between giving organisations confidence to engage with the Regulator and to seek advice, while still keeping the Regulator sufficiently feared / respected to deter bad practice and disregard for the legal duties of directors of charity and NFP boards.

Considerable thought has been given to the “look” and “feel” that the new legislation should have.

Treasury is presently working out what the governance requirements of the new legislation will look like.

Analysis of the opportunity provided by the writing of new legislation / regulations to draft legislation that reinforces the momentum for reform

We strongly support the conclusion of the policy makers that a different style and culture of regulator are fundamental to the urgent task of improving the quality of governance in the NFP sector.

We note our comments at Analysis of the Reform Agenda that:

- 8.1 There are no effective internal governance disciplines on the NFP sector to be cost effective.
- 8.2 Developing greater rigour in the governance of the sector requires attitudinal change among leaders in the NFP sector to govern their organisations well. To achieve this, there has to be a clear reason why people should change from the present ways of leading their organisations.
- 8.3 There is a serious need to strengthen the imperatives to drive greater rigour in the governance practices of the majority of NFPs.

The most powerful imperative in the NFP sector is the purpose for which each NFP is established and operates and the sense of commitment that leaders, managers, employees and volunteers in NFPs bring to their work.

We acknowledge that the “imperative of purpose” is an internal imperative and therefore easier to ignore than an external imperative; it is hard to define, and it is even harder to capture it as a specific driver of performance. Nevertheless, it resonates with the galaxy of reasons for which people join organisations in the NFP sector. It is the best option available for driving change in the particular circumstances of this sector at present.

The “imperative of purpose” provides the most powerful basis upon which to establish a new legislative / regulatory / governance framework that is so designed that it will best enable each NFP to achieve its objectives.

The drafting of new legislation offers the opportunity to define separately for the NFP sector the duties and responsibilities of directors leading NFP boards and to determine how / if these may need to differ from those of the *Corporations Act, 2001* and the *Commonwealth Authorities and Corporations Act, 1997*.

We would urge that the drafters work closely with people who are well familiar with the principles of good governance and how the practice of governance is evolving. We have seen so many constitutions and so much legislation where that didn't happen and the result is black letter law that is at odds with the principles and the practice of good governance.

Boards are hampered from working well and directors are exposed to much higher risk than they should be.

In particular, we note the structured conflicts of interest inherent in elements of the *CAC Act*, the extent to which some of the provisions differ significantly from the principles of best practice in corporate governance and the heightened risks this creates for directors of *CAC Act* bodies.

It will be a matter of policy judgement as to how the key governance principles and concepts we have noted at Section 7. above might be given a focus by being enshrined in the legislation, as distinct from being left to professional learning, the promotion of debate and the support / education roles covered at Section 3. above.

If at all possible, it would be a most significant step if the legislation could conduce to move the NFP sector away from the appallingly bad governance practise of representative boards, which are so prevalent in the sector and which cause so much dissension and inefficiency.

There is also a significant opportunity to re-craft how the “duties and responsibilities of directors” are drawn in order to strengthen understanding that good performance at the board level results in good performance permeating the entire organisation.

Presumably the standard practice will apply of Treasury providing drafting instructions to Attorney-General’s and the traditional legislative drafters getting on with their job.

It is a matter of policy and legal judgement as to where the balance is placed between conservative and innovative drafting. While recognising the inherent “down stream” risks of being innovative, the particular circumstances of the charities and NFP sector would seem to argue for a more innovative than conservative approach to the development of legislation to achieve effective reform.

While acknowledging the risks involved, it is to be hoped that the traditionally conservative perspective of the two Departments will not overtake the opportunity for development of a client-related, independent and transparent regulatory framework that becomes part of the momentum of reform in the sector.



## Section 9. Public Information Portal

### Situation

The Public Information Portal is in the design phase of development by the Melbourne-based portal design firm ASI, that will also build the parts of the Portal relating to the web site and registration processes. These will be operational by 1 July this year.

The intent of the Portal is to allow required macro-reporting from organisations in the first tranche in the sector about their performance, such as Annual Reports and other information required by the legislation.

However, the design of the Portal will also allow charities and other NFPs to include narrative in their data and to change it as required.

It is noted that innovative ways are being considered for potential donors to search the information on the Portal before deciding which charities or NFPs to support, including possibly an “App” for smart phones.

The Portal will provide an annual snapshot of what Charities and NFPs are working in particular areas of service delivery and this could be useful for consideration of where there might be efficiencies to be gained from amalgamation among competing organisations.

The first charities and NFPs which will be required to register with the Portal will be those 56,000 that are granted various forms of tax exemptions or other financial subsidies from the Australian government. This will include a clarification of the definition of “charity”.

The ATO is currently up-dating its details of the organisations that will be required to be included in the first round of registrations.

Design of the Portal includes a method for Charities and NFPs to access their details on the Portal and to up-date their own data. Fundamental to this is the concept that it is to the advantage of each organisation to display data that enhances its reputation, using the Portal to “benchmark” against competing organisations, as well as using its own web site.

The Portal is funded to complete the development work on this part of the sector by 2014. Decisions will be made about what its remit will be for the rest of the sector after that.

The ACNC will set the criteria for what information is demanded from the first tranche of Charities and NFPs that are required to be registered.

This then becomes the source for information used by all other Australian Government agencies – they will not be able separately to contact individual Charities and NFPs to

demand additional information. A “Compact Champion” will be established in the ACNC at Deputy Secretary level to ensure compliance by other agencies of government.

It intended that the Portal will add value to the work of the Charities and NFPs that are registered with it by providing education and guidance, especially for smaller organisations; for example, consideration is being given to a registration pack that includes a DVD on governance, simple hints for directors to use in meetings and advice on such issues as how to run objectives-driven meetings.

### *Analysis of the Public Information Portal*

This is the Information Age come to the Charities and NFP sector.

It will change the ways NFPs relate to their stakeholders, their members and their donors.

The Public Information Portal is the single most important imperative of the reform package, because it will create a better informed market that will force boards and management teams to respond to and to serve their members’ interests better in a highly competitive philanthropic environment.

See our comment on the inclusion of an education and training role as part of the work of the ACNC at Section 5 above. This comment also applies to what is provided through the Portal.

The intent is that, as people see it works for those NFPs that make use of it, this will attract others because they will want to use it, rather than because they are forced to. Once again, we commend the enlightened nature of this approach to reinforcing the reason for regulation – to do the best for the members and objectives of organisations in the sector, as well as the wider community.

At the top end of the sector, change will be forced by the external imperative of greater visibility about the performance of NFPs provided by the Public Information Portal. For the first time, light will be shed on the performance of NFPs and drive a heightened importance to serving their member’s interests well in a highly competitive environment.

For the rest of the sector, the Portal will serve as more of a tool and an encouragement.

## Section 10. Transitional issues

### Situation

Key transitional issues remain to be worked through, including:

- Agreement between the States / Territories and the Australian Government about when a growing incorporated association has reached the point where its financial size/ establishment/ import for the community becomes sufficiently substantial that it should evolve from being managed under state/territory jurisdiction to incorporating under the *Corporations Act*.
- Following the initially budgeted work to 2014, when will companies limited by guarantee be transferred from ASIC to the ACNC?

Treasury is presently reviewing the jurisdictional issues and what changes may be desirable in the regulation of companies limited by guarantee, though with a low priority. It may be a further 3 to 5 years before this issue is given prominence.

Details such as what sanctions / penalties are to be applied and how they are to be administered have yet to be worked out.

However, there is no reason why directors and board teams of NFPS not immediately included in the first tranche of participants should not give attention to their quality of governance for the good of their members. We note that opt-in provisions for NFPs in this category are being considered in the design of the Public Information Portal.

## Summary Overview

Provided the Australian Government achieves its stated central aim of reducing red tape and streamlining and simplifying regulation to produce a separate regulator for the Charities and NFP sector with an entirely different culture and style of relating to the sector, compared to ASIC and the general run of government regulators, the Government's initiative for NFP reform will change the governance landscape of this sector for the better and will provide a pattern to reform regulators in other sectors of the economy.

If the Government resiles from its stated aim of reducing red tape and streamlining and simplifying regulation - this fundamental basis of the reform agenda - or is unable to "make it happen", it will be "business as usual" in the sector. A once in a generation chance to improve the governance and productivity of the sector will have been squandered.

The overall tenor of the relationship between the sector and the ACNC will depend on how well the reforms work at the practical, day-to-day level for the organisations in the sector. The devil is in the micro level detail of how the new regulator goes about its business.

Assuming the Government remains resolute in its aim of reducing red tape and streamlining and simplifying regulation and is able to achieve it, we expect to see serious NFP leaders engaging with it progressively from now onwards.

Boards and management teams will need to review their strategic directions and their priorities within the coming year to engage with the reform agenda, even if they are not in the first tranche of Charities and NFPs that are required to be registered.

For the Charities and NFPs in the first tranche of registrations, review of their strategic directions will be forced by the external imperative of greater visibility about their performance provided by the Public Information Portal. Potential donors and intending volunteers will, for the first time, have access to information about who it is good to support and why.

The reform agenda will lead to much more discerning investors in the sector,

For most other NFPs, the reform agenda will be an opportunity to re-assess the priorities they give to implementing good governance practice as the means of best serving their members, the objects of the organisation and the quality of service they provide to the wider community.

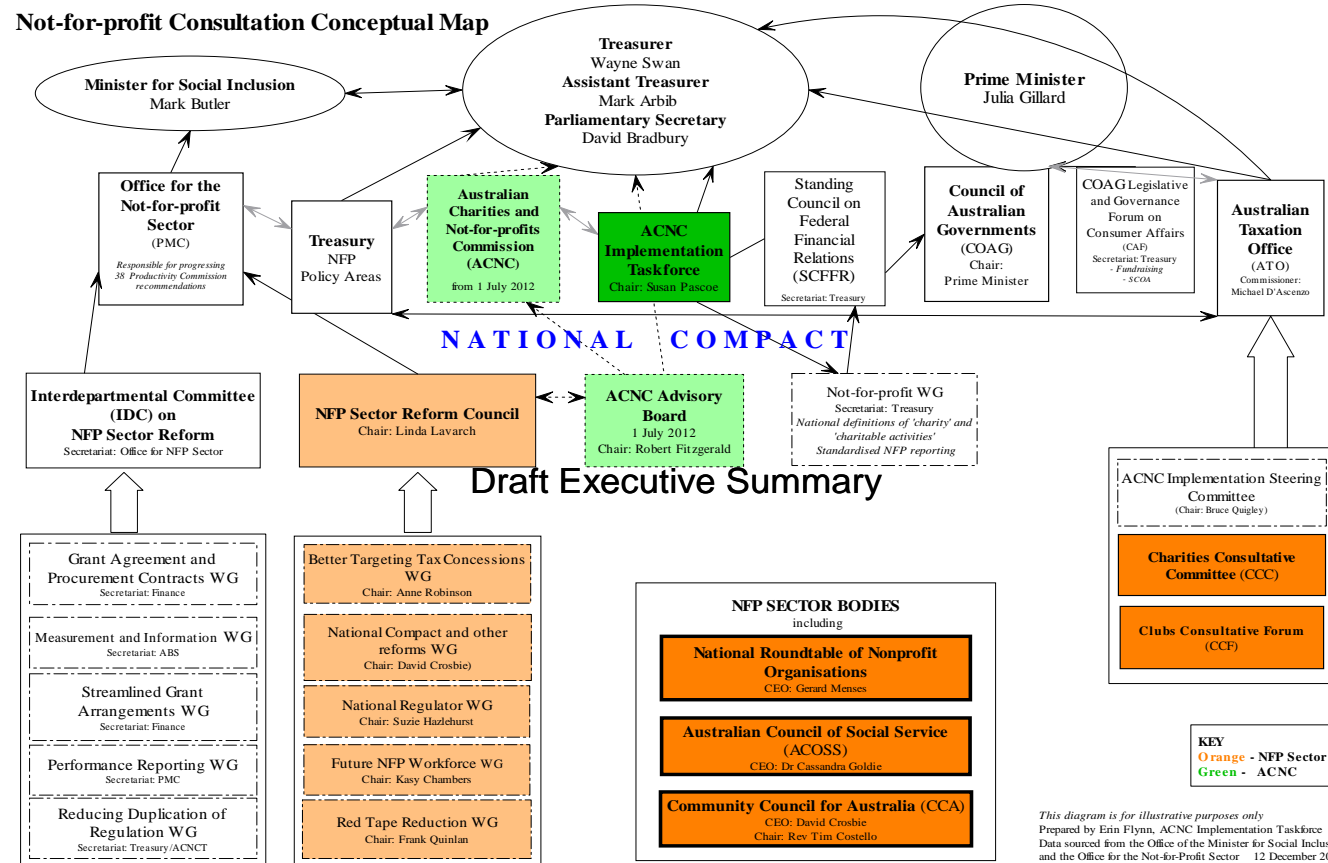
If the ACNC can provide a compliance regime that is “sufficient”, “aware” of NFP needs and easy for NFP boards and management to relate to, the reforms will change the culture in the sector from the present widespread disdain for good governance toward effective engagement with it, because it is in the interests of their members and the wider community.

If the Charities and NFP sector reform agenda succeeds, it has the potential to be used as a pattern to change the wider regulatory approach to managing compliance with required legislation and regulation.

Attachment 1.**NFP Reform Council**

Full membership of the Council includes:

<b>Member</b>	<b>Organisation</b>	<b>Role</b>
Linda Lavarch (Chair)	Australian Centre for Philanthropy and Nonprofit Studies, QUT	Research Fellow
Anne Robinson (Deputy Chair)	Prolegis Lawyers	Founder and Principle
Glenn Appleyard	Australian Accounting Standards Board	Board member
Ken Baker	National Disability Services Limited	Chief Executive
Sandy Blackburn-Wright	Westpac	Head of Organisational Mentoring, Group Sustainability and Community Involvement
Kasy Chambers	Anglicare Australia	Executive Director
David Crosbie	Community Council for Australia	Chief Executive Officer
Michael Coleman	Planet Ark Environmental Foundation	Chairman
Cassandra Goldie	Australian Council of Social Service	Chief Executive Officer
Suzie Haslehurst	Magabala Books Aboriginal Corporation	Chief Executive Officer
Evelyn O'Loughlin	Volunteering SA and NT	Chief Executive Officer
Frank Quinlan	Mental Health Council of Australia	Chief Executive Officer
Ron Edwards	Graham (Polly) Farmer Foundation	Founding Board Member
Robert Fitzgerald AM (ex officio member)	Australian Charities and Not-for-profits Commission Advisory Board	Chair



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*Neil is Managing Director of Primrose Solutions Pty Ltd, which supports company boards and management teams on governance, planning and leadership. He worked for over twenty years in central policy areas in several Commonwealth departments, led change management and micro-economic reform and helped with the establishment of two regulatory agencies.*

*Neil is a transformational leader. He has served as a volunteer, has taken a leading role in several NFPs and has been integrally involved in the governance reform of a number of leading charities. He writes and teaches about principles of corporate governance, has contributed to their development, and runs workshops to help clients tailor the principles of good governance as the basis of working well together as a team in their own, unique situations. He mentors directors and senior executives, as well as leading board performance assessment.*

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*As part of the suite of services that Commerce Management offers, Sue serves as Secretary to the Board of several leading national organisations. She has served as a volunteer and is presently a member of four NFP boards as a director in her own right, chairing one. She has the special advantage of seeing the workings of boards from both sides of the table. She is proceeding with an MBus with UNSW@ADFA with a particular interest in the field of leadership.*

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