



Australian Council of Social Service

**Submission to Consultation Paper on the
development of governance standards**

ACOSS Paper 198

February, 2013

Background

ACOSS has long supported the establishment of a national regulator for charities and not-for-profit organisations, and we have maintained detailed involvement in this reform leading up to the establishment of the Australian Charities and NFP Commission. Our position has been informed by national consultation with our members that found that ours was a sector that was overly but ineffectively regulated, and that member organisations were spending unreasonable amounts of time and resources meeting duplicated, and often unnecessary, regulatory reporting requirements.

In December 2012 the Treasury released a consultation paper seeking feedback on proposals to introduce governance standards for charities registered with the ACNC. Since an earlier draft, released in November 2011, and through an extensive process of policy development within the sector and with government, ACOSS has sought to ensure governance standards that support the value and effectiveness of charitable and not-for-profit community services. The Standards outlined in the present Consultation Paper reflect much of this work.

I. ACOSS principles for effective sector regulation

Through the recent phase of ACOSS policy development and advocacy towards improving the regulatory framework for the charitable and NFP sector, two driving objectives have emerged. These objectives underpin ACOSS' priorities in sector development, namely to support and strengthen:

- a diverse, vibrant and independent sector; and
- most importantly, the effectiveness of that sector for the people and communities who rely upon it.

From these objectives we set framing principles at the outset of this reform through which ACOSS has assessed development towards the governance standards in the current consultation; and future developments in the area of sector reform and regulation.

The strong advocacy for these principles, and their wide acceptance across the sector, has seen them incorporated into the ACNC Act. Given that they are what the legislation is intended to do, it is even more important that they continue to guide the evolution of this regulatory reform.

1.1 Principle 1 for Effective Sector Regulation: the independence of the charitable and NFP sector

Throughout the establishment of the ACNC, ACOSS asserted the primary importance of an independent Commission, marked by its own line of report to Parliament and control over financial and staffing resources. Equally important to the independence of the ACNC is the independence of the sector it is regulating, as a whole and through its constituent charitable and not-for-profit organisations.

The Productivity Commission's landmark study of the contribution of the sector refers to the independence of the sector from governance as a central 'feature' of the not-for-profit sector. It also notes the importance of preserving sector independence in the context of government funding and other financial arrangements.

In fact, independence is one of the key element that unites charities and not-for-profit organisations in a 'sector' that comprises enormous diversity across organisational structure, operational activities, funding, size, geography, the people who work in it and the people who benefit from it. The independence of the charitable and not-for-profit sector is a central principle that regulatory frameworks, including governance principles, must recognise and support.

1.2 Principle 2 for Effective Sector Regulation: reform by principle, not process

While regulatory standards should set minimum expectations of performance, the process by which those expectations are met should be at the discretion of individual organisations and their governance structures.

ACOSS strongly supports the stated intention of the draft governance standards as setting a minimum approach to the governance of charitable and NFP organisations. We welcome the express intention of this as an outcomes-based approach that sets the objective of a standard, while leaving the process by which that outcome is achieved to individual organisations (section 2.3.4). This is an extremely important principle that should guide the evolution of governance standards for the sector from this point on. Proportionality is an additional element of this principle, relating both to the proportionality of measures within the sector given the varying levels of resource available to organisations by size, scope and activities; and to the proportionality of governance arrangements compared to those in the government or corporate sectors.

In this submission we consider each standard against the two ACOSS principles for effective sector regulation, as well as against the key consultation questions of appropriateness of the principles encapsulated by each standard, and their wording.

This submission has been the subject of consultation with our members and incorporates their views. We also note in particular the submission of our members the Public Interest Legal Clearing House (PILCH), whose submission provides further detail on many of the concerns we raise here and on additional implications of the proposed governance standards.

2. Terms and introductory comments about the regulatory framework

The discussion of how the standards will operate and how they relate to the ACNC's regulatory powers is welcome (sections 2.3.4 and 2.3.5). This discussion sets out clearly the implications of a principles-based approach; and how the standards will operate in relation to the Commission's powers.

Unfortunately, this discussion makes no reference to the independence of the sector; nor to the importance of the regulatory framework in recognising, valuing and supporting that independence.

Recommendation: We recommend asserting the principle of sector independence into the framing discussion about the regulatory framework and the environment in which it is operating.

This discussion does however make clear the role of these standards as principles, while leaving the process necessary to meet the standards up to the discretion of individual organisations. In this way it satisfies the second of ACOSS' objectives in regulatory reform.

1.3 Draft Standard One: Purposes and NFP nature of a registered entity

Although there is no reference to the independence of the sector, this standard meets our core objectives of valuing the independence of the sector; and of setting a principle with being prescriptive about its process. It relies on current and relevant legal obligations to inform the standard; while allowing for a range of structures and approaches through which the standard might be met. For instance, it refers to governing documentation in general terms, but does not prescribe forms of governance documentation; nor does it require that this standard be met within governance documentation specifically or only.

While the governance framework should not dictate processes to be followed by organisations, it should be sensitive to the lengths an organisation would need to go to be able to demonstrate it met a standard. In this sense, governance should minimise unnecessary requirements including in reporting (ie 'red tape').

Both this standard and its wording are appropriate.

3. Draft Standard Two: Accountability to members

This standard is intended to reflect the importance of accountability by membership-based charities to their members and sets this out in principles while leaving open the process by which it is demonstrated. Our key concern about its value and operation is that it relates to a particular subset of charities, yet is presented on equal footing to the rest of the standards. This could be address in one of the following ways:

- i. While it recognises the diverse range of structures encompassing charities with members, it requires further detail to clarify the implications on particular structures, including identifying the types of registered entities that have members and would therefore be subject to this standard. Reference is made in section 3.2 to entities subject to the Corporations Act 2001 (Cth) and to an incorporated association. It would be helpful to specifically identify the sorts of entities that will be impacted by this standard. For example, draft regulation 45.10 (Appendix I) could provide guidance on the entities that have members and would therefore be subject to this governance standard.
- ii. The more significant problem with this standard is that it is relates to a particular subset of charities that is not clearly identified, yet is presented on equal footing to the rest of the standards. This could be address in one of the following ways:
 - a. If it is intended that this standard actually applies to the majority of charitable organisations, this fact and how it is demonstrated should be explicitly stated.
 - b. If it is a standard that applies only to a sub-group of charities that have members, as appears to be the case, then it is a sub-standard and should not be asserted at the same level as standards that apply to all charities.

We note the recommendation by PILCH to broaden out the application of this recommendation, which is one way to lift it from the value of a sub-standard (by virtue of its application to a subset of charitable organisations). However, we also recognise that this could add considerable confusion to operation of the standard and could potentially have unforeseen consequences, including undermining the independence of organisations and adding to the regulatory burden.

If these concerns are not resolved, the standard may undermine the objective of recognising and supporting an independent sector and the additional (previously stated) objective of ensuring proportionality in the regulatory framework for the sector, in so far as membership-based charities are subjected to an additional layer of regulation not applicable to the sector as a whole.

We are not convinced of the appropriateness of the principle reflected in this standard.

Recommendation: We recommend clarification about the application of this standard to its fullest extent and the identification of the sorts of entities that have members and would therefore be subject to this standard. If the standard does apply only to a particular part of the sector, we further recommend reducing its alignment to the rest of the standards that are applied without exception. In any event, we recommend further consultation be undertaken if this standard is to be revised or refined.

4. Draft Standard Three: Compliance with Australian laws

We understand that this standard is intended to enable the ACNC to investigate charities that have or are suspected to have breached Australian laws. It makes important qualifications to the nature of compliance, stating specifically that breaches of law that might trigger the powers of the Commission will be confined to serious or indictable offences; or civil offences that carry a high penalty.

However we remain concerned about whether this standard:

- i. relates to governance issues in the first place;
- ii. may be pre-emptive, on the basis that the ACNC could exercise its powers if a charity 'may' have breached Australian law; and
- iii. could be exercised unfairly in the future.

We note the detailed discussion of concerns about this standard from the PILCH submission, including their concerns about both its scope and application. We support their recommendation that a better way to ensure the protections intended by this standard would be achieved through the reform to the definition of charity, such that the definition could clarify that if a charity engages in illegal activity of the kind contemplated by standard 3, it would no longer be a 'charity'. This would give the ACNC a basis upon which to act in the event of illegal activity by a charity through its powers including de-registration; and through associated processes such as notification to alternative authorities.

We are concerned about the necessity of this as a standard of governance and its potential for unintended consequences.

5. Draft Standard Four: Responsible management of financial affairs

The drafting of this standard reflects a positive assertion of responsibilities and is therefore a welcome approach compared to, for example, one of risk management. However, we are concerned by this standard singling out financial responsibility as separate to, and more important than, all other areas of responsibility. Many sector organisations have a range of responsibilities including but not limited to financial affairs; industrial relations; work health and safety; human rights; diversity; and equal opportunity. Many of these carry legislative force. It remains unclear from the drafting of this standard why financial management should be privileged above the full range of responsibilities that fall on charities and their governing bodies.

While we contest the appropriateness of this principle; its wording, should it remain, is appropriate.

6. Draft Standard Five: Suitability of responsible entities

Maintaining the public's trust in the charitable and NFP sector is crucial. There is merit in prescribing certain minimum standards for responsible entities to provide some level of consistency, notwithstanding that certain charities (adopting certain structures and operating in specific jurisdictions) may otherwise be subject to more or less onerous responsibilities and obligations.

However, we have a number of concerns about this standard. We find it difficult to understand how it would work in practice; and cannot imagine any process for implementation that would not involve significant amounts of red tape to demonstrate the outcome intended.

As a matter of principle, we also have concerns about how this standard support participatory governance structures, of the type preferred by many organisations in the ACOSS network. The fact that a particular law exists somewhere in Australia to prohibit certain people from engaging in managerial or governance roles is not in itself justification to extend that prohibition to all charities nationally. For example, people who are users or consumers of services should generally be able to participate in their management structure, but the discussion in this standard implies that ex-offenders might not be able to join the Board of a charity supporting people post release from prison.

It is also unclear to us how the proposed register of disqualified responsible entities (draft regulation 45.150) will operate and its implications. For example, once listed on the register, will a disqualified responsible entity remain on the register indefinitely?

We are not convinced of the appropriateness of the principle reflected in this standard.

The removal of this standard would not weaken the overall value of the governance framework and therefore it is superfluous while being unnecessarily confusing. Moreover, our concern about the present drafting should not be taken as a preference for alternative and previously debated provisions such as a fitness test for persons holding responsibility for governance in an organisation.

Recommendation: Remove standard five.

7. Draft Standard Six: Duties of responsible entities

This standard should provide the basis upon which the ACNC takes action against organisations as well as individual directors. The intention behind this standard is to provide a lever for the ACNC to make a charity meet certain responsibilities; and also to be able to make individual directors meet those responsibilities. While the current standard places obligations on an organisation, we cannot see how it compels directors individually. That compulsion would previously have come from the Corporations Act, for those charities regulated by this legislation, such as companies limited by guarantee; but that Act no longer applies in this context. Therefore we see a gap within the intention of this standard and its coverage from the current drafting.

In addition, the current standard requires charities to find a way to make duties legally binding on their directors. For many organisations, those duties are not already in legislation. Therefore this is likely to require further processes being implemented by charities. We are concerned that this conflicts with the objective of reducing red tape and is likely to add a burden to organisations to ensure they can demonstrate compliance.

We remain concerned about whether duties that were developed to apply in the for-profit context are appropriate to apply to all charities.

Finally, this standard is the most difficult to understand. It reflects a concern we have often stated throughout this reform, about the absence of plain language from legislative drafting and explanatory materials. The word 'entity' is a good example here, being used to refer both to individuals (such as Board members) and organisations.

Alongside plain language, other elements that would improve the accessibility of these standards for the sector include more comprehensive definitions, incorporating terms such as 'benefit recipient' and 'related party transaction'. Footnotes would be equally helpful, given that there would be many organisations, including in emerging communities, who would find these concepts a barrier to understanding the standards. More examples that small organisations could identify with would also be of great benefit. This could be dealt with either in the notes to the standards or in the support materials to be developed by the ACNC.

We are not convinced that vesting responsibility with organisations, not individuals, is the appropriate principle to be reflected in this standard; nor are we satisfied with the clarity or appropriateness of the language here.

Recommendation: Standard six should set out clearly and simply the responsibilities on organisations and their governing bodies, and refer to the presence of legislative frameworks that require these as relevant. Defences need be set out only if they are not already covered in alternative legislation (such as for the elements being replaced from the Corporations Act).

8. Timing and transitional arrangements

The timing and transitional arrangements appear appropriate. While the governance standards would apply from 1 July 2013, we note specific provision that allow for:

- i. 18 months from the commencement of the governance standards to make any necessary changes (for example, to internal procedures), to meet the governance standards, except in relation to changes required to a registered charity's governing rules; and,
- ii. a registered charity whose governing rules are inconsistent with these standards, and needs to amend these accordingly, to have four years from 1 July 2013 to make these changes to be in compliance with the governance standards.

To discuss this submission further, contact ACOSS Deputy CEO Tessa.Boyd-Caine@acoss.org.au.