

Submission to the Review of Australian Charities and Not-for-profits
Commission (ACNC) legislation prepared by Dr Ted Flack, BEc., PhD., EFFIA

Mr Murray Crowe
Individuals and Indirect Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

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By email: ACNCReview@treasury.gov.au

Dear Sir

I write in response to your invitation to make submission to the Review of the ACNC legislation. The views and opinions expressed in this submission are my own and they represent no brief from any other person or organisation.

The recommendations in this submission reflect views developed from my more than 40 years' experience of work, volunteering and study in the not-for-profit sector. I have extensive experience in roles as a paid senior executive in several well-known charities, a volunteer Board Member and Chairperson in several others and a consultant to more than 50 charities. I have given evidence before several State and Commonwealth parliamentary enquiries on directly relevant matters to this Review. My doctorate reports the results of high level research into the accountability of charitiesⁱ.

The attached Submission contains four detailed responses to key issues raised in the Terms of Reference for this Review and makes the following recommendations:

1. **That the current ACNC legislation remain largely unamended while allowing for the ACNC's recommendations regarding necessary administrative amendments.;**
2. **That the Objects of the ACNC not be amended to include new objects "To promote the effective use of resources of not-for-profit entities" nor "To enhance the accountability of not-for-profit entities to donors, beneficiaries and the public", and that this issue be again considered when the State and Territory powers to regulate charities and charitable fundraising are referred to the Commonwealth;**
3. **That the ACNC give priority to working with the State and Territory governments to harmonise regulation so as to reduce the regulatory burden on charities, and**
4. **That in order to provide more qualitative information about the activities of each charity, the ACNC make provisions on its Charity Register for an on-line link to each charity's Annual Report and encourage all charities to either up-load or provide a link to their current Annual Reports.**

In the attached Submission, detailed arguments are put to support these key recommendations.

Yours faithfully



Dr Ted Flack

Recommendation 1 - That the current ACNC legislation remain largely unamended while allowing for the ACNC's recommendations regarding necessary administrative amendments.

Until the States and Territories refer their powers to regulate charities and other not-for-profit organisations to the Commonwealth government, expanding the powers of ACNC simply adds to the regulatory burden of these organisations and is contrary to one of the objects of the legislation.

The current ACNC legislation, based largely on the Commonwealth's taxation powers, is intended to regulate those charities that wish to take advantage of the Commonwealth tax concessions available only to charities. It is important to note that there are many legally recognised charities registered in every State and Territory that have chosen not to register with the ACNC yet continue to be recognised for tax-concessions by the Australian Tax Office (ATO) and regulated by the applicable State and Territory government legislation.

In addition there are many other types of not-for-profit organisations that enjoy a subset of the tax concessions available to charities and other not-for-profit organisations that are not required to register with the ACNC. These not-for-profit organisations continue to be regulated by State and Territory government legislation.

As stated on the ATO website

Examples of other NFP organisations are sporting and recreational clubs, community service organisations, professional and business associations, and cultural and social societies. NFP organisations that are not charities are able to self-assess their eligibility for exemption from income tax, but will need to register for other tax concessions.

And

Your NFP organisation may need to get an Australian business number (ABN). You may also need to register for some taxes such as GST, fringe benefits tax, PAYG withholding or other taxes.

Recommendation 2. That the Objects of the ACNC not be amended to include new objects "To promote the effective use of resources of not-for-profit entities" or "To enhance the accountability of not-for-profit entities to donors, beneficiaries and the public", and that this issue be again considered when the State and Territory powers to regulate charities and charitable fundraising are referred to the Commonwealth.

There are three arguments against such an expansion of ACNC powers "To promote the effective use of resources of not-for-profit entities".

First, it is argued that, since charitable entities are regulated by State and Territory legislation and the ACNC's powers are limited to those powers that are derived from the taxation powers, providing the ACNC with powers to make judgements about the "effective use of resources" by charities over-reaches the constitutional powers of the Commonwealth in respect of the regulation of charities.

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Second, the use of the term “effective use of resources” invites the question “on what basis will a determination be made about what is “effective” and what is “ineffective”? Further information about the grounds on which such judgements are to be made need to be articulated before this proposal can be seriously considered.

Third, the inclusion in the objects of the Act wording such as “effective use of resources” would require the ACNC to make judgements about the use of charity resources based on information either collected as a part of an investigation or alternatively from data routinely collected from the “Annual Information Statement” (AIS) or the charity’s Annual Financial Report (AFR).

This issue has the potential to involve the ACNC making judgements on matters that have traditionally been left to charity “trustees” or “responsible persons”. The information currently available to the ACNC from the AIS and AFR submitted by charities annually is not suitable for making assessments about the “effective use of resources” in the ordinary sense of the words.

Comment. At present, the data collected in the reports and returns required by the ACNC, including the AFRs submitted by charities, reflect wide variations in the use of terms used in financial data, such as “donations”, “grants” and “fundraising”, to name just a few lines of account, making accurate comparisons between both inter and intra state charities unsound (Flack et al, 2014ⁱⁱ; McGregor-Lowndes et al 2014ⁱⁱⁱ).

Since the information necessary to make such judgements is not currently available to the ACNC via the AIS and AFRs, the ACNC would need to collect information on which to make such an assessment either by conducting an investigation on a charity reported to it as not making effective use of resources, or the ACNC would need to routinely collect the data it needs to make such assessments from an amended AIS requiring more data. The ACNC currently has the powers necessary to liaise with the State and Territory charity regulators on such investigations.

If it is proposed to routinely collect more information from all charities in the attempt to identify the misuse of resources, then any such a proposal is likely to significantly increase the regulatory burden on all registered charities. Since one of the objects of the Australian Charities and Not-for-profits Commission Act 2012 (Cth) (ACNC Act) is to “promote the reduction of unnecessary regulatory obligations on the Australian”, it is difficult to justify the imposition of such a requirement given that there is no evidence that such a collection would achieve its purpose.

Whatever the “trigger” for the investigation of a charity suspected of not using its resources effectively, the ACNC would need to obtain detailed knowledge of the charities operational activities and the grounds on which judgements about the allocation of resources that had been made by the “responsible persons” and staff of the charity. Such investigations go well beyond both the current powers and resources of the ACNC.

If it is proposed to use some type of ratio(s) derived from financial data collected in the AIS or in the Annual Financial Statements in order to signal the potential for inappropriate use of resources, such as “overhead costs”, “cost of administration” or “cost of fundraising”, then the ACNC will be well advised to note that the use of such ratios is widely discredited and found to be useless as indicators of effective use of resources^{iv}. It is noted that the ACNC has previously responded to this issue in public statements on its website as follows:

[ACNC “Factsheet: Charities and administration costs”](#)

[ACNC “FAQs: Charities and administration costs”](#)

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[ACNC "FAQs: Charities and fundraising"](#)

From reading the ACNC's submission to this Review, is not clear on what grounds the ACNC would want to have these new objects inserted into the Act. The ACNC's Annual Report 2016-17 provides a comprehensive summary of the ACNC's compliance work indicating that where there is either non-compliance with governance or reporting standards, the ACNC has adequate powers to pursue the current objects in the Act. The Annual Report does not refer to any lack of powers to properly respond to the cases raised with it. It should be noted that at present the ACNC relies heavily on State and Territory charity regulators in order to conduct investigations. In this respect, it will also be noted that the ACNC's website provides the following advice:

"The ACNC is not a national fundraising regulator (there are many agencies who regulate fundraising), but the ACNC can take action in certain situations."

The inclusion of this proposal in the ACNC's submission therefore raises questions as to what emerging issues have caused the ACNC to recommend the inclusion of an object that refers to the "effective use of resources" in the ACNC' objects?

If it is not "administration costs" or "cost of fundraising" issues, then the ACNC may be responding to some recently expressed public concerns about the allegedly excessive salaries earned by some charity executives. If this is so, then the provisions in the Corporations Act and Australian Accounting Standards Board (AASB) 1046 may already apply to charities incorporated as companies which tend to be the larger charities. AASB does not apply to most smaller charities incorporated under other legislation. If the public disclosure of the salaries of charity executives is the central issue, then minor amendments to the disclosures required in the AIS could be used to fulfil this information requirement without alteration to the objects of the Act.

Since the purpose of the proposed new powers is "To enhance the accountability of not-for-profit entities to donors, beneficiaries and the public", then it is important that some evidence is offered to demonstrate that there is a demand for such information from donors, beneficiaries and the public and the nature of the information being sought. There is no rigorous, independent research that supports such a demand in Australia.

It has been proposed that by setting up systems that will require similar charities to disclose measures of their "efficiency", that this will allow donors to judge which charities are "most efficient". This initiative is pursued in the belief that donors will then use this information to choose the charities they wish to support.

Such a proposition is not supported by the international research about the decision-making processes that drive donors. In fact, the research suggests that such measures encourage the wrong management decisions^v within charities and that the donors don't use that kind of information (Connolly and Dhanani, 2013^{vi}; Hyndman and McKillop, 1999^{vii}; McGregor-Lowndes, et al 2014^{viii}; Moxham, 2014^{ix}).

Comment: It will be noted that in economics, "efficiency" is measured "at the margin" – not on an average calculation. So a practical example of the use of the theory might be - if the cost of delivering one more Christmas Lunch means that the unit cost overall goes down – then it's efficient to produce the extra meal. If on the other hand, producing one more meal means that the charity has to employ more staff or expand the kitchen, then providing that extra meal is less efficient than the one before. This does help us to understand that larger organisations have the potential to be

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more efficient – the economies of scale. However, when large charities take over from smaller less efficient charities, the evidence shows that there is a loss of personalisation and community connections.

While there is no evidence of a demand in Australia from donors, beneficiaries or the public for information about the “efficient use of resources, there is some evidence to support a demand for more information about the activities of charities. This type of narrative information is not at present available on the ACNC Register.

Recommendation 3. That the ACNC give priority to working with the State and Territory governments to harmonise regulation so as to reduce the regulatory burden on charities.

Six national inquiries on regulation of the not-for-profit sector have been conducted since 1995. Each of these inquiries found that it was necessary to simplify and harmonise regulation for the not-for-profit sector (and in particular charities) and recommended some form of independent national regulator as a solution.

The Productivity Commission’s review in 2010 recommended the establishment of a national one-stop-shop regulatory framework to oversee the not-for-profit sector, grant tax endorsements and to pursue greater harmonisation of regulation between the states and territories and the Commonwealth to reduce compliance costs.

The ACNC Bill was widely supported by the charity sector in the belief that a “one-stop shop” national regulator would reduce the regulatory burden caused by the fragmented and duplicative regulatory framework clearly identified in the numerous previous inquiries. The sector’s support for the ACNC was largely based on the understanding that there may be a relatively small increase in the regulatory burden initially, but that over time, the ACNC’s harmonisation work would lower the overall burden.

In the first five years the ACNC has made some progress in reducing the complex regulatory burden on charities – the major reason why the charity sector supported the establishment of the ACNC. Perhaps the most useful reductions have been the simplification of the annual reporting requirements for charities incorporated as companies under Commonwealth Corporations Law and “report once” arrangements with Incorporated Associations in the ACT. Progress has also been made with Victoria and Western Australian governments to reduce some duplicative reporting for charities incorporated as in those States.

Charities wishing to raise funds from the public continue to be regulated by their relevant State and Territory governments (except Northern Territory) and the ACNC has had little success so far in negotiations with the states in this area of regulation to reduce the regulatory burden. So far, only the ACT and SA have agreed to recognise the ACNC registration for the purposes of fundraising licensing. Charities in those jurisdictions continue to be required to comply with inconsistent regulation and reporting.

In summary, the charity sector has been largely supportive of ACNC in the hope that the regulatory burden will be further reduced. While there has been some impatience around progress on “red-tape” reduction, the sector recognises the difficulties inherent in negotiations with the States, especially during the period when the ACNC’s future was in some doubt during the Abbott government.

Recommendation 4. That in order to provide more qualitative information about the activities of each charity, the ACNC make provisions on its Charity Register for an on-line link to each charity's Annual Report and encourage all charities to either up-load a link to their current Annual Reports.

If the objective is to "To enhance the accountability of not-for-profit entities to donors, beneficiaries and the public", then the provision of narrative explanations of the charities activities, its allocation of resources and its governance arrangements is much more likely to meet those needs. Most large charities, many medium sized and some smaller charities already publish Annual Reports for distribution to their members and supporters as a part of their annual general meeting processes^x.

A simple and less burdensome means of providing information to stakeholders that would enhance the accountability of not-for-profit entities to donors, beneficiaries and the public would be to encourage charities to make their annual reports available to the public through the ACNC Register.

There are already well established annual reporting awards, such as such as the Australasian Reporting Awards^{xi} and the PwC's Transparency Awards^{xii} in Australia which provide examples of high standard annual reports prepared by charities.

ⁱ Flack, Edmund Douglas. "The Role of Annual Reports in a System of Accountability for Public Fundraising Charities." Thesis, Queensland University of Technology, 2007.
<http://eprints.qut.edu.au/16362/>.

ⁱⁱ Flack, Ted, Myles McGregor-Lowndes, Stephen Marsden, and Glenn Poole. "Go Your Own Way: Reporting of Fundraising in Australian Charity Financial Statements." *Third Sector Review* 20, no. 2 (2014): 9–22.

ⁱⁱⁱ McGregor-Lowndes, Myles, Ted Flack, Glenn Poole, and Stephen J. Marsden. "Chapter 5. State and Territory Regulation and Fundraising." Brisbane , Queensland: Queensland University of Technology, 2014.

^{iv} Guidestar. "BBB Wise Giving Alliance, Charity Navigator, and GuideStar Join Forces to Dispel the Charity 'Overhead Myth.'" *Targeted News Service*. June 17, 2013.
<http://search.proquest.com.ezp01.library.qut.edu.au/docview/1368619524>.

^v Ling, Qianhua, and Daniel Gordon Neely. "Charitable Ratings and Financial Reporting Quality: Evidence from the Human Service Sector." *Journal of Public Budgeting, Accounting & Financial Management* 25, no. 1 (Spring 2013): 69–90.

^{vi} Connolly, Ciaran, and Alpa Dhanani. "Exploring the Discharge of E-Countability by Charities." *Journal of Applied Accounting Research* 14, no. 2 (September 6, 2013): 108–26.
<https://doi.org/10.1108/09675421311291874>.

^{vii} Hyndman, Noel, and Donal McKillop. “Conversion Ratios in Charities in England and Wales: An Investigation of Economies of Scale.” *Financial Accountability & Management* 15, no. 2 (May 1, 1999): 135–53. <https://doi.org/10.1111/1468-0408.00078>.

^{viii} McGregor-Lowndes, Myles, Ted Flack, Wendy Scaife, P. Wiekking, and Marie Crittall. “Giving and Volunteering in Australia 2014 : Environmental Scan/Literature Review.” Report. Brisbane, Queensland: Australian Centre for Philanthropy and Nonprofit Studies, September 2014. <https://www.qut.edu.au/business/about/research-centres/australian-centre-for-philanthropy-and-nonprofit-studies>.

^{ix} Claire Moxham. “Understanding Third Sector Performance Measurement System Design: A Literature Review.” *International Journal of Productivity and Performance Management* 63, no. 6 (July 8, 2014): 704–26. <https://doi.org/10.1108/IJPPM-08-2013-0143>.

^x Flack, Ted. “Annual Reports Still Valuable for Not-for-Profit Organisations.” *Keeping Good Companies* 60, no. 2 (March 2008): 72.

^{xi} “Australasian Reporting Awards 2018.” Accessed February 16, 2018. <http://www.arawards.com.au/>.

^{xii} PricewaterhouseCoopers. “Transformation of PwC’s Transparency Awards.” PwC. Accessed February 16, 2018. <https://www.pwc.com.au/corporate-responsibility/transparency-awards.html>.