Australian Government

The Treasury

Parliamentary Joint Committee on Corporations and Financial Services

Inquiry into the Australian Charities and Not-for-profits Commission (ACNC) Bills, and the Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012

Submission by the Australian Treasury Portfolio

The ACNC Implementation Taskforce, the Australian Taxation Office, the Australian Securities and Investments Commission, the Australian Accounting Standards Board and the Auditing and Assurance Standards Board have been consulted in the preparation of this submission

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INTRODUCTION

Consultation and review processes in the development of the ACNC framework

1. A sound regulatory system for the not-for-profit (NFP) sector plays a key part in sustaining and supporting the sector, and the valuable contribution the sector provides to the community. While the Government provides significant support to the sector through tax concessions, exemptions and other entitlements, appropriate regulation of the sector will help to ensure that valuable resources are best used in furtherance of the NFP objectives, rather than unnecessary regulatory and compliance costs. At the same time, there needs to be an appropriate level of transparency and accountability, to protect the public and maintain confidence in the sector, which in turn, will promote further contributions to the sector and support its growth.

2. Australia's current regulatory regime imposes regulatory requirements on NFP entities for different and overlapping purposes. The Productivity Commission, in its 2010 report, noted that the 'current regulatory framework for NFPs is characterised by uncoordinated regimes at the Commonwealth and State and Territory levels. Disparate reporting and other requirements add complexity and cost, especially for organisations operating in more than one jurisdiction'. [1] In response to these concerns, a number of reviews have recommended the establishment of a national regulator for the NFP sector, and these recommendations have been supported by representatives of the sector.

3. The Government has undertaken extensive consultation on the ACNC legislation and the establishment of the ACNC. These consultation processes have built upon the past reviews and inquiries and have included public consultation on the Scoping Study for a National Not-for-profit Regulator from January 2011 to February 2011 and public consultation on the draft ACNC legislation, in December 2011 and January 2012 as well as extensive targeted consultation with NFP sector consultative groups.

4. A detailed outline of the consultation processes in developing the legislation, and the outcomes from these processes, including key changes made to the legislation following consultation, was provided in Treasury's submission to the House of Representatives' Standing Committee on Economics inquiry into the draft ACNC legislation.

House of Representatives' Standing Committee on Economics inquiry

5. On 6 July 2012, the Government referred the draft ACNC legislation to the House of Representatives' Standing Committee on Economics, for an inquiry over the Winter Parliamentary break.

6. Treasury provided a submission to the House of Representatives' Standing Committee on Economics report into the draft ACNC legislation (attached to this Submission). That Submission provides detailed background information on the sector, including past reviews and inquiries, and the need for a national 'one-stop shop' regulator for the NFP sector.

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1 Productivity Commission, *Contribution of the Not-For-Profit Sector Research Report,* January 2010, p 113. http://www.pc.gov.au/__data/assets/pdf_file/0003/94548/not-for-profit-report.pdf.

7. The Submission also outlines the role of other regulators and agencies within the Treasury portfolio under the new regime.

8. The Submission sets out the interaction with State and Territory regimes, and the current work the Commonwealth is progressing with the States and Territories to ensure that the ACNC is a truly national regulator.

9. The Submission also provides a short overview of a number of the other initiatives that form part of the Government's broader NFP reform agenda, including introducing a statutory definition of charity and better targeting NFP tax concessions.

10. In addition to the initial Submission, Treasury provided a Supplementary Submission to the Committee, which provided additional detail on the issues that were raised during the Committee hearings, this included information on:

    - the objects clause;
    - whether there would be an increase in red-tape due to other regulatory requirements;
    - the interaction between ACNC and the Australian Securities and Investments Commission (ASIC);
    - director liability;
    - 'likely' contraventions of the Act;
    - use of injunctions and the directions power;
    - external conduct standards and linkages with terrorism issues;
    - level of reporting thresholds;
    - preparation costs of financial reports;
    - deferral of reporting deadlines;
    - review and appeals framework;
    - consultation; and
    - independence from the ATO.

11. Detailed information on these issues is provided in the Supplementary Submission Treasury provided to the House of Representatives' Standing Committee on Economics, which is attached to this Submission.

Scope of this Submission

12. This Submission builds upon the evidence provided to the House of Representatives' Standing Committee on Economics.

13. Part one of this Submission provides an overview of the key changes that have been made to the ACNC legislation in line with the recommendations of the House of Representatives' Standing Committee on Economics.

14. Part two outlines the ACNC regulatory framework, and part three provides a detailed description of the ACNC legislation, including the consequential and transitional arrangements.

15. Part four provides an overview of the Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012.

16. Appendix A provides a summary table of the key changes to the ACNC Bills following House of Representatives' Standing Committee on Economics inquiry process.

PART ONE: OVERVIEW OF CHANGES

17. On 6 July 2012, the Government referred the draft ACNC legislation to the House of Representatives' Standing Committee on Economics, for an inquiry over the Winter Parliamentary break.

18. The Committee reported on 15 August 2012 and recommended the Bills be passed subject to a number of changes.

19. Changes have been made to the Bill, in accordance with the recommendations. The key changes are outlined below.

- A new clause has been added in the Bill's objects, to make clear the important role the ACNC will have in promoting a reduction in unnecessary regulatory obligations.

- Improvements have been made to ensure that registered entities have the opportunity to respond to compliance concerns, including the introduction of a requirement to issue 'show cause' notices unless the ACNC Commissioner, considering a number of legislated factors, believes that immediate enforcement action is necessary.

- A requirement has been introduced to provide that the ACNC Commissioner must not publish details of enforcement action on the Register for a period of time after the action is taken, unless it is in the public interest to do so earlier. This provides time for a registered entity to respond before such information is made publicly available. Such information entered on the Register will be removed after five years, unless the public interest requires that it be retained.

- A new regulatory power has been included in the Bill, to provide that the ACNC Commissioner must not include certain information on the Register in prescribed circumstances. The Government has announced its intention to make regulations to protect the privacy of private donors, such as those who maintain a private ancillary fund.

- The provisions of the Bill governing obligations, liabilities and offences of incorporated and unincorporated entities have been redrafted to give effect to the Committee's recommendations.

- These have been revised to remove any criminal liability for directors of incorporated charities. They now also make clear that where there is a non-criminal contravention of the Bill, a director of an incorporated charity is only liable for any amount payable by the body corporate where this arises from a

deliberate act or omission of the director involving dishonesty, gross negligence or recklessness.

- Additional detail has also been added to the explanatory memorandum to clarify the Commissioner's discretion regarding the issuing of administrative penalty notices.

- Transitional reporting arrangements have been included to allow the Commissioner to treat a statement, report or other document provided to another Government agency as meeting the reporting obligations of a particular registered entity under the ACNC reporting framework. This arrangement will apply until the 2014-15 financial year and can be extended by regulation.

- Consistent with the Committee's recommendation the legislation will be reviewed after five years.

20. A table outlining the changes to the Bill since the House of Representatives' Standing Committee on Economics inquiry is at Appendix A.

PART TWO: OVERVIEW OF THE ACNC REGULATORY FRAMEWORK

21. The ACNC legislation establishes a national regulator, the ACNC, and a national regulatory framework for the NFP sector. The Bill:

    - charges the ACNC with registering NFP entities and maintaining a register;

    - introduces a new national regulatory framework designed for NFPs;

    - provides for the powers of the Commissioner in relation to the regulation of registered entities; and

    - sets out the obligations and responsibilities of registered entities.

22. Initially, only tax endorsed charities will be regulated by the ACNC. However, the legislation establishes a regulatory framework that can be extended to all NFP entities in the future.

23. A national regulatory system that promotes good governance, accountability and transparency for NFP entities will help to maintain, protect and enhance the public trust and confidence that underpins the sector.

24. The ACNC will administer a new system of more effective and smarter regulation. The regulation will be proportional to the size of the NFP entity to minimise compliance costs, and to allow registered entities to focus on achieving their mission.

25. The Commissioner of the ACNC will cooperate with other government agencies to oversee a simplified and streamlined regulatory framework for NFP entities.

26. The Commissioner of the ACNC will also provide information to help the public understand the work of the NFP sector and the regulatory framework in which it operates and to improve the transparency and accountability of the sector. The educational role of the ACNC will help to improve public understanding of, and engagement with, the important work of the sector.

27. The establishment of a national regulatory system for NFP entities will provide significant benefits to the NFP sector over time by:

- reducing red tape and duplication by streamlining processes;
- reducing compliance burden by introducing a proportional regulatory system commensurate to the size of the NFP entity;
- improving public engagement with the NFP sector through a public information portal, and providing information to help the public understand the work of the sector;
- providing greater accountability and transparency, which will, in turn, maintain, protect and enhance trust and confidence in the sector; and
- providing information and guidance to the sector to assist registered entities to comply with their regulatory obligations and to fulfil their diverse and important goals.

28. The establishment of the ACNC will bring Australia into line with a number of other international jurisdictions that have established a regulator specifically for the NFP sector, in recognition of the uniqueness of the sector. Further detail and analysis of international regulatory models is available in Treasury's *Final Report on the Scoping Study for a National Not-for-profit Regulator*. [2]

29. The ACNC will be established as an independent statutory office structurally separate from the ATO. The Bill ensures the independence of the ACNC, for example, by requiring the ACNC to report directly to Parliament. The ACNC Bill also expressly provides that ACNC officers act independently of the ATO, such as when carrying out their duties under the ACNC legislation.

30. The structural separation will help to address any perceived conflicts of interest that currently exist with the ATO's revenue collection role and its current role as the default NFP regulator. This, in turn, will ensure that the public has confidence in the ACNC Commissioner's decision making processes.

31. On 17 May 2012, the Government announced that governance standards, external conduct standards and the financial reporting requirements will apply from 1 July 2013, which will enable further consultation on these issues. The Government has announced that these requirements will be developed in close consultation with stakeholders and will be released for public consultation in the coming months.

32. The delayed start dates will provide further time for consultation, give charities more time to transition to the new regulatory framework, and enable the ACNC to work with the sector to provide guidance and information to facilitate the transition to the new regime.

33. More detailed information about the ACNC legislation is included below under 'Detailed description of ACNC legislation'.

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[2] See Appendix A of the report, which can be accessed at: http://archive.treasury.gov.au/contentitem.asp?NavId=&ContentID=2054.

PART THREE: DETAILED DESCRIPTION OF THE ACNC LEGISLATION

The ACNC Bill

34. The ACNC Bill has three objects. Its first object is to maintain, protect and enhance the public trust and confidence in the NFP sector. Its second object is to support and sustain a robust, vibrant, independent and innovative NFP sector. The third object underlines the important role that the ACNC will have to promote the reduction of unnecessary regulatory obligations on the NFP sector.

35. The ACNC Commissioner will have the general administration of the ACNC Bill. In undertaking his or her role, the ACNC Commissioner will have regard to:

- the maintenance, protection and enhancement of public trust and confidence in the NFP sector;
- the need for transparency and accountability of the NFP sector to the public (including donors, members and volunteers) by ensuring the public has access to information about NFP entities;
- the benefits of providing information to the public about NFP entities;
- the maintenance and promotion of the effectiveness and sustainability of the sector;
- the upholding of principles relating to regulatory necessity, risk and proportionality;
- the need for cooperation with other Australian Government agencies and to administer effectively the laws that confer functions and powers on the Commissioner, including the minimisation of procedural requirements and duplication;
- the benefits derived from assisting NFP entities with their obligations under the legislation, including through the provision of education and guidance to NFP entities; and
- the nature and diversity of the NFP sector.

36. Below is a summary of the key elements of the draft legislation.

Registration and deregistration

37. The Bill provides the ACNC Commissioner with the power to register NFP entities under their specific charitable type or subtype. In the first instance, registration with the ACNC is limited to charities. However, the ACNC's role is expected to expand over time to include all NFPs.

38. Registration is voluntary. However, entities will need to be registered to access government support in the form of concessions, exemptions and other benefits. There are also other benefits to being registered, including having a web presence, and the ability for the public to more easily find out information about the entity.

39. Transitional rules apply in relation to charities that are endorsed by the ATO, ensuring a smooth transition to the ACNC.

40. The Bill sets out the processes and grounds for the revocation of registration by the Commissioner (for example, where the entity's application for registration was false and misleading, where a liquidator has been appointed, or where the entity has, or is more likely than not to, contravene the Act, or a governance or external conduct standard).

41. The Bill also sets out requirements for the issuance of show cause notices and for the Commissioner to take account of a range of matters before deciding to revoke the registration of an entity. These matters require the Commissioner to weigh a number of factors, including whether other actions could be taken to remedy compliance problems and the welfare of recipients of charitable services.

Register

42. The ACNC Commissioner will maintain a public register, containing key details about registered entities including contact details, the type of registration, information statements and, for certain charities, financial reports. The register will also include details of any warnings, directions, undertakings, injunctions, and any suspension or removal of responsible entities, including a summary of why the matter arose and details of any resolution or response to the matter.

43. The Bill provides that certain types of information (including, where the information is commercially sensitive, inaccurate, or likely to confuse or mislead the public) may not be published on the register, subject to a public interest test.

44. The Bill also provides a regulation making power, which allows for regulations to be made which address other classes of information, for example, circumstances in which the publication of the information may affect the privacy of philanthropic donors.

45. The public information portal has been modelled on similar portals established in England and Wales, New Zealand, Scotland, the United States and Canada.

Governance standards and external conduct standards

46. Registered entities will need to comply with a set of minimum principles-based governance standards covering matters such as the content of the entity's governing rules, the conduct of entity, and the processes that entities have in place. Compliance with the governance standards is a condition of registration. Registered entities will also need to comply with external conduct standards.

47. The purpose of the governance standards is to establish a set of minimum governance standards for a NFP entity, with the aim of removing the existing uncoordinated, duplicative and ad hoc governance requirements that currently apply to the NFP sector.

48. The purpose of the external conduct standards is to promote transparency and provide confidence across the sector and the general public that charitable funds and services are applied for legitimate purposes, and are not contributing to terrorist or other criminal activities.

49. The external conduct standards are expected to be based on the requirements of the Financial Action Task Force's (FATF) Special Recommendation VIII (SR VIII). The FATF is an inter-governmental body established in 1989 to promote measures for combatting money laundering, terrorist financing and related threats to the integrity of the international financial system.

50. As a member of the FATF, Australia has agreed to comply with the FATF recommendations. FATF SR VIII requires FATF members to 'combat the misuse of NPOs (non-profit organisations, that is, NFP entities) for the purpose of terrorism financing'. In FATF's last review of Australia's progress in 2005, it found that Australia was only partially compliant with SR VIII.

51. In May 2012, the Government announced that the governance standards and external conduct standards would be set out in regulations, which would be subject to further consultation. This consultation process will commence in the coming months. The governance and external conduct standards will commence from 1 July 2013. The regulations will be statutory instruments, disallowable by Parliament.

Reporting thresholds and reporting requirements

52. The Bill establishes a single reporting framework, which is proportional to the size of the registered entity, based on revenue thresholds. The differential reporting framework will minimise compliance costs, whilst ensuring appropriate levels of accountability and transparency.

53. The thresholds for reporting purposes are as follows:

- small entities — revenue of less than $250,000;
- medium entities — revenue of between $250,000 and less than $1 million; and
- large entities — revenue of $1 million or more.

54. The legislation includes a regulation making power which allows for the thresholds to be changed over time.

Financial reports

55. Small entities will not have to provide financial reports. Medium entities will have to provide financial reports which can be reviewed rather than subject to a full audit. Large entities will have to provide audited financial reports.

56. In May 2012, the Government announced that the detailed content requirements of the financial report would be set out in regulations, which would be subject to further consultation, which as noted above, will commence in the coming months. Charities will be required to prepare their first reports for the 2013-14 financial year. As a result, the first financial report will need to be lodged with the ACNC by 31 December 2014, or six months after the end of a substituted accounting period that commences after 1 July 2013.

57. Registered entities that notify the ACNC Commissioner, within six months of the commencement date, that they currently report under an Australian law using a substituted accounting period, will be taken to have been approved by the ACNC Commissioner (on an ongoing basis) to lodge their financial report to the ACNC on the basis of that other period. That is, existing substituted accounting periods will be grandfathered for such entities, and the ACNC Commissioner's approval to adopt the alternate accounting period will not be required in these cases.

Annual information statements

58. All registered entities will be required to provide an annual information statement in the approved form. This could include information relating to governance, finances, activities, purposes and or beneficiaries. The information statement will be

proportional, with the Commissioner able to approve different forms for small, medium and large registered entities.

59. The first annual information statement will relate to the 2012-13 financial year. As a result, the first information statement will need to be lodged with the ACNC by 31 December 2013, or six months after the end of a substituted accounting period that commences after 1 July 2012.

60. Further detail about the annual information statement is provided in the ACNC Implementation Report.[3]

Practical impact of reporting tiers

61. Based on ATO data, the majority of registered entities will fall into the small tier (see table below).

Table 2: Size of Australian charities within various tier thresholds (as at 24 June 2012)

Tier	Charity population %	Cumulative total %
Small registered entity Revenue up to $250,000	**78**	**78**
Medium registered entity Revenue between $250,000 & $1 million	**11**	**89**
Large registered entity Revenue greater than $1 million	**11**	**100**

Source: Based on ATO data

62. In practical terms, as the majority of entities will fall within the small tier, they will benefit from reporting and auditing exemptions, simplified annual information statements, as well as longer timeframes to notify the ACNC of various matters.

63. Medium entities will also benefit from simplified auditing requirements and simplified annual information statements. Many medium and large entities, particularly companies limited by guarantee, will benefit from a further reduction in reporting burden, as they will no longer need to prepare a directors' report as currently required by the *Corporations Act 2001* (Corporations Act).

64. Some stakeholders commented on the level of the tiers, and expressed the view that they should be increased. However, increasing the thresholds would create inconsistencies at the Commonwealth level, as well as at the State and Territory level.

65. The revenue thresholds adopted in the ACNC legislation are based on the same revenue thresholds contained in the Corporations Act for companies limited by guarantee. These thresholds were developed following extensive consultation, including consultation undertaken as part of a Treasury discussion paper entitled 'Financial Reporting by Unlisted Public Companies' released in June 2007.

Duty to notify

66. Registered entities will be required to notify the Commissioner of certain matters, for example, changes to its contact details, any significant contraventions of the Act or

3 The report can be accessed at: http://acnctaskforce.treasury.gov.au/content/Content.aspx?doc=publications/implementationreport/html/index.htm.

governance standards that would mean the entity is no longer entitled to registration.

67. This will ensure that the public register remains up-to-date and can be relied upon by the public. The duty to notify is based on similar provisions contained in the *Taxation Administration Act 1953* (TAA) for endorsed charities, but with less severe penalties for any breaches of the duty. Similar provisions are also contained in the Corporations Act.

Regulatory powers of the ACNC

68. The Bill provides the ACNC Commissioner with the regulatory powers it requires to fulfil its responsibilities. These powers are based on the powers of existing regulators, including the ATO and ASIC.

69. There are a range of powers and sanctions available to the ACNC Commissioner, to enable the Commissioner to respond appropriately to the facts of each case. These powers are intended to be used to allow the ACNC Commissioner to conduct regulatory oversight in an effective manner, and to actively monitor on-going eligibility for registration.

70. In the first instance, the ACNC will rely on education, rather than its enforcement powers, to encourage compliance with the new provisions. This approach was outlined recently in the ACNC Implementation Report.[4] The ACNC's educative role will include providing assistance and support to the sector on technical matters, and assisting the sector during the transition to the new regulatory environment.

71. In more serious cases of non-compliance, the type of enforcement power used by the Commissioner will be determined by the kinds of actions which are required to address the contravention or non-compliance.

72. Where guidance and education have not resolved the issue, there will be some cases where all that will be required is the issuance of a warning notice to encourage self-correction, however, in other cases where an entity has persistently failed to meet regulatory obligations, or committed a very serious contravention such as fraud, the Commissioner may need to remove a responsible entity.

73. The legislation provides the Commissioner, or their delegate, with the following powers to use at their discretion following the meeting of a number of preconditions:

- gathering information, monitoring activities and inquiring about matters relating to general compliance with, or potential breaches, of the provisions of the new laws. An ACNC officer may enter premises for the purpose of monitoring, with the occupier's consent or under a monitoring warrant;

- giving a registered entity a warning notice or a direction if the Commissioner reasonably believes the entity has, or is more likely than not to, contravene the Act, governance standards, or external conduct standards;

- accepting enforceable undertakings from registered entities to comply with the Act, governance standards or external conduct standards;

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4 The report can be accessed at: http://acnctaskforce.treasury.gov.au/content/Content.aspx?doc=publications/implementationreport/html/index.htm.

- applying for injunctions to restrain registered entities from contravening the Act, or to compel compliance with the Act; and

- suspending or removing a responsible entity of a registered entity (following a show cause notice), if the Commissioner reasonably believes that the registered entity has, or is more likely than not to, contravene the Act, governance or external conduct standards. The Commissioner may appoint acting responsible entities, subject to certain limitations, to enable the registered entity to continue to function.

74. In order to ensure the accuracy of information provided to the ACNC, and to provide a remedy where entities provide misleading information or fail to provide information to the ACNC, the Bill provides an administrative penalty regime, consistent with the TAA. This regime is based on the level of culpability of the entity, as well as their subsequent actions. For example, an entity that makes an innocent mistake is likely to be relieved of any penalty, but an entity that intentionally disregards the law and then attempts to prevent the ACNC from finding out is likely to be more harshly penalised.

The Advisory Board

75. The Bill establishes the Advisory Board, to provide advice and make recommendations to the Commissioner in relation to the Commissioner's functions under the Act. The Advisory Board will consist of two to eight general members, appointed by the Minister. Collectively, the general Advisory Board members must have expertise relating to charities and NFP entities, or experience and appropriate qualifications in law, taxation or accounting.

Secrecy

76. The Bill establishes a secrecy framework to ensure that where the Commissioner and ACNC officers have access to personal or confidential information in the ordinary course of performing their duties, they are subject to a general prohibition on the use and disclosure of that information.

77. However, to ensure the ACNC is able to fulfil its functions under the Bill, including promoting good governance, transparency and accountability, disclosure of the protected information is permitted in specified circumstances.

78. In administering the secrecy framework, the ACNC will adopt a coordinated and cooperative approach with other relevant authorities, consistent with the ACNC's function as a 'one-stop shop' regulator.

Review and appeals

79. The Bill sets out the process for an entity to challenge all core decisions of the ACNC Commissioner if they are dissatisfied with the Commissioner's decision. An entity that is directly affected by the decision will be able to utilise full merits based review and appeal rights in respect to the decision of the Commissioner.

80. The remaining non-core decisions made by the ACNC Commissioner will not be subject to a merits based review, but will be subject to review under the *Administrative Decisions (Judicial Review) Act 1977*.

81. The Bill provides for the combination of multiple reviews and appeals to minimise compliance costs.

Obligations of responsible entities

82. The Bill imposes certain obligations, liabilities or offences on certain entities that are responsible for managing entities. This ensures that certain responsible entities are accountable for fulfilling the obligations contained in the Bill. This is particularly important in the case of entities that do not have legal personality, such as unincorporated associations and trusts, as they cannot themselves be sued or penalised.

83. In respect of unincorporated associations and trusts, the framework contained in the ACNC legislation is based on the existing framework in the TAA.

84. In contrast, a body corporate does have separate legal personality, and can be sued or penalised. For this reason, the Bill sets out a more streamlined and targeted framework for attaching personal liability to directors of a body corporate. The directors of the body corporate are not personally liable for any offences contained in the Bill. In the case of a non-criminal contravention of the Bill, directors will only be personally liable for the liabilities of the body corporate in certain limited cases, for example, if there is a deliberate act involving dishonesty on their part.

The ACNC (Consequential and Transitional) Bill 2012

Transitional provisions

85. The transitional provisions provide a smooth transition to the new framework. For example, transitional provisions:

    - provide for the automatic registration of charities that are endorsed by the ATO unless the entity opts out within six months. Where entities are endorsed by the ATO as a specific subtype of charity (including public benevolent institution) the ACNC will register these entities under their subtype;

    - grandfather existing substituted accounting periods applying to entities in certain cases; and

    - allow the Tax Commissioner to pass on certain information to the ACNC Commissioner to populate the Register, and allow this information to be made public.

86. The transitional provisions allow the ACNC Commissioner to treat a statement, report or other document given under an Australian law to an Australian government agency (other than the Commissioner) by a registered entity as being an information statement or a financial report for a financial year given to the Commissioner under the ACNC Bill.

87. This enables the ACNC Commissioner to address potential reporting duplication during the process of establishing the ACNC as a 'one-stop shop' regulator and operates at least until the 2014-15 financial year.

88. The non-government schools sector and charitable Indigenous corporations would be examples of classes of entity that are intended to benefit from the exercise of the discretion of the ACNC Commissioner.

89. These transitional provisions also provide for a statutory review of the operation of the ACNC regulatory framework to be undertaken after five years of operation.

Consequential amendments

90. As announced during the 2011-12 Budget, the ACNC will be a 'one-stop shop' regulator for the NFP sector. The ACNC's initial responsibilities will include:

- determining the legal status of entities seeking charitable status, including public benevolent institution status, on behalf of all Commonwealth agencies;
- registering entities under their charitable status; and
- administering a new system of smarter regulation which will be proportional to size and risk, and minimise any regulatory duplication.

91. The consequential amendments enable the ACNC to determine the charitable status of entities on behalf of all Commonwealth agencies; to minimise any regulatory duplication which may exist at the Commonwealth level; and to cater for the establishment and integration of the ACNC into the Commonwealth Government.

92. Charities receive concessions, exemptions and benefits from the Commonwealth Government in recognition of the public benefit they provide. Commonwealth concessions, exemptions and benefits usually appear in Commonwealth Acts.

93. To access the numerous concessions, exemptions and benefits, entities have to satisfy the Commonwealth agency which administers these Acts that they are charities within the common law definition of the term.

94. Providing the ACNC with a central registration function will ensure that entities have to apply for charitable status on a single occasion. This will ultimately reduce the compliance cost and regulatory burden faced by NFP entities, and the administrative burden on the Commonwealth Government.

95. To ensure the ACNC's registration applies across all Commonwealth agencies, consequential amendments to Commonwealth Acts which provide charities with concessions, exemptions and benefits were made. A large share of consequential amendments included in the ACNC Consequential and Transitional Bill require charities to be registered by the ACNC under their charitable status, as a precondition to accessing the concessions, exemptions and benefits.

96. The amendments to Division 30 of the *Income Tax Assessment Act 1997*, Division 50 of the *Income Tax Assessment Act 1997*, to the *Competition and Consumer Act 2010* and the *Do Not Call Register Act 2006* are all examples of this type of amendment.

97. In specific cases where Commonwealth concessions, exemptions and benefits are earmarked for a particular subtype of charity, amendments require ACNC registration as a particular subtype.

98. The amendments to the *Fringe Benefits Tax Assessment Act 1986*, the *A New Tax System (Goods and Services Tax) Act 1999*, and certain items of Division 30 of the *Income Tax Assessment Act 1997* are all examples of this type of amendment.

99. The ACNC Consequential and Transitional Bill also makes consequential amendments to Commonwealth legislation to cater for the establishment of the ACNC and ensure the smooth transition of the ACNC into the Commonwealth Government.

100. For example, these amendments eliminate the need for the Australian Securities and Investments Commission (ASIC) to continue to regulate NFP entities that are

incorporated under the Corporations Act, and ensure that the ACNC has the legal infrastructure required to function effectively, for example to enable the ACNC to share information with other regulators. The amendments to the Corporations Act are discussed in more detail below.

101. Consequential legislative amendments also remove instances of direct regulatory duplication. These include, for example, amendments to the *A New Tax System (Family Assistance) (Administration) Act 1999*, the *Aged Care Act 1997*, and the Corporations Act.

102. Treasury liaised with numerous Australian government agencies when finalising the consequential amendments, including with State and Territory Governments through the Legislative and Governance Forum for Corporations (previously known as the Ministerial Council for Corporations).

103. In order to move towards the long-term objective of a truly national regulatory system, the Commonwealth will continue work with the States and Territories on a national regulatory framework.

104. This work is being progressed by the NFP Reform Working Group (NRWG) of COAG. Further information about the NRWG's work is provided in Treasury's submission to the House of Representatives' Standing Committee on Economics inquiry into the draft ACNC legislation.

Amendments relating to the interaction between ASIC and the ACNC

105. The ACNC Consequential and Transitional Bill clarifies the responsibilities of ASIC and the ACNC, as entities registered with the ACNC will be primarily regulated by the ACNC, rather than ASIC, in relation to the day to day activities of the registered entity.

106. Under the new regime, ASIC will continue to register companies, including companies limited by guarantee, but will have limited oversight of the financial reporting and governance arrangements of those companies that choose to register with the ACNC, as oversight of these arrangements will be performed by the ACNC.

107. Currently, ASIC conducts surveillance of financial reports prepared by companies, registered schemes and disclosing entities, and their compliance with Part 2M.3 of the Corporations Act. ASIC will not continue to be responsible for financial reporting surveillance in respect of entities registered with the ACNC from 1 July 2013, as this function will instead be performed by the ACNC.

108. As part of consequential amendments to the *Australian Securities and Investments Act 2001*, ASIC will retain the power to obtain information in respect of ACNC audits.

109. ASIC will also continue its current oversight role with respect to external administration processes, such as liquidations and administrations, undertaken under the Corporations Act.

110. The consequential amendments will also remove duplication by turning off the following requirements in the Corporations Act for entities registered with the ACNC:

- the requirement for entities to notify ASIC of various matters, such as changes to its address or its directors, as these notifications will now be provided to the ACNC, as part of its 'one-stop shop' function;

- certain director's duties for entities registered with the ACNC, as under the new regime, the responsible entities will be subject to equivalent governance standards that will be specifically tailored for the NFP sector. These governance standards will be set out in regulations that will commence on 1 July 2013;

- the financial reporting requirements in the Corporations Act, as these requirements are contained under the draft ACNC legislation. Further detail about the content of financial reports will be set out in the regulations that will commence on 1 July 2013; and

- the procedural requirements relating to the conduct of Annual General Meetings, as an equivalent procedure, which will be simplified and tailored for the NFP sector, will be set out in regulations that will commence on 1 July 2013.

111. A regulation making power will enable other provisions of the Corporations Act to be turned off in respect of registered entities. This regulation making power provides a mechanism which allows any duplication in the Corporations Act to be addressed, as a result of future reporting and governance standards that will be developed following consultation and will commence from 1 July 2013.

PART FOUR: TAX LAWS AMENDMENT (SPECIAL CONDITIONS FOR NOT-FOR-PROFIT CONCESSIONS) BILL 2012

Overview of the Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012

112. The Government announced in the 2009-10 Budget that it would amend the 'in Australia' special conditions in Division 50 of the *Income Tax Assessment Act 1997* to ensure that Parliament retains the ability to fully scrutinise those organisations seeking to pass money to overseas charities and other entities.

113. The announcement was prompted by a High Court decision which held that charities may be pursuing their objectives principally 'in Australia' where they merely pass funds within Australia to another charitable institution that conducts its activities overseas.

114. This finding was inconsistent with the Commissioner of Taxation's interpretation and with the clear policy intent underlying the special conditions. Prior to the High Court's decision a charitable institution needed to meet two requirements to be exempt from income tax: first, it must have a physical presence in Australia and, second, to the extent it has a physical presence in Australia, it must incur its expenditure and pursue its objectives principally in Australia.

115. Traditionally, entities cannot be income tax exempt unless they are operated principally in Australia, are prescribed as exempt in the *Income Tax Assessment Regulations 1997* or are a deductible gift recipient (DGR). While both income tax exempt entities and DGRs are subject to 'in Australia' special conditions, they are subject to different thresholds.

116. The publicly funded taxpayer concession was primarily meant to be used principally in Australia for the broad benefit of Australians, and not be passed on through entities and then spent overseas. In addition, where money is sent overseas there is an increased risk of the funds being misdirected to inappropriate and unauthorised operations, such as money laundering and terrorist financing.

117. The Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012:

- re-states the 'in Australia' special conditions for income tax exempt entities, ensuring that they generally must be operated principally in Australia and for the broad benefit of the Australian community (with some exceptions);
- standardises the other special conditions entities must meet to be income tax exempt, such as complying with all the substantive requirements in their governing rules and being a 'not-for-profit' entity (with some exceptions);
- standardises the term 'not-for-profit', replacing the defined and undefined uses of 'non-profit' throughout the tax laws; and
- codifies the 'in Australia' special conditions for DGRs ensuring that they must generally operate solely in Australia, and pursue their purposes solely in Australia (with some exceptions, such as overseas aid funds and some environmental organisations).

118. There are a number of exceptions to the application of special conditions in the case of DGRs, allowing certain organisations to undertake overseas activities. These include:

- those under the category of 'international affairs', including overseas aid funds approved by the Overseas Aid Gift Deductibility Scheme (OAGDS); and
- those on the Register of Environmental Organisations, which the Secretary of the Environment Department authorises as being exempt from the 'in Australia' special conditions.

119. These schemes are an exception to the longstanding policy of successive governments that DGRs should operate only in Australia, for the benefit of the Australian public. The Government recognises that although organisations in this category are not operating in Australia, it is considered that helping these overseas aid objectives contributes to providing a broad public benefit to Australia.

120. Restating the 'in Australia' special conditions will provide support to the anti-avoidance measures in the tax law which limit income tax exempt entities expending money offshore and ensure tax supported funds remain in Australia.

121. As a member of the Financial Action Task Force (FATF) (an inter-governmental body dedicated to combating money laundering and terrorist financing), Australia has agreed to comply with FATF recommendations. FATF Special Recommendation VIII (SR VIII) requires FATF members to 'combat the misuse of NPOs (non-profit organisations, that is, not-for-profit organisations) for the purpose of terrorism financing'. In FATF's last review of Australia's progress, it found that Australia was only partially compliant with SR VIII.

122. The 'in Australia' special conditions provide additional measures to address possible abuse of not-for-profit entities for the purposes of money laundering and terrorist financing, and ensure the proper operation of not-for-profit entities, their use of public donations and funds, and the protection of their assets. By limiting the use of monies to specified areas, in conjunction with greater regulatory requirements, this ensures those monies are expended appropriately and in a manner consistent with the eligibility for tax concession status.

123. The Bill will help maintain a sustainable and certain tax system.

Consultation

124. The Government has consulted extensively on the Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012.

125. The Government issued two public exposure drafts on 4 July 2011 and 17 April 2012 and has revised the amendments in response to stakeholder feedback.

Main changes from the first exposure draft

126. Public consultation on the draft legislation and explanatory materials was conducted between 4 July 2011 and 12 August 2011. Following a first round of consultation, the Government made changes to the Bill in response to sector feedback.

127. The exemption from the 'in Australia' special conditions for DGRs was expanded to allow for certain environmental organisations to operate overseas, subject to certain integrity requirements.

128. The 'in Australia' special conditions were altered so that an entity may give money or property (to further its purpose) to another entity that is not entitled to be income tax exempt, however the use of those funds by those other entities should be taken into account when determining whether or not the entity giving the money has met the 'in Australia' special conditions.

129. The 'in Australia' special conditions that apply to DGRs were altered so that if a deductible gift recipient gives property or benefits to a non-deductible gift recipient entity to further its purpose, the spending of the entity's funds should be taken into account when determining whether or not that entity meets the 'in Australia' special conditions for DGRs.

130. An income tax exempt entity will be allowed to disregard the spending of government grants and non-tax deductible donations when applying the 'in Australia' special conditions, but only in cases where the entity demonstrates adherence to some basic governance principles (to be set out in the regulations) about how they operate overseas.

131. It was made clear that the deductible gift recipient rules only apply to an entity to the extent it is a deductible gift recipient. The more lenient tests (within the income tax exemption rules) apply to the other operations of the entity.

132. Entities that are currently prescribed in the regulations under section 50-50 of the *Income Tax Assessment Act 1997* have been grandfathered, and are therefore unaffected by the changes to the 'in Australia' special conditions. In addition, the existing prescription process has been maintained.

133. It was made clear that an entity must comply with only the substantive governing rules (e.g., those setting out an entity's purpose and not-for-profit status) to maintain a tax exemption, and that the Australian Taxation Office would not be expected to remove an entity's tax exemption for a minor and insignificant breach of its governing rules.

134. The definition of 'not-for-profit' was rewritten, and now expressly allows transfers of profits or assets between not-for-profit entities with similar purposes, as well as payments for genuine compensation for services provided to, or reasonable expenses incurred on behalf of, the not-for-profit.

135. Further detail was added to the explanatory materials to clarify areas of uncertainty raised during the consultation process.

Main changes from the second exposure draft

136. A further round of public consultation on a revised exposure draft and explanatory materials was held between 17 April and 11 May 2012. In response to sector feedback, some further changes were made to the Bill.

137. The Bill was revised to provide more clarity in the case of organisations such as public benevolent institutions, which may operate a fund that is exempt from the special conditions. The bill will not remove whole-of-entity PBI status for organisations that have a fund approved to operate overseas. The organisation would only need to consider its other operations (ignoring the approved overseas component) when assessing its activities against the special conditions.

138. The Bill was revised to provide a regulation-making power to allow certain medical research institutions to be listed in the regulations, reflecting that medical research is

an activity dependent on international collaboration. Listed medical research institutes will still be required to be established in Australia, but will be exempt from the remainder of the 'in Australia' special conditions. A review will be undertaken within three years to examine options for the development of a permanent DGR category for medical research institutions that undertake a significant part of their activities overseas.

139. Some arts organisations undertake activities overseas. In many cases, these overseas activities are merely incidental to the operation and pursuit of the entity's purposes in Australia, or the overseas activities are minor in extent and importance when considered with reference to the operations and pursuit of the entity's Australian activities. In these circumstances, their DGR status will be retained. Examples have been provided in the Explanatory Memorandum to provide clarity on this issue.

140. The Bill was revised to provide that the Australian Chamber Orchestra Pty Ltd and the Sydney Dance Company be listed in the 'international affairs category', and exempt from the 'in Australia' special conditions, provided their overseas activities remain under 25 per cent of their overall activities. These organisations are designated international touring organisations.

APPENDIX A — SUMMARY TABLE - CHANGES TO THE ACNC LEGISLATION

Changes to the ACNC Bills following House of Representatives' Standing Committee on Economics inquiry

Section of the Bill or Explanatory Memorandum	Reference	Committee recommendation	Change
Objects	ACNC Bill — Paragraph 15-5(1)(c)	Recommendation 1	A new object of the Act has been added to make clear the important role the ACNC will have in promoting the reduction of unnecessary regulatory obligations on the Australian not-for-profit sector.
Objects and Guide	ACNC Bill — Section 10-5 Explanatory Memorandum — Paragraphs: 1.85 to 1.99	Recommendation 2	The guide material has been altered so that it reflects that the Commissioner will support the transparency and accountability of the sector. The explanatory materials have been added to, in order to better explain the operation of elements of the objects clause.
Registration provisions and enforcement powers	ACNC Bill — Sections 35-15, 100-10 and 100-15	Recommendation 7	Improvements have been made to ensure that registered entities have the opportunity to respond to compliance concerns, including extending the requirements to issue 'show cause' notices unless the ACNC Commissioner, considering a number of factors, believes that immediate enforcement action is necessary. These changes ensure greater procedural fairness for registered entities, while also providing the Commissioner with the discretion to revoke registration or suspend or remove a responsible entity without giving the entity a show cause notice in appropriate circumstances
Governance standards	Explanatory Memorandum — Paragraphs: 5.37 to	Recommendation 4	Material has been added to the explanatory materials to explain that sector-developed codes of conduct for certain

Section of the Bill or Explanatory Memorandum	Reference	Committee recommendation	Change
	5.42		entities can be endorsed as part of the governance standards.
The Register	ACNC Bill — Subsection 40-5(2)	Recommendation 8	A requirement has been introduced to provide that the ACNC Commissioner must not publish details of enforcement action on the Register for a period of at least 14 days, unless it is in the public interest to do so earlier. This provides time for a registered entity to respond before such information is made publicly available. Such information entered on the Register will be removed after five years, unless the public interest requires that it be retained.
The Register	ACNC Bill — section 40-10(1)	Recommendation 5	A new regulatory power has been included in the Bill, to provide that the ACNC Commissioner must not include certain information on the Register in prescribed circumstances. This will allow regulations to be made to protect the privacy of private donors, such as those who maintain a private ancillary fund.
Obligations, liabilities and offences	ACNC Bill — Division 180	Recommendation 6	The provisions of the Bill governing obligations, liabilities and offences of incorporated and unincorporated entities have been redrafted to give effect to the Committee's recommendations. These have been revised to remove any criminal liability for directors of incorporated charities. They now also make clear that where there is a non-criminal contravention of the Bill, a director of an incorporated charity is only liable for any amount payable by the body corporate where this arises from a deliberate act or omission of the director involving dishonesty, gross negligence or recklessness.
Administrative penalties	Explanatory Memorandum	Recommendation 9	Additional detail has also been added to the explanatory memorandum to clarify the Commissioner's discretion

Section of the Bill or Explanatory Memorandum	Reference	Committee recommendation	Change
	— Paragraphs 13.137 to 13.162		regarding the issuing of administrative penalty notices.
Transitional reporting arrangements	Schedule 1, subitem 10 of the Consequential and Transitional Bill	Recommendation 3	Transitional reporting arrangements have been included to allow the Commissioner to treat a statement, report or other document provided to another Australian Government agency as meeting the financial reporting obligations of a particular registered entity under the ACNC Act. This arrangement will apply until the 2014-15 financial year and can be extended by regulation.
Statutory review	Schedule 1, subitem 16 of the Consequential and Transitional Bill	Recommendation 10	Consistent with the Committee's recommendation the legislation will be reviewed after five years.