

NOT-FOR-PROFIT NEWSLETTER

NEWSLETTER DATE: OCTOBER 2014

CHARITIES' GOVERNANCE ISSUES

INSIDE THIS ISSUE:

CHARITIES' GOVERNANCE	2
ACNC ACTIVITIES	3
FINANCIAL REPORTING INSIGHTS	4
ACNC'S FUTURE IN FOCUS	6

ATO's draft ruling on special conditions

The Australian Taxation Office (ATO) has released draft ruling TR 2015/D5: 'Income tax: special conditions for various entities whose ordinary and statutory income is exempt'.

The conditions require that an entity must comply with all the important demands of its governing rules (Governing Rules Condition).

The ruling also stresses that charities must use their income and assets solely for the purpose for which they have been set up (Income and Assets Condition). Three questions must be considered to determine whether a not-for-profit entity satisfies these conditions:

- What are the charity's 'governing rules'?
- What are the 'substantive requirements' in the entity's governing rules?
- Has the charity complied with all of these in its governing rules?

The ruling applies to some, but not all, income-tax-exempt entities that are listed at Section 50 of the Income Tax Assessment Act 1997 (ITAA).

These bodies must satisfy special conditions applicable to the relevant item for their ordinary and statutory income to be exempt from income tax.

Income-tax-exempt entities should

- review their governing rules
- identify their 'substantive requirements'
- assess whether the requirements are being complied with
- assess whether income and assets are being applied solely for the purpose for which the

entity is established.

If a breach or misapplication is identified, the income-tax-exempt entities should immediately take steps to fix it. You might have to notify the Commissioner of Taxation.

When a final ruling is issued, it will apply both before and after its date of issue.

Curtin Charities 2013 Report – a comprehensive picture of the sector

The *Curtin Charities 2013 Report* gives the first comprehensive, evidence-based analysis of Australian charities, revealing previously unknown facts about the sector.

Written by the Curtin University Not-for-profit Initiative, it analysed data from more than 38,000 charities registered with the Australian Charities and Not-for-profits Commission (ACNC).

Variety in the sector's activities and beneficiaries is remarkable, and it is believed that most of the regulatory burden is felt by a minority of charities.

Australian charities employ nearly a million people. Ten per cent of them employ more than 90 per cent of workforce. Another two million volunteers work for no fees. The sector has a total income of more than \$100 billion, and the report revealed that the sector had grown by 2 per cent annually since 1990.

The analysis was drawn from 38,341 Annual Information Statements submitted by charities in their first year of reporting to the ACNC (up to 30 June 2014). It provided the first single-source, evidence-based research into the charity sector.

Almost 70 per cent of charities

worked in one or more areas other than their primary pursuit.

A 10th of the charities administered about 80 per cent of the total number of staff and volunteers employed in the sector. A 10th also accounted for 90 per cent of the sector's full-time jobs and almost \$90 billion of its income.

A staggering 75 per cent of smaller charities do not employ full-time staff.

The report is invaluable for anyone – members of the general public, charitable organisations, researchers and policy makers – wanting to understand more about the sector.

Red tape for charities is in funding agreements

Commonwealth funding-agreement obligations are imposing a greater burden on charities than legislative obligations, a study into the ACNC's regulatory duties has found. The report *Research into Commonwealth Regulatory and Reporting Burdens on the Charity Sector* by Ernst & Young (EY), demonstrated that there was significant scope for improvement of the regulatory and reporting environment faced by charities and not-for-profit organisations.

It concluded that of the key sources of regulatory and reporting obligations faced by charities, fulfilling Commonwealth funding agreements imposed a far greater burden than legislative requirements. It recommended that Commonwealth funding agencies and departments ensure that their reporting and acquittal requirements align with the Commonwealth Grants Rules and Guidelines. It urged them to use key tools to reduce red tape, such as the ACNC's Charity Passport and

CHARITIES' GOVERNANCE ISSUES (CONTINUED)

National Standard Chart of Accounts (NSCOA).

EY estimated that the Commonwealth reporting burden on the 15 case-study charities had an average cost of \$108,000 for the 2012-13 year – between \$27,000 and \$38,000 constituted the expense of complying with red tape. The average Commonwealth burden cost small charities (charities with revenue less than \$250,000 a year) \$18,000 a year, and the counterpart figure for big charities (charities with revenue over \$1 million a year) was \$235,000. EY estimated that the average annual burden imposed by ACNC reporting obligations was \$150, or 0.1 per cent of total annual burden. EY defined 'red tape' as regulatory and reporting obligations that are excessive, unnecessary or confusing. The report estimated that 25 to 35 per cent of Commonwealth obligations constituted red tape, funding-agreement obligations being the key source.

The report said that 'red tape' included having to report too often and provide excessive information. When entities reported on multiple programs they were required to provide duplicate information to different government levels. Governments made different financial-reporting demands and required differing reporting processes, and there were inconsistencies in regulatory frameworks across states and territories.

The Commonwealth's burden on charities made it harder for them to achieve their aims. It concluded that the ACNC should consider adopting an 'honest-broker' role to drive government reforms that would reduce charities' burdens.

The ACNC minimises its own regulatory requirements and

supports robust innovation. It also works with other agencies to reduce unnecessary and duplicative administrative requirements under the principle of 'report once, use often'.

Warning for charities operating overseas

Overseas-aid charities need to protect themselves from vulnerability to criminal activity, including money-laundering and financing terrorism, the ACNC has advised. About 6,100 registered Australian charities on the ACNC register say that they have charitable purposes and activities overseas.

The ACNC Act has a specific provision, requiring the regulator to consider whether charities are engaging in or supporting, terrorist or other criminal activities. Every registration application the ACNC receives is checked carefully against lists by government agencies.

If they fail to have appropriate safeguards and processes in place, all charities are vulnerable to fraud and theft regardless of where their charitable activities are carried out. However, charities may be at greater risk when sending money overseas. Funds can be diverted or misused for criminal activities, money laundering and financing terrorism. The ACNC advised that the simplest way to avoid a misuse of funds is for charities to 'follow the money' to ensure that they are not duped or become complicit. Charities should also be aware of their legal obligations when providing financial aid overseas, particularly in countries where there is conflict and civil unrest.

Charities' obligations monitored

The ACNC has provided an overview of the role taken by a compliance team in response to concerns about charities meeting their obligations under the

ACNC Act. More information can be found on the ACNC website under, [areas of concern for charity regulation](#).

Generally, the public alerts the ACNC to concerns about charities. Charities' regular reporting and referrals from other agencies also sometimes reveal concerns about activities. The compliance team is responsible for ensuring that charities meet their obligations under the ACNC Act and its governance standards.

The team considers whether any intervention is necessary and in serious cases intervenes and conducts either a compliance review (to review a charity's general level of compliance with the Act and address any risks identified) or an investigation (for higher-risk and more complex cases).

Governance standards reminder

Since 1 July 2013, there are new governance standards that apply to charities registered with the ACNC. These standards set out a minimum standard of governance, including requiring registered charities to be accountable to their members and to ensure that their governing bodies ('responsible entities') under the ACNC Act of what the ACNC calls 'responsible persons' comply with the duties outlined in the governance standards specifically tailored for the not-for-profit sector.



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ACNC ACTIVITIES

400 charity tax concessions are at risk

The ACNC plans to revoke the charity status of 400 organisations it believes are no longer operating. These charities are being removed from the ACNC register as they have not been in contact with the commission since its establishment on 3 December 2012. They have failed to respond to letters and calls, and have not completed their 2013 Annual Information Statement. The ACNC was also unable to find evidence to suggest that these charities were still operating.

The revocations follow the removal or revocation of almost 4000 charities from the register since the commission was set up, including 246 in August. Some have revoked their registration voluntarily.

Charities that have had their status revoked no longer get tax concessions. If a charity is revoked but later found to be operating, the ACNC will work with it to restore its status.

A total of 3200 charities might be removed from the register over coming months. Charities are advised to complete their 2013 Annual Information Statement to ensure that they maintain their status and do not incur penalties.

The full list of charities marked for revocation, and information on how charities can contact the ACNC, is available at www.acnc.gov.au/whereareyou.

240 'lost' charities status revoked

The ACNC has revoked the charity status of more than 240 entities it has been unable to find. They include religious organisations, pre-school and parents clubs, trusts and foundations, and health-related organisations.

The charities form the first group of an estimated 4000 to have their registrations removed from the commission's register. Their revocation will also result in the loss of access to Commonwealth tax concessions. The ATO will be notified of the revocations.

Charities that have had their charity status revoked but are still operating are encouraged to contact the ACNC immediately and provide the necessary information to help the ACNC restore their registration.

Not solely charitable – status revoked

The status of two 'charities', Care 4 Kids Foundation of Australia Ltd and Indigenous Foundation of Australia Ltd, has been revoked after the ACNC ruled that their operations were not solely charitable.

The decision follows a five-month ACNC investigation into the charities' activities and purposes. The investigations were undertaken with the charities' cooperation. Both charities were given an opportunity to show why their registrations should not be revoked, and their responses were taken into account before a final decision was made. The charities are able to object to this decision and can re-apply to be registered once the ACNC's concerns are wholly addressed.

An entity is entitled to registration with the ACNC if it meets the requirements set out in section 25-5 of the *Australian Charities and Not-for-profits Commission Act 2012*. Registration entitles charities to apply for a range of Commonwealth tax concessions such as 'deductible gift recipient status', and income-tax exemption. Charities lose these benefits if their charity status is revoked.

Care 4 Kids Foundation of Australia Ltd operates in New South Wales, Victoria, Tasmania and South Australia. Indigenous



Foundation of Australia operates in New South Wales and Tasmania. Both charities are managed by the same directors. These directors are also involved with a for-profit organisation, Cancer Foundation of Australia Pty Ltd. This organisation is not a registered charity and not within the ACNC's jurisdiction.

The ACNC has dealt with more than 800 complaints or concerns about charities since its inception in December 2012. In most cases, the commission has worked with charities to allow them to resolve issues. The majority of complaints were resolved with education and advice. The commission has worked with boards to rectify concerns.

Charity status revoked – Canberra church

The ACNC has revoked the charity status of Canberra-based The New Connection Church Incorporated. The decision to revoke the church's registration and status follows a warning and direction to provide information and address breaches of the Act.

On 28 April, the ACNC advised the church that it had breached the Act by failing to lodge its 2013 Annual Information State-

ment. On 26 May, the commission reminded the church that it had failed to respond to advice about filing relevant information in its annual information statement. Information about the warning and direction is recorded on the ACNC's website under 'compliance' decisions.

Help with regulatory and compliance guides

A guide to the ACNC's regulatory approach and self-assessment compliance test are the latest tools to help charities stay on track.

'Your charity and ACNC Compliance' helps to demystify the role of the commission's compliance team when investigating concerns it receives about charities.



ACNC ACTIVITIES (CONTINUED)

The 'Take the ACNC compliance test: is your charity complying?' enables charities to check that they are meeting their obligations.

'Your charity and ACNC Compliance' explains how and when investigations and reviews are conducted, when charities may be notified, and what information can be shared or disclosed. It also provides advice on actions charities should take if they find that they are not meeting their obligations.

The ACNC has received more than 1000 concerns about charities since December 2012, more than half being resolved by the commission's advice service. Of 350 concerns referred to the compliance team, about three-quarters were from the public. The Compliance Directorate finalised 51 cases last year, which saw 83 compliance issues substantiated and addressed.

Four charities had their registrations revoked as a result of non-compliance. In 2014-2015 the ACNC expects these numbers to increase – serious concerns continue to be brought to the commission's attention.

The commission found that charitable funds were being inappropriately used and that board members and trustees were failing to declare conflicts of interest and maintain accurate records. Criminal activity – such as employee theft – was also uncovered, and some charities simply failed to be accountable to their members, a requirement of their constitutions.

During 2013-14 year, the ACNC took a range of actions, including working with charities to improve record-keeping, managing conflicts of interest and engaging professional advisors. It helped charities to develop

agreements to guarantee the long-term protection of their assets; shared information with other agencies. Sometimes, enforcement was appropriate.

The compliance test is quickly and easily completed. It has five simple questions, and 'no' and 'not sure' answers are enough to alert an organisation to investigate further its activities or take remedial action.

Deductible Gift Recipients fact sheet

A fact sheet on Deductible Gift Recipients (DGRs) is available on the ACNC website. Not all charities qualify for DGRs, however charities can apply for DGR endorsement and the ACNC will pass on the information to the ATO, which determines DGR eligibility.



Charities must lodge financial statements with the ACNC not ASIC



FINANCIAL REPORTING INSIGHTS

Financial report reminder

Charities must lodge financial statements with the ACNC not ASIC

Companies that are registered with the ACNC do not need to lodge financial reports for years commencing on or after 1 July 2013 with ASIC. Instead, medium and large charities registered with the ACNC are required to provide annual financial reports to the ACNC.

The ACNC registers organisations as charities. These may include organisations registered with ASIC including:

- public companies limited by guarantee – the most common type of company structure used by charities (and other not-for-profit purposes)
- proprietary companies limited by shares – such as a

business that is wholly owned by a charity that has a similar charitable purpose

- registered Australian bodies – such as an incorporated association registered under a State Act and registered with ASIC if it carries on business outside the state or territory in which it is registered. and
- foreign companies – such as a charity formed or incorporated outside Australia but registered to carry on business in Australia.

Registered charities are required to prepare their first financial reports for the ACNC 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 within six months after the end of an approved substituted accounting period that commences after 1 July 2013.

Large registered charities will be required to have their financial reports audited, and medium registered charities can generally choose to either have their financial reports reviewed or audited. There is no mandatory financial statement lodgement required for small charities. The ACNC Act defines charity size according to annual revenue as follows:

- small registered charity – annual revenue is less than \$250 000
- medium registered charity – annual revenue is \$250 000 or more but less than \$1 million. and
- large registered charity – annual revenue is \$1 million or more.

Companies that are not registered with the ACNC, or cease to be registered with the ACNC,

FINANCIAL REPORTING INSIGHTS (CONTINUED)

must lodge their annual financial reports with ASIC if they are required to do so under the existing tests in the Corporations Act.

Consolidation required for NFP entities

Australian Accounting Standard AASB 2013-8 'Amendments to Australian Accounting Standards – Australian Implementation Guidance for Not-for-Profit Entities – Control and Structured Entities' applies to 31 December 2014 balance date for the first time. Schools, churches and charities are likely to be affected.

The amendments provide significant guidance to assist not-for-profit entities in private and public sectors to apply AASB 10 'Consolidated Financial Statements' and AASB 12 'Disclosure of Interests in Other Entities'.

The main change from the previous requirements is that the concept of control is now more specific. A three-step approach is applied to determine if control exists focusing on power, returns and a link between power and returns. That is, the investor must have:

- power over the investee
- exposure, or rights, to variable returns from its involvement with the investee, and
- the ability to use its power over the investee to affect the amount of the investor's return.

All three of these criteria must be met for control to be established. NFPs must reassess whether they still control or now control other entities under AASB 10.

Many schools have a building fund or foundation in which money is held for special projects. In the past, these funds might not have been consolidated in financial reports, but as schools can direct their use, school councils need to be aware of new reporting obligations.

Religious entities will also be

affected. They often have relationships with entities that provide education programs within a church, say, or that are devoted to fundraising. Religious entities might not have previously thought that these needed to be included in a consolidated report. If they direct the activities of these entities, they will now need to be included.

Charity reporting released

Chartered Accountants Australia and New Zealand released 'A guide for charities reporting under the ACNC Act 2012' to help them to determine whether the ACNC reporting requirements apply. The guide provides details about obligations on not-for-profit entities in relation to record-keeping, reporting and audit-

ing. It also covers what financial reports need to be lodged.

National Standard Chart of Accounts updated

The National Standard Chart of Accounts (NSCOA) has been updated and is available on the ACNC website.

NSCOA is a data-entry tool and data 'dictionary' for not-for-profits, including charities. All Australian governments (Commonwealth, State and Territory) have agreed to accept NSCOA when requesting information from not-for-profit entities.

While NSCOA is not compulsory,

there are benefits in using it, and it is part of the ACNC's efforts to reduce red tape. It provides a common approach to the recording and reporting of accounting information, reduces the time and cost of preparing financial statements, and provides a consistent approach to preparing financial information for reporting to multiple jurisdictions.



Not-for-profit Accountants & Auditors At Your Service!



LBW & Partners is a firm of chartered accountants that offers specialist audit services to not-for-profit organisations.

Our team members are able to help with unique issues faced by not-for-profits such as: reporting to funding agencies; ACNC compliance; fundraising related accounting and tax issues; FBT rules and impact on PBIs; GST concessions; constitutions and governance.

We work with a range of not-for-profit organisations including:

- ◊ Associations
- ◊ PBIs
- ◊ Charities & DGRs
- ◊ Churches, congregations, religious institutions
- ◊ Aged care
- ◊ Peak Industry Bodies
- ◊ Community organisations
- ◊ Sports Clubs
- ◊ Registered training organisations
- ◊ Companies limited by guarantee

If you are looking for accountants with specialist not-for-profit expertise, please contact Rupa Dharmasiri or Joe Kofod.

Replacing the ACNC – an options paper is released

The Federal Department of Social Services (DSS) has released an options paper entitled 'Australia's Charity and Not for profits' that describes plans to replace the ACNC with a National Centre of Excellence and ways of transferring its regulatory functions back to the Australian Securities and Investments Commission (ASIC) and the ATO.

The paper explains:

- the current legislative arrangements
- the government's plans to establish new self-reporting arrangements. Charities will be required to maintain a publicly accessible website that features the names of responsible persons; details of all funding received from government (Commonwealth, State and Local) and financial reports. Charities will have until 1 July

2015 to update their websites

- reinstatement of the previous ASIC reporting obligations for charities that are companies
- the transfer of charitable-status determination back to the ATO, identifying two options relating to how the ATO might complete this work. One option proposes an independent panel comprising external experts to provide advice on objections raised by charities that disagree with the initial ATO assessment on the determination of their charitable status.

The second option proposes a separate unit within the ATO responsible for determining outcomes for applicants who objected to findings on eligibility and related tax concessions

- charities currently exempt from providing financial reports would retain the exemption. Such charities

include small organisations and religious charities

- the revised compliance arrangements that will involve using the current powers of the states, ATO and APRA, and
- transitional arrangements that give charities until 1 July 2015 to comply with the new arrangements.

The paper says that the Australian Charities and Not-for-profits Commission (Repeal) (No.2) Bill is scheduled to be introduced into parliament later this year, but that the new arrangements for the ATO and ASIC will take effect immediately.

The current national register will be archived, and there is no intention to continue maintaining anything similar. As a result, there will be no need for an Annual Information Statement.

Comments on the paper closed on 20 August 2014. The department intends to provide a sum-

mary of written submissions on its website.

The Federal government is also consulting on the proposed NFP National Centre of Excellence (NCE) as part of the ACNC. The consultation on the NCE explicitly excludes any issues related to the abolition of the ACNC and stresses that the NCE is not a regulator.



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