



OTS MANAGEMENT PTY LTD

Advice from outside the square

**AN OTS MANAGEMENT
WHITE PAPER**

**PRACTICAL IMPLICATIONS OF
CHARITY GOVERNANCE STANDARDS**

Treasury's Consultation paper on the development of
governance standards for charities and its implica-
tions

March 2013



OTS Management is a quality and value-driven boutique consulting and company that provides organisational development and accounting services.

Our clients are commercial, growth-oriented Small and Medium Enterprises who require growth and business advice and coaching.

We give our clients comfort in their decision-making by providing them with our experience and independent advice which saves them time and helps them grow.

We meet our own high expectations in order to exceed the expectations of clients.

OTS Management Pty Ltd
Suite 7, 88 Walters Drive
Osborne Park WA 6107
Australia

Postal Address:-
P O Box 198
Wembley WA 6913

Tel: (61-8) 9242 2085
Fax: (61-8) 9443 7845

Email: ots@otsmanagement.com.au

PRACTICAL IMPLICATIONS OF CHARITY GOVERNANCE STANDARDS

Treasury's consultation paper on the development of governance standards for charities and its implications

Teik P Oh FCA, ATII

March 2013

www.otsmanagement.com.au

© OTS Management Pty Ltd, and Teik P Oh, 2013. All rights reserved.

For information or permission to reprint or quote extracts, please contact OTS Management Pty Ltd at

Email: post@otsmanagement.com.au

Mail: OTS Management/Permissions

P O Box 198

Wembley WA 6913

Australia

The information in this white paper does not constitute “advice”. The reader who wishes to follow the information contained in this white paper will need to obtain his or her own advice on how the information may apply to their specific circumstances.



Contents

Introduction—The changes in the regulatory framework for charities	1
The Consultation Paper on Governance Standards for Charities	2
The 6 Practical Implications for your charity	3



INTRODUCTION—THE CHANGES IN THE REGULATORY FRAMEWORK OF CHARITIES

Charities used to be endorsed by the Australian Taxation Office. This was a rigorous process by which entities (companies, trusts, funds) were required to show that they were a Not For Profit "Private Benevolent Institution", and that they operated as a Charity, in order to obtain various tax exemptions and concessions, and then if required further, to apply for endorsement as a Deductible Gift Recipient.

From time to time, these ATO endorsed charities receive audit requests from the ATO and they may have been investigated through a series of reviews of their activities and governance prin-

ciples to see that they maintained their charitable and therefore tax-exempt status.

All this changed from December 2012 when the Australian Charities and Not-For-Profit Commission (ACNC) commenced. Their first task was to transfer all charities previously endorsed by the ATO to their register. Many charities would have by now received a form from the ACNC to confirm their registered charity details.

The ACNC will now be responsible for the registration and administration of charities, taking functions away from the ATO as well as the Australian Securities and Investment Commission (ASIC).

The process to register a new charity is now the responsibility of the ACNC and not of the ATO. In this new process, the first step is to provide your information to the ACNC to have them investigate, and if appropriate, register you as a charity. They will then pass on your information directly to the ATO if you have also requested tax exemptions and concessions during the application process.

A new statutory definition of "charitable purpose"

1. **Until now, "charitable purpose" was defined by common law which was, generally, "to provide to the community" or a significant section of the community:-**
 - **The direct relief of poverty, sickness or needs of the aged;**
 - **Advancement of education;**
 - **Advancement of religion; and**
 - **"other purposes beneficial to the community" such as Not-for-profit childcare, art & culture, health, animal welfare, and protection of the environment.**
2. **A new statutory definition is expected and is intended to apply from 1 July 2013.**
3. **In the past the common law definition has evolved to meet the circumstances of each case, and it is unknown at this stage whether the new statutory definition will restrict certain activities such as the running of businesses.**

It is intended that from 1 July 2013 the ACNC will be fully operational and all aspects of the ATO and ASIC in relation to charities will cede to the ACNC.

The most important matter of this change-over, apart from the fact that charities will now have to satisfy ACNC staff as well as the ATO procedures, is the expectation of a new, statutory definition of "charitable purpose" (see box).



THE CONSULTATION PAPER ON GOVERNANCE STANDARDS FOR CHARITIES

In December 2012 Treasury issued a consultation paper called "Development of governance standards", in order to receive submissions on proposed governance standards for charities.

The paper provided six draft Governance Standards:-

1. Purposes and NFP character of a charity;
2. Accountability to members;
3. Compliance with Australian laws;
4. Responsible management of financial affairs;
5. Suitability of responsible entities;
6. Duties of responsible entities.

The paper provided definitions for some of the terms used above:-

- **Governance** means the set of practices

and procedures in place to ensure that an entity operates to achieve its objectives in an effective and transparent manner

- **Responsible entity** is an individual (or in some limited cases a corporation) who is responsible for running a charity, who is a member of the governing body—for all intents and purposes, the Directors.

The consultation paper comments in several places that the draft governance standards were not intended to be prescriptive but rather to be "principles-based" which specified an outcome rather than the means to achieve that outcome.

In various places the paper also emphasises that while compliance with the governance standards will be part of the ACNC's governance framework, "most registered charities will already be meeting these standards and have practices and procedures in place to cover them". This assertion is largely based on the intention that the proposed governance standards in some cases "merely" replace existing requirements.

However, the proposed governance standards, like the expected statutory definition of charitable purpose, add a new dimension of codification.

This can have important practical implications to the operation of a charity's day to day activities.

The consultations closed in February 2013.

Early indications are that the final governance standards will not substantially change from those in the consultation paper.



THE 6 PRACTICAL IMPLICATIONS FOR YOUR CHARITY

On the assumption that the final governance standards will not be substantially different from those in the consultation paper, there are positive steps you can take now to ensure that your systems and procedures are in place, in readiness for 1 July 2013.

While many existing processes may actually satisfy and comply with new governance standards for charities, the introduction of these governance standards (and the discussions in the consultation paper) imply that there are some additional issues that charities will need to be particularly mindful of.

OTS Management has drawn from the paper six practical implications for your charity.

1. Most governance standards will not differ from previous requirements despite consolidation and codification but you will need to check

For example the standard on accountability to members should be satisfied with ongoing arrangements to hold annual general meetings and have minutes available to members.

However, some existing requirements have been clarified with examples, and this clarification may require you to add another layer on to your existing processes.

When the governance standards are finalised, it is necessary for you to check that your existing

processes are sufficient, in light of any clarification of requirements.

2. Throughout the paper and in the standards, there is an implication that the charity is continually reviewing compliance

For example the paper states that "once a charity is registered with the ACNC, it will be responsible for assessing its own compliance with the governance standards".

Charities will need to show some evidence of an ongoing responsibility to assess its own compliance. For example, the existence of an Audit and Governance Committee, entries in minutes showing review of charitable purpose from time to time, and so on.

This should no longer be an informal process but should be built into the structures and Board meeting processes.

3. The charity's purposes will need to be available to the public

One limb of the first standard on the purposes and NFP nature of a registered charity is the requirement to "make information about its purposes available to the public".

Practically this may mean a statement in the website about the charitable purposes of the charity, in brochures, and in information available to the public as well as available on request.

It is also important to note that this is not only about the "activities" of the charity, but about information "in relation to their purposes" - meaning a linkage between activity and the purposes in its governing rules.

4. The charity must take "responsible steps for the reasonable management" of its financial affairs

This is now, or will be, a specific governance standard. The paper provides examples (often an indicator on what will be judged) that includes "general practices around the spending of funds...as well as who bears the risk and what procedures should be followed, if fraud occurs".

From a practical point of view, Directors should explicitly approve financial internal control procedures, delegation authorities and so on, and

be engaged in their reviews and maintenance.

5. The charity itself must take steps to ensure its Directors are not disqualified persons

While it has been included in corporate legislation previously that people are disqualified from acting as an officer of the company in certain circumstances, proposed standard number 5 introduces the concept that it is the charity itself that must take steps to ensure its Directors are not disqualified persons.

This means that there needs to be a regular review process, and one in place for new Directors that:-

- Checks the ASIC Disqualified Persons Register; and
- Checks the ACNC Register of Disqualified Responsible Entities; and
- Possibly obtain declarations from Directors at reasonable intervals stating that he/she has never been convicted of an offence against the Corporations Act 2001 or of an offence involving dishonesty in or outside of Australia which is punishable by imprisonment for at least 3 months; and that he/she is not an undischarged bankrupt nor currently subject to a personal insolvency agreement which has not been complied with.

6. The charity itself must take reasonable steps to ensure its Directors are subject to and comply with their legal duties

Previously it was the responsibility of Directors to comply with their legal duties and it was the individual who might have been penalised for any breach.

Proposed governance standard 6 introduces the new concept that it is the charity itself that has a responsibility to take "reasonable steps" to ensure their Directors comply with their legal duties (as further outlined in the standard).

This means that a charity will need to show that a process exists where the responsibility of Directors are "reasonably" monitored so that the charity can become aware of individual's breaches.

An interesting issue here is that the paper provides an example where a Director did not disclose a pecuniary conflict of interest and benefited from it, and states that "the charity would be expected to dismiss Mike and/or take some

other action to enforce its governing rules, otherwise it would be in breach of the governance standards". It goes on further to say that "inaction by the charity may put it in breach of the standard".

Clearly, if the charity becomes aware of an individual's breach of their duty (how does it do that other than implement a monitoring and review process?) it must take some sort of action (including dismissal, and therefore would need to ensure its disciplinary rules are well established).

For a complete list of OTS Management publications and information about how to obtain copies please visit our website at www.otsmanagement.com.au

For any further information on this white paper, or any other information and services, please email us with your query on ots@otsmanagement.com.au