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Dear Sir/Madam

## **SUBMISSION – REVIEW OF NOT-FOR-PROFIT GOVERNANCE ARRANGEMENTS**

Grant Thornton Australia Limited (Grant Thornton Australia) appreciates the opportunity to provide comments to Treasury on the Consultation Paper 'Review of not-for-profit governance arrangements' dated 8 December 2011. We fully support the need for short-term reform to ensure that the sector is able to benefit from both reduced red tape and also have improved transparency and accountability. However, we are disappointed that Treasury has allowed for only a short 4 week period for comment on what we believe are fundamental reforms to the not-for-profit ("NFP") sector. The practical implications of a timeframe this short is further exacerbated by the timing of the consultation period spanning the Christmas and New Year holidays. Over this period, many of our staff and our clients in the NFP sector are on leave, reducing the potential for our response to reflect a richer, more thorough and balanced response to the consultation questions posed.

Our comments in the form of responses to the questions posed in the Consultation Paper are attached to this letter.

In addition to those specific responses, there are four key matters that we believe should be considered in the context of the consultation process relating to NFP governance:

- The key message arising from the Productivity Commission Report 'Contribution of the Not-for Profit Sector' was the need for wide-ranging reforms to remove unnecessary burdens and costs faced by the NFP sector and improve accountability. This stated aim should be used as the filter through which decisions are made during the process for determining the core organisational governance principles applied to NFP entities. We believe there needs to be a high level of

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support accompanying the rollout of the principles through model rules and other templates, guidance forms and supply of consistent information to assist responsible individuals at NFPs meet their governance obligations.

- We would strongly support a principles-based approach to developing core organisational governance principles for NFP entities, which allows for continued development through the common law, rather than a prescriptive codification approach. We feel this approach would allow for flexibility in a constantly changing sector.
- We strongly agree with a tier-based approach being applied to these core organisational governance principles. We feel that the tier-based approach needs to address the distinction in need between charitable and non-charitable NFP entities and do not feel that this has been fully considered within the consultation paper. We believe that the greater level of public interest and support conferred on charities requires a commensurate increase in governance-related requirements.
- Whilst the consultation paper consistently refers to 'responsible individuals', no opinion was sought from respondents regarding how this concept should be defined. We note that paragraph 85 of the consultation paper deals with the 'expected' definition to be contained in ACNC legislation, however given the significance of this concept in the context of NFP governance, we consider it should have also been addressed in this paper.

Should have any queries in relations to these matters please do hesitate to contact me on 07 3222 0307.

Yours faithfully  
GRANT THORNTON AUSTRALIA LIMITED



Mr Simon Hancox  
Partner - Audit & Assurance



## Responses to Questions

1. *Should it be clear in the legislation who responsible individuals must consider when exercising their duties, and to whom they owe duties to?*

Given the broad range of entities and missions within the sector, we do not believe that the stakeholders are sufficiently consistent between NFP entities to enable the legislation to clearly define who must be considered. We believe the legislation would be better placed to require the responsible individuals to identify the entity's stakeholders. This list of stakeholders should be reviewed on a regular basis. Guidance should be provided by the ACNC to assist the responsible individuals in identifying these stakeholders.

2. *Who do the responsible individuals of NFPs need to consider when exercising their duties? Donors? Beneficiaries? The public? The entity, mission and purpose of the entity?*

As mentioned above, given the diversity of the sector, the factors to consider will vary from entity to entity. In determining who the stakeholders may be, the responsible individuals should consider factors such as:

- The structure of the entity;
- The purpose of the entity;
- The funding sources of the entity;
- Employees / volunteers; and
- How the entity interacts with the public.

3. *What should the duties of responsible individuals be, and what core duties should be outlined in the ACNC legislation?*

In keeping with our belief that a principles-based approach is the most appropriate mechanism to drive governance in NFPs, we believe the duties set out in paragraph 91 of the consultation paper should be the core duties incorporated into the ACNC legislation. These duties being:

- A duty of care and diligence;
- A duty to act in good faith and in the best interests of the entity;
- A duty to not misuse their position;
- A duty to not misuse information; and
- A duty to disclose material personal interests

are well supported by a body of common law and are generally well understood.





4. *What should be the minimum standard of care required to comply with any duties? Should the standard of care be higher for paid employees than volunteers? For professionals than lay persons?*

The minimum standard of care required should be that of the 'reasonable person', as incorporated in the Corporations Act and supported by a body of common law. This standard of care should apply to all responsible individuals, irrespective of whether they are paid or voluntary or professional or lay persons.

5. *Should responsible individuals be required to hold particular qualifications or have particular experience or skills (tiered depending on size of the NFP entity or amount of funding it administers)?*

We do not believe that responsible individuals should be required to hold particular qualifications or have particular experience or skills. The introduction of such requirements, even on a tiered basis, could lead to organisations losing valuable talent and imposes a requirement above that of a for-profit company. We do however believe that exclusions to being a responsible individual should be in place, for example, bankruptcy.

6. *Should these minimum standards be only applied to a portion of the responsible individuals of a registered entity?*

The minimum standard of care should apply equally to all responsible individuals.

7. *Are there any issues with standardising the duties required of responsible individuals across all entity structures and sectors registered with the ACNC?*

Provided that the duties are principles-based we cannot identify any issues with standardising the requirements across all entity structures and sectors.

8. *Are there any other responsible individuals' obligations or considerations or other issues (for example, should there be requirements on volunteers?) that need to be covered which are specific to NFPs?*

We have not identified any other responsible individuals' obligations or considerations specific to NFPs that should be addressed in relation to their core duties.

9. *Are there higher risk NFP cases where a higher standard of care should be applied or where higher minimum standards should be applied?*

Providing the concept of a 'reasonable person test' is applied to the standard of care, there is no requirement to specifically address higher minimum standards to higher risk NFP cases.



10. *Is there a preference for the core duties to be based on the Corporations Act, CATSI Act, the office holder requirements applying to incorporated associations, the requirements applying to trustees of charitable trusts, or another model?*

Our preference is for the core duties to be based on the Corporations Act as this definition is more regularly considered by the courts and has a higher base of common law.

11. *What information should registered entities be required to disclose to ensure good governance procedures are in place?*

An initial corporate governance policy should be provided as part of the initial registration process. To facilitate consistency of reporting, and to ensure the level of reporting is appropriate to the size and nature of the organisation, the ACNC should develop suitable templates.

Consideration could be given to an annual confirmation of adherence to those policies in whatever reporting process the ACNC develops for NFP registrants.

For large public-interest entities, including charities, consideration should be given to the provision of a publically available corporate governance report similar to that required by companies listed on the Australian Stock Exchange.

12. *Should the remuneration (if any) of responsible individuals be required to be disclosed?*

Given the level of public interest in the sector, and the aims of these reforms to improve transparency in the sector, we believe that disclosure of responsible individuals' remunerations would be appropriate. Whether remuneration is required to be disclosed at an aggregate or individual level should be determined with reference to the entity's tier – lower tiers should require less onerous disclosures than large public-interest NFPs.

Further to quantitative disclosures, some disclosure relating to the methodology adopted in determining remuneration of responsible individuals should be made.

13. *Are the suggested criteria in relation to conflicts of interest appropriate? If not, why not?*

We consider the suggested criteria in paragraph 126 of the consultation paper to be appropriate.

14. *Are specific conflict of interest requirements required for entities where the beneficiaries and responsible individuals may be related (for example, a NFP entity set up by a native title group)?*

We are not aware of any instances where specific conflict of interest requirements are required.



15. *Should ACNC governance obligations stipulate the types of conflicts of interest that responsible individuals in NFPs should disclose and manage? Or should it be based on the Corporations Act understanding of 'material personal interest'?*

Our preference is that the concept of a 'material personal interest' as defined in the Corporations Act is adopted.

In some jurisdictions, where specific types of actions have been prohibited, constant revision of the legislation has been required to address unforeseen circumstances. We do not believe that such an approach would lead to a reduction in red tape.

16. *Given that NFPs control funds from the public, what additional risk management requirements should be required of NFPs?*

We do not believe there is any need to codify specific risk management requirements for NFP entities.

Consistent with the responsible individuals' duty of care, risk assessment processes appropriate to the size and nature of the NFP entity should be undertaken and reviewed on a regular basis. To enable NFP entities to undertake these processes the ACNC should develop suitable templates to facilitate the documentation of risk management and mitigation strategies. The templates should be modified for each tier to allow for appropriate scaling to entities of differing sizes.

17. *Should particular requirements (for example, an investment strategy) be mandated, or broad requirements for NFPs to ensure they have adequate procedures in place?*

We would support broad requirements for NFPs to ensure they have adequate risk management procedures in place. We recognise that there may be specific subsets (for example, Private Ancillary Funds), where specific requirements such as investment strategies may appear desirable. However, we would argue that such requirements are a natural extension of a reasonable person applying a duty of care.

18. *Is it appropriate to mandate minimum insurance requirements to cover NFP entities in the event of unforeseen circumstances?*

Underlying the Productivity Commission's report was a desire to reduce the costs and red-tape associated with NFP entities. We do not believe that imposing minimum insurance requirements without appropriate cost-benefit consideration meets that mandate.

19. *Should responsible individuals generally be required to have indemnity insurance?*

This assessment is a personal consideration by the responsible individual and is reflective of the private level of risk they are willing to accept in their role. Accordingly, a requirement to hold indemnity insurance should not be mandatory.





20. *What internal review procedures should be mandated?*

We do not believe that any specific internal review procedures should be mandatory.

Consistent with the responsible individuals' duty of care, internal control and review procedures appropriate to the size and nature of the NFP entity should be developed.

21. *What are the core minimum requirements that registered entities should be required to include in their governing rules?*

The core minimum requirements should address:

- The objectives of the entity and the process for changing those objectives;
- The mechanism for making decisions;
- The appointment, removal, responsibilities and powers of responsible individuals;
- The appointment, removal and rights of members;
- The mechanism for holding meetings;
- Mediation, arbitration and dispute resolution procedures; and
- The process for winding up the entity, including the distribution of any surplus assets.

22. *Should the ACNC have a role in mandating requirements of the governing rules, to protect the mission of the entity and the interests of the public?*

The ACNC should adopt an approach similar to that adopted under the Corporations Act – that is, one which specifies mandatory and replaceable rules to allow flexibility within the governing rules to fit the nature and size of the NFP.

23. *Who should be able to enforce the rules?*

The members or the trustees (in the case of non-membership based organisations) should be able to enforce the governing rules in accordance with the entity's dispute resolution procedures.

24. *Should the ACNC have a role in the enforcement and alteration of governing rules, such as on wind-up or deregistration?*

We view the ACNC's role in relation to the enforcement of the governing rules as being the arbiter when a member of the NFP is dissatisfied with the outcome of the NFP's dispute resolution procedures or where a non-member (such as a beneficiary or donor) has a complaint against the NFP. The ACNC's power in such a situation should be limited to deregistering the entity.



We view the ACNC's role in relation to the alteration of the governing rules is solely that of maintaining the register of governing rules and is therefore a notification right only, providing the modifications do not alter a mandatory rule or otherwise affect its status as a NFP.

25. *Should model rules be used?*

Consistent with the Productivity Commission's aim to reduce the administrative burden on NFPs, we believe the provision of model rules for each identified tier of NFP would be appropriate.

26. *What governance rules should be mandated relating to an entity's relationship with its members?*

Mandatory governance rules pertaining to the member's relationship to a NFP should focus upon their rights as members, including:

- The ability of members to remove responsible individuals;
- The right to an annual general meeting; and
- The right of access to financial information.

Further, inclusion of replaceable dispute resolution procedures is necessary to enable members to address grievances.

27. *Do any of the requirements for relationships with members need to apply to non-membership based entities?*

We have not identified any requirements for relationships with members that need to be applied to non-membership based entities.

28. *Is it appropriate to have compulsory meeting requirements for all (membership based) entities registered with the ACNC?*

We believe that at a minimum an annual general meeting of members should be compulsory for all membership-based entities. Further meeting requirements could be dealt with by way of replaceable rules to allow for flexibility.

29. *Are there any types of NFPs where specific governance arrangements or additional support would assist to achieve in better governance outcomes for NFPs?*

We have not identified any types of NFPs where specific governance arrangements beyond those applying to all registered entities would be necessary.

Particularly for smaller NFPs, we believe there needs to be a high level of support from the ACNC accompanying the rollout of the principles through model rules and other templates, guidance forms and supply of consistent information to assist responsible individuals at NFPs meet their governance obligations.





30. *How can we ensure that these standardised principles-based governance requirements being administered by the one-stop shop regulator will lead to a reduction in red tape for NFPs?*

During the transition period, we envisage that there could be several pieces of legislation covering the operation of a single NFP. We would recommend that once an organisation is appropriately registered with the ACNC it is exempt from the governance requirements imposed by other legislations.

Additionally, there needs to be clear direction and guidance by the ACNC as to what its requirements are so that the registration process is as clear and uncomplicated as possible.

31. *What principles should be included in legislation or regulations, or covered by guidance materials to be produced by the ACNC?*

The legislation should define who a responsible individual will be and their principles-based duties and minimum standard of care. The governance requirements should be in the form of mandatory and replaceable rules similar to the approach adopted in the Corporations Act. All other matters should be addressed in guidance issued by the ACNC.

32. *Are there any particular governance requirements which would be useful for Indigenous NFP entities?*

We have not identified any particular governance requirements which would be useful for Indigenous NFP entities.

33. *Do you have any recommendations for NFP governance reform that have not been covered through previous questions that you would like the Government to consider?*

The consultation paper consistently refers to 'responsible individuals', however no opinion was sought from respondents regarding how this concept should be defined. We note that paragraph 85 of the consultation paper deals with the 'expected' definition to be contained in ACNC legislation, however given the significance of this concept in the context of not-for-profit governance, we consider it should have also been addressed in this paper.

Particularly we believe the reference to 'an individual with the capacity to significantly affect the registered entity's financial standing' has the potential to include significant donors as responsible individuals which will be an unintended consequence of this definition.