

Submission to Commonwealth Treasury

Review of Australian Charities and Not-for-profits Commission (ACNC) Legislation

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Introduction

This submission addresses the questions raised in the Terms of Reference regarding the Review of Australian Charities and Not-for-profits Commission (ACNC) Legislation. The aim of this submission is to provide an informed debate on the *ACNC Act 2012* (Cth) over its first five years of operation.

If any of the responses require further explanations, please contact Dr Marina Nehme at the University of New South Wales, Sydney, The Law Faculty at m.nehme@unsw.edu.au

General Observation

The observations made in this submission can be summarised in the following manner:

- The objects of the *ACNC Act* are relevant and contemporary;
- The regulatory framework should be extended to cover other classes of not-for-profit organisations;
- Within the resources it has, the ACNC has started reducing the duplicative reporting on charities. More has to be done in this sphere. The regulator has to be equipped with the necessary resources to continue this task;
- The ACNC has adopted a mix regulatory strategy of persuasion and deterrence and this has allowed the regulator to address misconduct in the sector. This regulatory approach has further meant that the ACNC has struck the right balance between deterrence and supporting the charity sector;
- Civil penalties need to be introduced to the ACNC regulatory framework;
- A changes to the penalty regime may be needed in respect to the way certain conducts are dealt with by the legislation. For instance, some conduct should not be criminalised while other conduct should be, instead of merely attracting an administrative sanction, especially when that conduct involves dishonesty.

1. Are the objects of the ACNC Act still contemporary?

According to s 15-5, the object of the ACNC Act are the following:

- (a) to maintain, protect and enhance public trust and confidence in the Australian not-for-profit sector; and
- (b) to support and sustain a robust, vibrant, independent and innovative Australian not-for-profit sector; and
- (c) to promote the reduction of unnecessary regulatory obligations on the Australian not-for-profit sector.

These objectives are relevant and contemporary. They focus on building trust and confidence while at the same time supporting innovation within the sector. Further, the provisions in the Act are well equipped to achieve such outcomes.

The last objective of reducing unnecessary regulatory burden is also of key relevance. However, the ACNC has faced a range of challenges in facilitating this aim due to the constitutional limitations faced by the regulator.

- 2. Are there gaps in the current regulatory framework that prevent the objects of the act being met?**
- 3. Should the regulatory framework be extended beyond just registered charities to cover other classes of not-for-profits?**
- 8. Has the ACNC Legislation been successful in reducing any duplicative reporting burden on charities? What opportunities exist to further reduce regulatory burden?**

For a long time, the regulatory framework for the charities and not-for-profit sector has been viewed as ‘complex, lack[ing] coherence [and] sufficient transparency, and ... costly.’¹ One of the challenges the ACNC faces in simplifying the system is the reduction of unnecessary regulatory obligations that may apply to this sector.² In order to achieve this, the Reporting and Red Tape Reduction Directorate has been established to ensure that the ACNC’s resources are targeted to prioritise this aim. The Directorate is working with the States and Territories to harmonise the regulatory requirements for charities registered at the State and Territory level.³ The ACNC has also entered into memoranda of understanding with ASIC,⁴ ORIC⁵ and the Australian Tax Office⁶ to ensure effective collaboration in this area. Table 1 highlights the progress and the challenges that the ACNC faces in its cooperation effort with different agencies at different levels.

¹ Australian Government Productivity Commission, *Contribution of the Not-For-Profit Sector – Productivity Commission Research Report* (January 2010), xxiii.

² See *Australian Charities and Not-for-profits Commission Act 2012* (Cth), s 15-5(1)(c).

³ ACNC, ‘Red tape reduction’

<http://www.acnc.gov.au/ACNC/About_ACNC/Redtape_redu/ACNC/Report/Red_tape.aspx?hkey=02c36842-0881-4e67-98ad-0533e728658a>.

⁴ ACNC, ‘ASIC and the ACNC Sign a MOU’ (Media Release, 18 June 2013) <http://www.acnc.gov.au/ACNC/Comms/Med_R/MR_029.aspx>.

⁵ ACNC, ‘Registrar and the ACNC Work Together to Support Aboriginal and Torres Strait Islander charities’ (Media Release, 21 June 2013) <http://www.acnc.gov.au/ACNC/Comms/Med_R/MR_032.aspx>.

⁶ ACNC, ‘Memorandum of Understanding between the ACNC and the ATO’

<<http://www.acnc.gov.au/ACNC/Pblctns/Pol/MOU/ACNC/Publications/MOU.aspx?hkey=6dc20099-799a-4d17-b3bd-0921d6f10c50>>.

	Report once	Common audit thresholds	Updating addresses once	Waived fee
ASIC Companies	✓	✓	✓	✓
ORIC Indigenous Corporations	✓	N/A	✓	N/A
Ancillary Funds	✓	✓	✓	N/A
TAS Incorporated Associations	✓	✓	✗	✓
SA Incorporated Associations	✓	✓	✗	✓
ACT Incorporated Associations	✓	✓	✓	✓
VIC Incorporated Associations	In progress	✓	✗	In progress
NT Incorporated Associations	In progress	In progress	✗	In progress
WA Incorporated Associations	In progress	✓	✗	In progress
NSW Incorporated Associations	✗	✗	✗	✗
QLD Incorporated Associations	✗	✗	✗	✗

Table 1 - Red tape reduction – legal Structure⁷

As highlighted by the above table, more work must be done to deal with the fragmentation of the not-for-profit sector. Another step that has to be taken is to extend the existing frameworks under the *ACNC Act* to not-for-profit organisations. The challenge attached to this is the fact that a number of not-for-profits are registered and operate at a State/Territory level. A cooperation regime needs to be set up at different State/Territory levels to harmonise the systems that are already in existence.

⁷ Table adopted from the ACNC website: https://charity.acnc.gov.au/ACNC/About/ACNC/Redtape_redu/ACNC/Report/Red_tape.aspx

6. Have the risks of misconduct by charities and not-for-profits, or those that work with them, been appropriately addressed by the ACNC legislation and the establishment of the ACNC?
7. Have the risks of misconduct by charities and not-for-profits, or those that work with them, been appropriately addressed by the ACNC legislation and the establishment of the ACNC?
9. Has the ACNC legislation and efforts of the ACNC over the first five years struck the right balance between supporting charities to do the right thing and deterring or dealing with misconduct?

The *Australian Charities and Not-for-profits Commission Act 2012* (Cth) has provided the ACNC with a range of tools to enable it to implement a regulatory policy based on cooperation. The charities regulator has taken the view that ‘most people involved in charities are honest, acting in good faith and trying to do the right thing’.⁸ The ACNC has further observed that its dealings with regulated entities will be based on the presumption of honesty and a respect for the sector. Accordingly, the regulator is starting from a premise that the entities it regulates are ‘good apples’ rather than ‘bad apples’ and, as such, do not require stringent regulation.⁹ It is of the view that gentle persuasion will work in securing charities’ compliance with the law. Consequently, the starting point of the ACNC’s regulatory strategy is trust in the charity sector.

Further, the ACNC has implemented plans to communicate, listen to and work with the charity sector to deal with potential breaches of the law.¹⁰ As Smith and Mackie noted, ‘norms must be brought to mind before they can guide behaviour’¹¹—and new legislation, such as the *Australian Charities and Not-for-profits Commission Act 2012* (Cth), brings an opportunity to create new norms.

The legislation itself supports this approach as it states that, in performing its functions, the ACNC will ‘assist registered entities in complying with and understanding this Act, by providing them with guidance and education’.¹² Therefore, the regulator is not merely empowered, but also obliged, by the legislation to provide educational information to the charities sector and to deal with non-compliance in a non-confrontational manner. The ACNC’s approach is summarised in Table 2.

	ACNC’s cooperative approach
Regulatory objective	Aims to achieve the regulatory goal set out in the legislation: enhancing confidence and accountability in the charity sector
Instruments	Education and guidance
Assumptions	Presumption of honesty in the regulated sector
Emphasis	Building capacity of the entities to meet the requirements of the legislation by listening to and communicating with entities

Table 2: Summary of the ACNC’s cooperative approach

Such an approach allows the regulator to take measured and reasonable action to deal with breaches of the law. This is especially important in the early stages of the introduction of the

⁸ ACNC, ‘Australian Charities and Not-for-profits Commission Statement: Regulatory Approach’ (2013), 5.

⁹ Eugene Bardach and Robert Kagan, *Going by the Book: The Problem of Regulatory Unreasonableness* (Temple University Press, 1982), 92–3.

¹⁰ ACNC, ‘Memorandum of Understanding between the ACNC and the ATO’ <<http://www.acnc.gov.au/ACNC/Pblctns/Pol/MOU/ACNC/Publications/MOU.aspx?hkey=6dc20099-799a-4d17-b3bd-0921d6f10c50>>.

¹¹ Eliot Smith and Diane Mackie, *Social Psychology* (Psychology Press, 2nd ed, 2000), 377.

¹² *Australian Charities and Not-for-profits Commission Act 2012* (Cth), ss 15-5(2)(b)(iii) and 110-10(1).

regulator, as the regulated entities may not be familiar with it or with the way the ACNC would interpret the legislative provisions. Time needs to pass for such familiarity to be established. Further, in the long run, this approach will enable the regulator to adopt problem solving strategies to deal with breaches of the law.

However, the cooperative approach by itself is not enough to ensure compliance with the law. Any lack of cooperation by the regulated entities needs to be met with a deterrence response to avoid abuses of the system. The legislation has equipped the ACNC with a number of enforcement tools that would enable it to strike at offenders. These sanctions fit within the different levels of the enforcement pyramid. The variety of sanctions available to the regulator allows the ACNC to apply proportionate responses to breaches of the law and are represented in Diagram 1.



Diagram 1: Gradual Approach to Enforcement¹³

A. *Proactive Sanctions*

An advantage of the current regime is the fact that not all the sanctions with which the ACNC has been equipped are reactive in nature. Some sanctions such as enforceable undertakings may be used proactively to prevent potential breaches of the law. Warnings and directions may also be relied upon to deal with likely breaches of the law. The tools available to the ACNC thus allow it to implement both proactive as well as reactive responses.

B. *Suspension and Revocation – an Important Part of the Regulatory Framework*

The *ACNC Act 2012* does not directly provide the ACNC with the power to ban people from managing the entities it regulates. However, closer examination of the legislation and particularly Division 100 reveals that the ACNC has the power to suspend and remove a responsible entity of a registered entity.¹⁴ For the purpose of this provision, a responsible entity is defined as a director or a

¹³ This pyramid is based on Braithwaite's pyramid of enforcement.

¹⁴ *Australian Charities and Not-for-profits Commission Act 2012* (Cth), ss 100-5(1), 205-30.

trustee of a registered entity.¹⁵ Under Governance Standard 5, the duties of the responsible entity are the following:¹⁶

- Act with reasonable care and diligence;
- Act in good faith for the best interest of the charity and in accordance with the organisation's purpose;
- Avoid conflict of interest;
- Ensure that the financial affairs of the charity are conducted appropriately; and
- Prevent insolvent trading.

A breach of these obligations would negatively impact the way the organisation is run. Accordingly, the ACNC may suspend or remove a director or a trustee of a federally regulated entity if the regulator reasonably believes that the charity:¹⁷

- has contravened, or that it is more likely than not that it will contravene, a provision of the Act; or
- has not complied with, or that it is more likely than not that it will not comply with, a governance standard; or
- has not complied with, or that it is more likely than not that it will not comply with, an external conduct standard.

The ACNC may only issue such an order if the Commissioner considers that it is necessary to address the contravention or non-compliance.¹⁸ The effect of the suspension is that the person suspended cannot act as a responsible entity of the charity until the suspension ends.¹⁹ Similarly, the removal of a responsible entity means that the person cannot act as a director or trustee for the registered entity.²⁰ In both instances, the person against whom the order is made by the ACNC cannot be involved in the affairs of the charity. A breach of the suspension or removal order is a criminal offence.²¹ Additionally, such orders may impact on that person's ability to be appointed as a responsible entity for another charity.²² Accordingly, suspension or removal of a responsible entity by the ACNC is akin to the banning order that may be issued by other regulators.

A suspension or removal can only be issued by the ACNC for the protection of the public.²³ This sanction provides the regulator with a proportionate response to breaches of the law, as the duration of the suspension may vary depending on the breach.²⁴ The sanction of suspension or removal of a responsible entity allows the ACNC to deal with breaches of the law in a timely manner

¹⁵ *Australian Charities and Not-for-profits Commission Act 2012* (Cth), ss 100-5(2), 205-30.

¹⁶ ACNC, 'Governance Standard 5: Duties of Responsible Persons' <https://www.acnc.gov.au/ACNC/Manage/Governance/GovStds_5/ACNC/Edu/GovStandard_5.aspx?hkey=c39296b7-ca7d-4d16-94c4-42aea680462a>.

¹⁷ *Australian Charities and Not-for-profits Commission Act 2012* (Cth), s 100-1.

¹⁸ *Australian Charities and Not-for-profits Commission Act 2012* (Cth), ss 100-10(1), 100-15(1).

¹⁹ *Australian Charities and Not-for-profits Commission Act 2012* (Cth), s 100-20(1).

²⁰ *Australian Charities and Not-for-profits Commission Act 2012* (Cth), s 100-20(2).

²¹ *Australian Charities and Not-for-profits Commission Act 2012* (Cth), s 100-25.

²² ACNC, 'Disqualified Persons Register' <https://www.acnc.gov.au/ACNC/FindCharity/About_Register/Disqual_reg/ACNC/Reg/Disqual_personReg.aspx?hkey=b6e384ce-b4ab-4652-9be0-e3814e187c76>.

²³ *Australian Charities and Not-for-profits Commission Act 2012* (Cth), ss 100-10(9), 100-15(6), 35-10(2). For a discussion about the purpose of this sanction, see: Marina Nehme, 'Latest Changes to the Banning Order Regime: Were Amendments Really Needed?' (2013) 31(6) *Company and Securities Law Journal* 341, 345-9.

²⁴ Revised Explanatory Memorandum, Australian Charities and Not-for-profits Commission Bill 2012, 150.

without needing to go to court.²⁵ However, it has been argued that providing the ACNC with this enforcement tool creates legal uncertainty as it allows the ACNC to have powers that are not yet ‘tested and defined by judicial process’.²⁶ For example, in their submission to the Senate Economics Legislation Committee, the Financial Services Council stated:²⁷

The suspension, removal and replacement provisions in the ACNC Act grant powers to the Commissioner that go well beyond the powers of any other Federal regulator. The Commissioner can remove and replace the responsible entity of a regulated entity for actual and potential breaches of the ACNC regime, without a court process. This means that the directors of a public listed entity could potentially be removed from office by the Commissioner in the absence of a proper court process that ensures due process and the application of the rules of evidence.

The reality is that the suspension or removal of a director from a charity will have a punitive effect on the person acting in this position as they may lose their livelihood for the duration of the order. The suspension or removal may also attract negative publicity, which may be damaging to the director’s reputation and standing within the community. As such, the sanction may negatively impact upon the reputation and finances of the responsible entity.²⁸ The Senate Economics Legislation Committee recommended accordingly that ‘it was inappropriate for there to be a Commonwealth charities regulator with the power to remove or suspend directors and trustee without court proceedings’.²⁹

However, this recommendation ignores the fact that such a power ensures that the regulator is not a toothless tiger. While ASIC does not have the power to disqualify directors on its own accord except in certain circumstances,³⁰ the *Corporations Act 2001* (Cth) does provide the corporations and financial services regulator with the power to ban people from working in the financial services industry if they have breached their obligations under the law or are likely to breach such obligations.³¹ The principles that apply in the context of ASIC’s banning power will also apply to the ACNC’s removal and suspension powers. For instance, it is important that the duration of a suspension is not punitive in nature, as this may allow the responsible entity to successfully challenge the suspension order.³² Consequently, use of the sanction can only be relied on in rare instances to deal with major breaches of the law. Section 100-1 of the *Australian Charities and Not-for-profits Commission Act 2012* (Cth) highlights that the use of this power will be applying similar standards and principles to the ones guiding ASIC, noting that the power may only be used when the suspension or removal is deemed necessary to address the contravention or non-compliance, and only after the consideration of a range of policy matters.

²⁵ Revised Explanatory Memorandum, Australian Charities and Not-for-profits Commission Bill 2012, 150.

²⁶ Senate Economics Legislation Committee, Senate, *Australian Charities and Not-for-profits Commission (Repeal) (No 1) Bill 2014 [Provisions]* (June 2014), 20.

²⁷ Financial Services Council, *Submission to the Senate Economics Legislation Committee (No 58)*, 3.

²⁸ Marina Nehme, ‘Latest Changes to the Banning Order Regime: Were Amendments Really Needed?’ (2013) 31(6) *Company and Securities Law Journal* 341, 349; *Re Howard and Australian Securities and Investments Commission* (2008) 101 ALD 602, 653.

²⁹ Senate Economics Legislation Committee, Senate, *Australian Charities and Not-for-profits Commission (Repeal) (No 1) Bill 2014 [Provisions]* (June 2014), 25.

³⁰ *Corporations Act 2001* (Cth), s 206F.

³¹ *Corporations Act 2001* (Cth), s 920A.

³² Nehme, n 28, 351–2; *Kamha v Australian Prudential Regulation Authority* (2005) 147 FCR 516, 533–4.

Due to its severity, the suspension or removal of a responsible entity should be used as a sanction of last resort. The ACNC has adopted such an approach as it has noted that:³³

In the majority of situations where suspension or removal becomes necessary, we will not generally exercise this power without first considering less coercive enforcement measures.

Further, the fact that the ACNC's use of its suspension or removal power is subject to review by the Administrative Appeals Tribunal should, in principle, ensure that the regulator's reliance on this sanction is not heavy-handed and will further ensure the transparency and fairness of the regulator's decisions.

C. *Additionally Sanctions Needed – Filling the Gap*

One of the weaknesses in the current enforcement system is the fact that in the enforcement pyramid the level entitled 'Civil sanctions' contains only one type of sanction: injunction. An injunction is not really a penalty. As such, when the pyramid is applied there may be considered to be a gap between administrative/quasi-administrative sanctions and criminal penalties. With the exception of injunctions, a middle ground between the use of soft and drastic measures is missing. This may not be a problem while the legislation is still new and a lenient approach from the regulator is acceptable: at present, the use of injunctions may adequately fill the gap. However, when more serious breaches of the law occur in future and neither criminal nor administrative/quasi-administrative sanctions are appropriate, the regulator may find it difficult to determine a course of action. Consequently, civil penalties may need to be introduced into the legislation. Such sanctions may also result in the decriminalisation of certain conducts that are currently considered as criminal offences.

D. *Need a Change in the Way certain Conducts are Viewed*

Additional changes to the system may be needed in respect of the way certain conduct is dealt with by the legislation. For instance, some conduct should not be criminalised while other conduct should be, instead of merely attracting an administrative sanction, especially when that conduct involves dishonesty. Such amendments will better ensure that the regulator applies proportionate sanctions to offending conduct and result in an enhancement of the regulatory system.

Administrative penalties may be defined as non-discretionary financial sanctions imposed by a regulator without the intervention of a court or tribunal.³⁴ The application and method of calculation of administrative penalties are predetermined by the relevant legislation.³⁵ Unlike other regulators such as ASIC and ORIC, the ACNC has this sanction at its disposal. The ACNC may issue an administrative penalty in respect of the following two breaches of the law:

- an entity making a false or misleading statement;³⁶
- an entity failing to submit required documents to the ACNC on time.³⁷

³³ ACNC, 'Commissioner's Policy Statement: Compliance and Enforcement' (CPS2013/01) [55]. <https://www.acnc.gov.au/ACNC/Publications/Policy_PDFs/CommSt_Compliance.aspx>.

³⁴ ALRC, *Principled Regulation: Federal Civil and Administrative Penalties in Australia*, Report No 95 (2002), 79; Revised Explanatory Memorandum, Australian Charities and Not-for-profits Commission Bill 2012, 225.

³⁵ ALRC, *Principled Regulation: Federal Civil and Administrative Penalties in Australia*, Report No 95 (2002), 79.

³⁶ *Australian Charities and Not-for-profits Commission Act 2012* (Cth), s 175-10. The false and misleading statement may be issued to the ACNC or to others.

³⁷ *Australian Charities and Not-for-profits Commission Act 2012* (Cth), s 175-35.

These breaches of the law may result in the imposition of different administrative penalties, as illustrated in Table 3.

Breach	Factors	Amount	Amount in \$
Making a false or misleading statement ³⁸	Intentional disregard of the Act by the entity or its agent	60 penalty units	\$10,800
	Recklessness by the entity or its agent	40 penalty units	\$7,200
	Failure of the entity or of its agent to take reasonable care to comply with the Act	20 penalty units	\$3,600
No timely submission of required documents to the ACNC ³⁹	Medium registered entity	2 x base penalty	\$360 for each period of 28 days or part thereof
	Large registered entity	5 x base penalty	\$900 for each period of 28 days or part thereof
	Other	Base penalty = 1 penalty unit for each period of 28 days or part of a period of 28 days the document is late	\$180 for each period of 28 days or part thereof

Table 3: Administrative penalties that may be imposed

As may be seen from Table 3, the ACNC has been provided with a flexible and speedy sanction to deal with the two abovementioned breaches of the law. However, these administrative penalties may attract the same criticism attached to the use of fines: administrative penalties do not remedy the breach, but impose a monetary penalty that may not necessarily change a charity's compliance culture. As such, the penalty may not prevent similar breaches from occurring in the future. Accordingly, while administrative penalties have certain advantages in dealing quickly with a breach, their benefits are limited.

More importantly, it may be questioned whether it is appropriate for an entity intentionally making a false or misleading statement merely to have an administrative penalty of \$10,800 imposed upon it.⁴⁰ An intentional breach of the law should not be remedied with a mere 'slap on the wrist'; rather, such conduct should be dealt with criminally, as it may well be construed as a 'defined social problem' needing to be remedied.

Conclusion

Despite the issues surrounding the creation of the ACNC and the limits and constitutional challenges the ACNC faces in regulating the landscape of not-for-profit organisations, the establishment of the

³⁸ *Australian Charities and Not-for-profits Commission Act 2012* (Cth), s 175-20.

³⁹ *Australian Charities and Not-for-profits Commission Act 2012* (Cth), s 175-40.

⁴⁰ This raises the question of whether the sanction can achieve the aims set out in the Revised Explanatory Memorandum, *Australian Charities and Not-for-profits Commission Bill 2012*, 225.

regulator can nevertheless be viewed as essential because it recognises the unique and distinctive role that charities play in Australia.⁴¹

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⁴¹ *Australian Charities and Not-for-profits Commission Act 2012* (Cth), Preamble; Ken Henry et al, *Australia's Future Tax System: Report to the Treasurer – Part 2* (December 2009), 205; Standing Committee on Economics (Senate), *Disclosure Regimes for Charities and Not-for-Profit Organisations* (December 2008), [5.14]; Nathan MacDonald and Phoebe Duggan, 'Not-for-profits Organisations to Finally Have a Dedicated Regulator' (June 2011) *Keeping Good Companies* 264, 264.