



SUBMISSION BY THE  
**Housing Industry Association**

To  
**The Treasury**  
In relation to the  
**Governance Standards Consultation Paper December 2012**  
and the  
**Exposure Draft - Requirements for Annual Financial Reports  
under the ACNC Framework – December 2012**

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## 1. INTRODUCTION.

1. HIA is the premier industry organisation in the home building sector of the Australian economy, and represents some 30,000 members throughout Australia. It employs a professional staff of some 270 persons and forms its policies through an internal democratic system of committees made up of its members serving in a voluntary capacity. HIA Members are the builders and contractors with whom consumers deal when contracting for domestic building projects.
2. HIA is a Not for Profit association incorporated as a company limited by guarantee. Under its Constitution HIA is an organisation whose purpose is the development of the industrial resources of Australia under para 50-40 8.2 of the ITAA. HIA also sponsors the HIA Charitable Foundation, a DGR.

## 2. SUMMARY OF HIA'S COMMENTS.

3. HIA supports the application of governance standards to charities. However, HIA has concerns about the vague and subjective nature of many of the proposed standards, which fail to provide a firm legal basis for charities to assess their own compliance. There are a number of existing governance standards with clearer and better understood obligations such as that of the Australian Institute of Company Directors or the Australian Stock Exchange, which might alternatively be adopted.
4. For companies previously regulated by ASIC, the proposed governance standards would represent a new and different regime which would effectively replace the rule of law with the rule of ACNC officials.
5. Contrary to ACNC and Treasury statements, the proposed governance standards represent a significant divergence from existing corporate regulation which can only grow wider over time. For example, senior company officers such as the company secretary and the general counsel who are deemed to be liable as directors under the Corporations Act are not caught by the ACNC Act and governance standards.
6. There are also many significant uncertainties arising out of the interaction of the new standards with state law and common law which have not been appreciated by Treasury or addressed by the Consultation Paper, and which cannot be simply left for the courts to sort out.
7. HIA considers the 60 civil penalty unit limit in Standard 3 is too low, as this will apply to many minor offences not involving any dishonesty.
8. HIA is also concerned that the administrative burden of formal compliance may be excessive for smaller charities. HIA considers that the governance standards should, at least for the time being, apply only to charities with turnover in excess of \$10m (who if they are already complying with Corporations Act requirements should automatically pass).
9. In addition, HIA considers that the proposed governance standards may not be consistent with that level of business confidentiality which many charities require to protect their interests in relation to their commercial fund raising.
10. HIA sees no need for smaller registered entities to be required to prepare annual information statements and financial information statements.
11. Finally, HIA does not consider that it would be appropriate to extend any

governance standards or reporting requirements finally adopted for charities into the wider not-for-profit sector without full consideration and review.

12. HIA continues to oppose much of the Government's current approach to reform of the NFP sector, and considers that regulation of charities and DGRs should be on a completely separate basis from the regulation of other NFPs. HIA also considers that Charities and NFPs which are companies should continue to be regulated under the *Corporations Act 2001* by ASIC. HIA has previously made submissions on these issues and asks that they be again taken into account.

### 3. GOVERNANCE STANDARDS AND MANAGEMENT OBLIGATIONS

13. It has been stated by ACNC staff that it has to go down a principles-based route in order to cover all the multitudinous types of charity, but HIA considers that a more modest aim might have been selected, of covering major charities in the first instance and extending the governance regime to smaller charities at a later date. Certainly the universal, immediate, top-down approach to regulation which has been proposed carries its own disadvantages.
14. One disadvantage is that the standards completely obscure the distinction between governance and management. The proposed ACNC governance standards actually focus on how managers should operate the charity rather than on how directors should discharge their responsibilities to oversee management.
15. There are a number of existing well-known governance codes such as those of the Australian Institute of Company Directors and the Australian Stock Exchange, which actually related to governance rather than management conduct. These codes contain a reasonable level of detail and definite, ascertainable obligations with which directors can objectively assess their compliance. The ASX code also operates on the basis of 'if not, why not' – if a company does not follow the code, it is entitled to do that provided it has a reason, providing needed flexibility.
16. While the ASX Code does not apply to charities or NFPs (which cannot be ASX listed or have tradeable shares), very many of the persons who are directors of charities and NFPs are also directors of listed companies, or advisers to listed companies such as accountants and solicitors, and would be familiar with such existing standards. This familiarity on the part of directors would be a big advantage in terms of ensuring a high level of compliance by registered entities.
17. The adoption of these existing governance standards would appear more appropriate than the ones put forward by the ACNC, as they are consistent with existing law and actually relate to improving governance rather than extending the administrative enforcement powers of the ACNC.
18. The proposed governance standards, by contrast, involve an entirely new and uncertain compliance regime. While it has been stated by ACNC and Treasury that the proposed governance standards simply restated the governance requirements for incorporated charities currently regulated under the *Corporations Act 1991*, that is not in fact true, as will be discussed below.
19. But even if it were true, it must be remembered that the content of these ASIC-enforced standards has in the past been subject to significant disputation and doubt, and their easy translation into the field of unincorporated charities should not be taken for granted.

#### 4. GOVERNANCE STANDARDS AND THE RULE OF LAW

20. HIA has strong concerns about the vague and subjective nature of many of the proposed standards, which fail to provide a firm legal basis for charities and their directors to assess their own level of compliance.
21. No-one could argue with unambiguous obligations on a responsible entity to ensure that their registered entity not commit an indictable offence, or meet other definite requirements such as ensuring that the entity publishes audited accounts. But most of the obligations in the proposed governance standards are much less definite than this.
22. In particular, the suggested governance standards frequently use term such 'take reasonable steps', provide 'adequate opportunity' and act 'in a responsible manner'. While apparently adopted to cover all possibilities and all sizes of charity, such vague requirements tend to undermine the rule of law.
23. In the charitable context, these are words of such all-embracing vagueness that their interpretation is a matter of individual desire, and corporations law can give only limited interpretative assistance. This vagueness is undesirable when there are statutory penalties for non-compliance, and very wide ACNC administrative enforcement powers.
24. In HIA's view, the current situation is one in which a government is clear about what it intends, and sees its proposed regulations in that light, without appreciating that to an outside observer the regulations can bear a wide variety of different meanings. The principles stated might be appropriate as a set of guidelines but fall short of an appropriate regime of legal enforcement, and also fail to provide a firm legal basis for professional advisers to charities to give meaningful advice on compliance.
25. Generally speaking, lawyers use such subjective language as 'reasonable' (notably in contracts) when they wish to ensure that in the event of a disagreement, the actions concerned can be the subject of judicial review through litigation at the instance of an aggrieved party. A court will then adjudicate, on the evidence, as to what was 'reasonable' in these particular circumstances as between the individual parties.
26. In statutes, such subjective words are normally used to modify what would otherwise be an absolute duty, to provide citizens with a defence to a suit or prosecution in circumstances where their actions have harmed others (such as in Tort law, in Corporations law, or in Work Health and Safety laws). Such defences are available to be considered by courts and tribunals on their merits.
27. However, in this case, the actions are to be subject (in the first instance) to continuing administrative oversight by a third party, the ACNC. This is a very different legal environment. When applied on a continuing basis, it enables ACNC to investigate and take action whenever its officials consider that the actions of a charity were not 'reasonable' or 'responsible'.
28. For example, the current criteria for disqualification of directors under the Corporations Act relate to conviction of an indictable offence or bankruptcy. These are serious matters with serious consequences. By contrast, a director of a charity which provides a young person with one day's unpaid clerical work experience in its office (a per se breach of the Fair Work Act not requiring intent, and attracting a maximum civil penalty 60 penalty units) thereby causes the charity to breach governance standard 3 and (whether the director is charged and convicted or not) may be disqualified as a director of a

responsible entity (charity) by ACNC.

29. Under Division 80 of the ACNC Bill, the Commissioner may give a registered entity a warning notice or a written direction if 'the Commissioner reasonably believes that the entity has not complied with a governance standard, or that it is more likely than not that the entity will not comply with a governance standard'. The entity must comply with the written direction on pain of suspension or removal, and while a person may appeal to the AAT or a court, the Commissioner's decision stands (ss.165-50, 170-25) while the appeal is pending.
30. These direction powers are very wide, and as matter of day to day administrative practice by registered entities, it is concerning that a person who is a 'responsible entity' cannot be sure that what they are doing will be considered 'reasonable' by the ACNC. It is inherent in human nature that people will differ as to what is, in any particular situation, 'reasonable', and inevitable that a particular person's view as to what is reasonable will in some cases not be that of the Commissioner. HIA is concerned that the subjective nature of the governance standards will create an area of considerable uncertainty and disputation.
31. To say that ACNC is unlikely to do anything unfair or improper misses the point - a legal liability for disqualification in certain very specific serious circumstances is to be broadened out into an administrative discretion to disqualify for what are relatively trivial matters. An obligation to obey the law is converted into an obligation to obey the officials. This is not in the best legal traditions of protection of the rights of the individual.
32. It is also inevitable that such broad brush obligations in Regulations will over time be clarified, supplemented and expanded on through ACNC education activities. Red tape quickly expands to fill such an administrative vacuum, not least because the regulated demand it in order to obtain clarity of obligations.
33. There is a further point of caution that needs to be appreciated. A very wide administrative discretion is not always the easiest thing for an administrator to manage. Where the decision-maker's information is incomplete, the offence is a subjective one, the available enforcement options are numerous, and the consequences are unclear, administrative decision-making is made much more difficult and unintended results frequently follow. The Pan Pharmaceuticals case is a perfect illustration of this point.
34. HIA suggests that, at least initially, the wide and general words of the standards be replaced by the definite obligations that are in many cases given in the consultation paper as examples of what ACNC would expect to be included in their context. For example, rather than say "A registered entity must: a) be able to demonstrate ...its purposes and character as a not-fro-profit entity", the standard could say "A registered entity's governing document must include [those specific details set out in Division 50 of the ITAA 1997]".
35. Likewise, rather than saying that a registered entity must be 'accountable' and 'transparent', the standard should set out a limited number of specific requirements drawn from the Corporations Act such as the requirement to hold annual meetings and publish accounts and annual reports.
36. It might be argued that the Corporations Act criteria are too limited. However they would be a good start on which to build. Such certainty would be welcomed by most charities.
37. Later in this submission HIA argues that governance standards should apply

for the time being only to larger charities with turnovers in excess of \$10m. In such cases the specific obligations such as this would present no problem.

## 5. INTERACTION WITH STATE LEGISLATION AND COMMON LAW

38. HIA appreciates that, apparently for constitutional reasons, the ACNC legislation places the regulatory duty on the registered entity rather than on the responsible entity (director). This leads to the likelihood of inconsistency with State legislation that places duties on directors of incorporated associations. Unlike Corporations Act duties, these will not be switched off when the governance standards come into operation.
39. Also, once the Corporations Act is switched off in relation to regulated entities, existing common law rights and duties will remain, and previous common law duties (overridden by inconsistent provisions of the Corporations Act) will revive, particularly in relation to duties of directors and rights of members. How will the governance standards interact with the common law? Are the governance standards intended to create private rights, and if not, will the switching off of the Corporations Act mean that existing private rights of action of company members (e.g. to seek a general meeting of members or to bring an action in the name of the company against a director for misfeasance) will disappear?
40. These are all very important questions that have not been addressed by the Government. It is no answer, and denigration of those subject to this new regime, to say that the courts will work things out over time. It is the Commonwealth that is creating a new regulatory regime for particular types of companies, and it is the Commonwealth that must take responsibility for ensuring that it does not cause serious and avoidable legal problems while doing so.
41. HIA also notes that the proposed Governance Standards place no obligation on registered entities in relation to company officers and managers who are not regulated entities i.e. Directors and Trustees. This means that, for example, a company secretary or general counsel who is not also a director will have no liability under the new Standards, nor under the Corporations Act once this is switched off. Their liability, if any, will derive from the common law.
42. This is a very substantial change from existing corporations law. Much of the recent James Hardie litigation involving Mr Peter Shafron, for example, would have had quite a different outcome under an ACNC regime. It is therefore already clear, even before the switch of enforcement from ASIC to ACNC has occurred, that a divergence of corporate regulation is occurring, which over time can only grow wider.
43. HIA reiterates its previous submission that regulation of companies should remain with ASIC under the *Corporations Act 2001*.

## 6. DISCLOSURE OF CONFLICT OF INTEREST

44. There seems no justification (standard 6-3) for directors of incorporated charities to have to disclose conflicts of interest to all members of the company, rather than simply to the other directors as at present. It also seems completely impractical in the case of a company with thousands of members.

## 7. PENALTIES

45. HIA points out that the proposed governance standard 3 – compliance with Australian laws – includes conduct which may be dealt with by way of a civil penalty of 60 units or more. This is a very low standard, and in HIA's view should be increased to, say, 100 penalty units.
46. A civil penalty of up to 60 penalty units is the penalty provided, for example, for most breaches of the Fair Work Act 2009, which are also absolute offences containing no element of dishonesty or guilty intent. Given the complexity of workplace law and the limited compliance resources of most charities, this is a fertile area of mistakes. Thus, a registered entity which inadvertently misclassifies or underpays a staff member and thereby breaches a Modern Award will also breach Standard 3, would have to notify the ACNC of this, and may be subject to written direction by the ACNC. Similarly, there are many traffic offences attracting a penalty of up to 60 units which could apply in relation to a motor vehicle owned by the registered entity.
47. While a responsible entity may be able to claim a protection under standard 6, the registered entity itself would have no defence. It is difficult to see what advantage is achieved by registered entities having to notify the ACNC of all these minor breaches which do not involve dishonesty or recklessness and are irrelevant to the stated aims of the governance standards.

## 8. ADMINISTRATIVE BURDEN

48. HIA is also concerned that the administrative burden of formal compliance with these governance standards, even having regard to (or perhaps particularly because of) their vaguely expressed requirements, may be excessive for smaller charities.
49. HIA considers that the governance standards should, at least for the time being, apply only to charities with turnover in excess of \$10m (who if they are already complying with Corporations Act requirements should automatically pass). At least this will provide an opportunity to see how the standards work out in practice when administered by properly resourced professional organisations.

## 9. NEED FOR COMMERCIAL CONFIDENTIALITY

50. There are many charities which are running commercial operations to fund their activities. As part of that activity, there are commercial-in-confidence considerations which may impinge on the 'accountability to members' governance standard. Such information would be valuable to competitors in the marketplace and would not normally be disclosed by any company. There should be a specific carve-out from Standard 2 of information relating to the commercial activities of regulated entities.

## 10. NOT-FOR-PROFIT SECTOR GENERALLY

51. Finally, HIA considers that it would certainly not be appropriate to extend any governance standards finally adopted for charities into the wider not-for-profit sector without full consideration and review. This is a much more diverse group than charities, and the problems identified above would apply with



correspondingly greater force. In addition, as no public money is involved, there is less justification for legal interference at public expense in the internal affairs of entities such as clubs and associations.

## 11. EXPOSURE DRAFT – REQUIREMENTS FOR ANNUAL FINANCIAL REPORTS UNDER THE ACNC FRAMEWORK

52. There is a new requirement for all registered entities to prepare an annual information statement and an annual financial information statement. However, there is no detail surrounding this requirement. Most of the large registered entities are fully disclosing their financial information in their current annual financial statements to ASIC.
53. For Charities, the annual information statement is yet to be finalised, however it proposed to cover;
  - a. how the charity works towards its charitable purpose (over the past 12 months and future 12 months);
  - b. number of volunteers and paid staff;
  - c. type of beneficiaries who benefit from your charity's activities.
54. While there may be some merit in requiring this information from larger charities (almost all of whom are already disclosing it in their annual reports), HIA sees no need for this new requirement to be imposed on small registered charities. In the case of small charities it will simply generate a great deal of paper which no-one outside the entity will ever read.
55. There is no clarification whether such requirements will also apply to all not-for-profit entities in the future, but this seems to be what is intended. HIA considers that this would be inappropriate in the case of smaller NFPs such as clubs, as non-charitable NFPs are not dealing with public donations and there is no corresponding public right to know these details.
56. There is also a lack of detail on how the annual financial reports and annual information statements are to be lodged with the ACNC. HIA presumes this will be via the ACNC website, which would be the most convenient process.
57. Whilst the paper mentions timeframes for lodgements of the financial reports, it does not mention anything about penalties that would be applicable, if in any case this timeframe is not met. If this is to be at the discretion of ACNC, clear guidelines need to be adopted if this is to be fairly administered.
58. There seems to a lack of clarification in the explanatory material as to what will be the ongoing role of ASIC. HIA understands that those entities currently reporting to ASIC would cease to do so and report only to ACNC, but reporting to the ATO will broadly be unchanged (although apparently ACNC will have a role in overseeing the annual self-reviews of the organisation's tax status).
59. HIA considers that if tax matters are to stay with the ATO and not be transferred to ACNC, then ACNC will not in fact be a 'one stop shop' as promised, and there is therefore no reason why corporate financial matters should not stay with ASIC and not be transferred to ACNC.

Housing Industry Association Limited

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