Ten matters to consider when designing improved nonprofit regulation for Australia

By Professor Myles McGregor-Lowndes

There are numerous issues to be considered in creating a better regulatory environment for Australia's nonprofit organisations. Here are some suggestions and please send in your comments or additions to the list. Once again the usual CPNS chocolate frogs will be 'snail mail' dispatched to contributors.

1. All nonprofit organisations should be considered in regulatory reform - not just community welfare or charitable organisations. The focus of the regulation should not be based merely on legal forms, tax status or activity alone, but the essential characteristics of nonprofit organisations.

2. A strong and robust political champion is required to operate across whole of government and provide leadership to largely uninterested and myopic government departments and state governments.

3. Australia has fallen behind globally converging regulatory standards for nonprofit organisations and a strategy of incremental reform is a fast diminishing option. Paradigm shifts will be required with significant costs and consequences, if reform opportunities are not taken soon.

4. A central independent regulator, whatever its form, will need significant resources: an under resourced body will be worse than the present situation. There may be some savings in a transition. Everyone calls for more sector regulation, but no one puts up their hands to pay for it.

5. Regulatory response needs to be proportionate, particularly at the large and small end of the nonprofit environment - no one size fits all.

6. Any attempt to rationalise the chaotic regulatory landscape will produce winners and losers, particularly in relation to taxation concessions and exemption from regulation.

7. The definitional issues of Public Benevolent Institutions have largely been driven by Fringe Benefit Tax (FBT) salary sacrifice concessions and not donation tax deductibility. Vested interests (with much to gain or lose in salary concessions) often argue the case using the proxy of 'donation deductions', thus hiding the underlying policy issue of poor remuneration of sector workers.

8. In relation to annual reports, sector specific accounting standards are required which mesh with broad standards and more emphasis needs to be placed on the narrative account of how organisations are achieving their stated objects.

9. The Australian Bureau of Statistics (ABS) requires assured long term funding to compile and update baseline data on the whole of the nonprofit sector; this provides an essential part of the evidence base for policy makers.

10. The governance body (e.g. board, trustees, management committee and the membership forum - if any) should be the central focus for ensuring appropriate behaviour of organisations.

Any suggestions or comments can be emailed to CPNS (cpns@qut.edu.au)

Comments and suggestions will then be uploaded to the CPNS Wiki

1. All nonprofit organisations should be considered in regulatory reform - not just community welfare or charitable organisations. The focus of the regulation should not be based merely on legal forms, tax status or activity alone, but the essential characteristics of nonprofit organisations.

Efficiency and effectiveness would be promoted in regulatory design, meta-policy development and community understanding if there was a whole of government approach to non-government and non-business organisations. The regulatory framework should not be defined by government departmental silos, organisational purpose or activity alone. At the margins the definitions of nonprofit organisation/third sector organisations will be contested, but there is significant agreement on the core as demonstrated by the ABS Satellite Accounts project. Such an approach permits a central regulator to be charged with building the public's trust and fidelity of such organisations, whatever their purposes, which avoids constraining missions such as protecting the taxation base (Australian Taxation Office), financial investors (ASIC) or a specific industry (e.g. arts/sports/health). The community needs protection from those who would abuse the nonprofit constraint.

2. A strong and robust political champion is required to operate across whole of government and provide leadership to largely uninterested and myopic government departments and state governments.

Jurisdictions which have moved beyond piecemeal, ineffectual reforms have been characterised by a strong political champion who can bring different parts of government together to focus on broad issues, provide integrated solutions and mediate powerful community stakeholders concerns. The limited implementation of previous reports is evidence of this requirement.

3. Australia has fallen behind globally converging regulatory standards for nonprofit organisations and a strategy of incremental reform is a fast diminishing option. Paradigm shifts will be required with significant costs and consequences, if reform opportunities are not taken soon.

In comparison to England, Wales, Ireland, Canada, New Zealand and Singapore, Australia is now lagging in its nonprofit regulatory environment. The direct result is that in the global market for philanthropic funds, Australian organisations are at a competitive disadvantage because of the confusing and ineffective regulatory framework.

The current regulatory framework constrains the ability of nonprofit organisations to provide an effective and efficient alternative to government or for-profit organisations. The current regulatory environment also hinders the ability of nonprofit organisations to provide goods and services, create social capital and contribute to civil society.

In addition, Australia's recent history of failure to act in any meaningful way to reforms as suggested by the failure to act on the recommendations...
A central independent regulator, whatever its form, will need significant resources: an under resourced body will be worse than the present situation. There may be some savings in a transition. Everyone calls for more sector regulation, but no one puts up their hands to pay for it.

The 2007/08 expenditure of the Charity Commission of England and Wales which supervises about 190,000 organisations with 471 staff has a budget of £33.5 million. The New Zealand Charity Commission regulates about 25,000 organisation with a budget of approximately $NZ73.7 m. The US Internal Revenue Service (IRS) has 316 full time equivalent staff, 159 of who are engaged in audits. In comparison Australia’s largest nonprofit regulatory agency is the Australian Taxation Office (ATO) with approximately 60 staff. Moreover, incorporated associations and fundraising offices at the state level are chronically understaffed and do little effective pro active regulation.

Any move to a central independent regulator requires a well resourced agency or it will fail and place the nonprofit sector, organisations and the community in a worse position than the current regulation framework.

Private donors, government funders and the media on behalf of the general public all call for greater reported detail on nonprofit organisational accounts and activities. However, at the same time they express a strong desire for less expense on administration and fundraising and do not wish any of their contributions to go towards such expenses. Such measures are not costless, even when performed by volunteers. A paradox that needs to be solved.

5. Regulatory response needs to be proportionate, particularly at the large and small end of the nonprofit environment - not one size fits all.

Mature nonprofit regulatory regimes are characterised by different regulatory tools and exemptions at both ends of the spectrum. For example, small organisation are largely exempt in England and Wales #fn1 (under £10,000 and likely to be increased to £25,000) and IRS threshold in the United States is US $25,000. #fn2 Of the one million organisations registered with the IRS in 2004, approximately 63 percent had annual revenues of less than US $25,000 and were not required to file with the IRS. Of those obligated to file with the agency, nearly 63 percent reported total budgets of less than US $200,000.

In Queensland it is estimated that 4 out of 5 incorporated associations have fewer than 100 members with total assets and total annual turnover of less than US $50,000. In Victoria, 26.23% of incorporated associations have fewer than 20 members with only 9.3% having at least US $200,000 in annual revenue and US $500,000 in assets. #fn3 In New South Wales a sample of 5,000 incorporated associations found that approximately 66% of organisations had an annual income under US $500,000. #fn4 An examination of Deductible Gift Recipient (DGR) endorsement returns indicates that 25% of DGRs have an annual income of less than US $8,213 and 50% less than US $55,304. #fn5

At the other end of the scale there are some very large organisations with complex branch structures. However, some very large organisations (e.g. churches) are actually made up of many small organisations. We need to understand much more about the characteristics of nonprofit organisations before we can with any confidence design proportionate regulation that details exempt or excepted bodies.

In the UK, large organisations or those with special regulation are either exempt or excepted bodies. #fn6 for example large educational institutions, cultural bodies and religious bodies. In the U.S the IRS has ‘group rulings and exemptions’ for religious bodies with large branch structures. #fn7

6. Any attempt to rationalise the chaotic regulatory landscape will produce winners and losers, particularly in relation to taxation concession and exemption from regulation.

It is to be expected in an undisciplined policy environment which has been lacking any evidence base, that privileged anomalies will have risen, particularly in relation to taxation exemption and concessions. The move to a simpler, rational, evidenced based regulatory framework will have winners and losers. Leadership is required by all stakeholders to find a way to move out of the swamp.

7. The definitional issues of Public Benevolent Institutions have largely been driven by Fringe Benefit Tax (FBT) salary sacrifice concessions and not donation tax deductibility. Vested interests (with much to gain or lose in salary concessions) often argue the case using the proxy of ‘donation deductions’, thus hiding the underlying policy issue of poor remuneration of sector workers.

The debate about the fate of PBIs would be more rational if it was based on the central issues of various stakeholders, rather than upon often inconsequential issues which are easier to promote. The issue of inadequate remuneration for sector staff, professionals and management needs to be debated openly and all options for resolution of the underlying issue need to be canvassed. The tax expenditures tools via the PBI FBT exemption is probably not the best device for rectifying the remuneration issue given the distortion it causes in other areas.

8. In relation to annual reports, sector specific accounting standards are required which mesh with broad standards and more emphasis needs to be placed on the narrative account of how organisations are achieving their stated objects.

The call for financial accounts to inform the public about the relative worth of organisations is growing. Standards that enable a sensible financial comparison to be attempted need to be devised and applied. The current regime of ‘vanilla business accounting standards’ are inappropriate and out of step with the rest of the developed world.

Further, financial reports as used in for-profit markets are an incomplete and perhaps misleading tool for nonprofit organisations. More emphasis should be placed on an annual narrative which explains the mission of the organisation, how it intends to achieve that mission and how much it has achieved in the period. A good example is the Charity Commission’s SIR (Summary Information Return).

9. The Australian Bureau of Statistics (ABS) requires assured long term funding to compile and update baseline data on the whole of the nonprofit sector; this provides an essential part of the evidence base for policy.

Australia lacks the evidence base to model policy impacts on the sector. The impact statement in relation to the introduction of GST and capping of certain FBT exemptions provide compelling case studies of the price paid for such ignorance. Smart regulation requires an extensive evidence
base: we as a country know how many cattle there are from week to week, but have no idea of the number of nonprofit organisations from decade to decade.

10. **The governance body (e.g. board, trustees, management committee and the membership forum - if any) should be the central focus for ensuring appropriate behaviour of organisations.**

Those who have the direct responsibility for 'monitoring, judging and influencing' organisations should be the focus of the regulatory effort to ensure the fidelity of the sector as a whole. Better organisational governance at this level will translate into better esteem of the whole sector. 'Stick and carrot' regulatory strategies are required.

The excesses of the reliance on ’contracts’ by government departments has led to an over emphasis on the 'stick' and created many 'risk averse' boards. Government departments have marginalised boards by interference in management decision making and excessive management reporting. Imposition of 'quality standards', forced disclosure of management records, with forensic restrictions on expenditures, take away the responsibilities of boards for the achievement of their organisation’s mission.

Footnotes
(3) Stronger Community Organisations Project, Report of the Steering Committee, Oct 2007 at P13
(6) Refer, [http://www.charitycommission.gov.uk/supportingcharities/ogs/g057a001.asp](http://www.charitycommission.gov.uk/supportingcharities/ogs/g057a001.asp)