
REGULATING THE NOT-FOR-PROFIT SECTOR

July 2011

Joyce Chia, Matthew Harding, Ann O'Connell and Miranda Stewart

Melbourne Law School, email: law-nfp@unimelb.edu.au.

INTRODUCTION

This Working Paper presents research on regulation of the Not-for-Profit sector, conducted as part of the Not-for-Profit Project, a three-year research project funded by the Australian Research Council which began in 2010.¹ The project aims to provide the first comprehensive Australian analysis of the legal definition, taxation, and regulation of not-for-profit organisations (NFPs).

In the federal Budget for 2011-2012, presented in May 2011, the Gillard government announced its intention to establish a national NFP regulator.² The government proposed the establishment of a new independent statutory agency, the Australian Charities and Not-for-profits Commission (ACNC) by 1 July 2012. The ACNC will be headed by a Commissioner appointed by the Government which will report to Parliament through the Assistant Treasurer. Its establishment will be preceded by the establishment of an implementation taskforce in Treasury from 1 July 2011 and by the Australian Taxation Office (ATO) structurally separating its determination of charitable status from its administration of tax concessions. The ATO will also provide corporate service support to the ACNC. The Commonwealth Government will also negotiate with the States and Territories on the possibility of a new national regulator in the future.

The ACNC will be responsible for determining the charitable, public benevolent institution, and other not-for-profit status of organisations for all Commonwealth purposes. It will also provide education and support to the sector; implement a 'report-once use-often' general reporting framework for charities; and implement a public information portal.

The Budget proposal builds on the federal Treasury's Consultation Paper, *Scoping Study for a National Not-for-Profit Regulator*, which was released in January 2011 ('Consultation Paper').³ Further details of the proposal were announced in the Treasury's *Final Report on the Scoping Study for a National Not-for-Profit (NFP) Regulator*, released on 4 July 2011 ('Final Report').⁴ The recommendations of this Final Report are discussed throughout this Working Paper.

¹ A version of this Working Paper was provided as a submission to the Australian Treasury, *Scoping Study for a National Not-for-profit Regulator* (Consultation Paper, No 1934, 21 January 2011) <<http://treasury.gov.au/contentitem.asp?NavId=037&ContentID=1934>>.

² Hon Bill Shorten MP and Hon Tanya Plibersek MP, *Making It Easier for Charities to Help Those Who Need It* (Media Release, No 77, 10 May 2011) <<http://assistant.treasurer.gov.au/displaydocs.aspx?doc=pressreleases/2011/077.htm&pageID=003&min=brs&Year=&DocType=0>>; Australian Treasury, *Budget 2011-12, Part 1, Revenue Measures, Treasury* <http://www.budget.gov.au/2011-12/content/bp2/html/bp2_revenue-07.htm>.

³ Treasury, *Scoping Study for a National Not-for-profit Regulator*, above n 1.

⁴ Treasury, *Final Report: Scoping Study for a National Not-for-Profit Regulator* (No 2054, 4 July 2011) <<http://www.treasury.gov.au/contentitem.asp?NavId=035&ContentID=2054>>.

The proposal for a new regulator is part of a wider process of reforms of the NFP sector being undertaken by the Australian Government, as well as some reforms that are ongoing by various State governments. In recent decades, there have been several important inquiries and reports on reform of the NFP sector in Australia, including:

- The report of the Industry Commission on *Charitable Organisations in Australia* (1995);⁵
- The report of an independent inquiry chaired by Justice Sheppard on the definition of charities (2001) ('Sheppard Inquiry');⁶
- The parliamentary report on disclosure requirements of NFP organisations (2008);⁷
- The report of the Productivity Commission on the contribution of the NFP sector (2010);⁸ and
- The report of the Henry Review on the taxation system, including taxation of NFPs (2010).⁹

In addition, the Victorian Government has pursued reform of the NFP sector, which has generated significant reports including, relevantly, reports on the regulation of the NFP sector by the State Services Commission and the Stronger Community Organisations Project.¹⁰

With the exception of the early Industry Commission report,¹¹ the Australian reports have consistently recommended the introduction of a national NFP regulator, albeit in differing forms.

⁵ Industry Commission, *Charitable Organisations in Australia* (16 June 1995) <<http://www.pc.gov.au/ic/inquiry/45charit>>.

⁶ Ian Fitzhardinge Sheppard, Robert Fitzgerald and David Gonski, *Report of the Inquiry into the Definition of Charities and Related Organisations* (2001) <<http://www.cdi.gov.au/html/report.htm>>.

⁷ Senate Standing Committee on Economics, *Inquiry into the Disclosure Regimes for Charities and Not-for-Profit Organisations* (2008) <http://www.aph.gov.au/senate/committee/economics_ctte/charities_08/index.htm>.

⁸ Productivity Commission, *Contribution of the Not-for-Profit Sector* (Research Report, 11 February 2010) <<http://www.pc.gov.au/projects/study/not-for-profit/report>>.

⁹ Treasury and Australia's Future Tax System Review Panel, *Australia's Future Tax System—Final Report* (2 May 2010) <http://taxreview.treasury.gov.au/content/Content.aspx?doc=html/pubs_reports.htm>.

¹⁰ Karen Spindler, *Improving Not-For-Profit Law and Regulation: Options Paper* (Allen Consulting Group, 1 December 2005) <<http://www.allenconsult.com.au/publications/view.php?id=314>>; Christine Parker, *Self-Regulation and the Not-for-Profit Sector* (State Services Authority, May 2007) <[http://www.ssa.vic.gov.au/CA2571410025903D/WebObj/NFP_Research_Parker/\\$File/NFP_Research_Parker.pdf](http://www.ssa.vic.gov.au/CA2571410025903D/WebObj/NFP_Research_Parker/$File/NFP_Research_Parker.pdf)>; State Services Authority (Vic), *Review of Not-for-Profit Regulation: Final Report* (September 2007) <[http://www.ssa.vic.gov.au/CA2571410025903D/WebObj/NFP_FinalRpt/\\$File/NFP_FinalRpt.pdf](http://www.ssa.vic.gov.au/CA2571410025903D/WebObj/NFP_FinalRpt/$File/NFP_FinalRpt.pdf)>; Steering Committee, *Stronger Community Organisations Project* (Victorian Government, November 2007) <<http://www.dpcd.vic.gov.au/web14/dvc/dvcmain.nsf/headingpagesdisplay/community+developmentoffice+for+the+community+sectorbackground+to+the+action+plan>>; Susan Pascoe, *Regulating the Not-for-Profit Sector* (State Services Authority, January 2008) <[http://www.ssa.vic.gov.au/CA2571410025903D/WebObj/NFP_Research_Pascoe/\\$File/NFP_Research_Pascoe.pdf](http://www.ssa.vic.gov.au/CA2571410025903D/WebObj/NFP_Research_Pascoe/$File/NFP_Research_Pascoe.pdf)>.

¹¹ The Commission concluded that there was not a "convincing" case for establishment of national monitoring agency, and suggested many of the perceived benefits could be achieved through greater inter-

The Budget proposals implement these recommendations. This Working Paper draws on the research conducted as part of the Not-for-Profit Project on the issue of regulation to address some of the key issues raised by the proposal for a new regulator. It is anticipated, however, that the Project will continue work on this aspect. The key issues addressed here are:

- The goals of regulation;
- The form of a regulator, including constitutional and jurisdictional issues;
- The scope of the regulator, including in relation to legal entity forms and its functions; and
- Funding of a regulator.

The Final Report also confirmed that the Australian Government will adopt a statutory definition of charity, based on the recommendations of the Sheppard Inquiry and on further consultation, and will seek to harmonise the definition across Australian jurisdictions. While this is not separately addressed in this Working Paper, it is a topic the Not-for-Profit Project is considering and it has published a literature review on this aspect.¹²

GOALS OF REGULATION

Identifying the correct goals for regulation is fundamental to the design and effectiveness of any regulatory regime. Several reports have helpfully considered the question of the goals of regulating the NFP sector and it has also been considered in some detail by Jonathon Garton.¹³ Yet too often these regulatory goals are commonly put in terms of generic regulatory principles, or draw too heavily upon theory derived from the regulation of markets. The framework for understanding regulatory goals that is proposed here integrates the insights of earlier scholars to provide a deeper and more contextually based understanding of the appropriate regulatory goals for a national NFP regulator.

Understood in its broadest sense, regulation seeks to change or channel behaviour in desirable ways. It is therefore critically important to understand the characteristics of the behaviour that is sought to be regulated, as well as to identify the desirable behaviour that is not presently being achieved. The first and most important lesson of regulatory theory is the significance of *regulatory context*.

The Consultation Paper usefully set out some of the distinctive aspects of the regulatory context of the NFP sector, including:

- The focus of organisations on achieving a community, altruistic or philanthropic purpose (the mission orientation of NFPs);

governmental cooperation and more specific regulatory mechanisms: Industry Commission, *Charitable Organisations in Australia*, above n 5, 210.

¹² Joyce Chia et al., *Defining Charity: A Literature Review* (Not-for-Profit Project, Melbourne Law School, 23 February 2011) <<http://tax.law.unimelb.edu.au/download.cfm?DownloadFile=560AEA8E-5056-B405-51449B7990F9ABEF>>.

¹³ Spindler, *Improving Not-For-Profit Law and Regulation: Options Paper*, above n 10; Parker, *Self-Regulation and the Not-for-Profit Sector*, above n 10; Jonathon Garton, *The Regulation of Organised Civil Society* (Hart Publishing, 2009).

- The provision of what are commonly termed in economics ‘public goods’ or ‘quasi public goods’ which cannot be efficiently provided by the market;
- The diversity of the sector, including in size and activity;
- The foundational role of the sector in enabling an active civil society;
- The growth of the NFP sector in part due to government contracting for delivery of government services; and its
- Contribution to community wellbeing.

There are, however, other distinctive aspects of the regulatory context which deserve mention, including:

- The mission and public benefit focus of the NFP sector means that NFPs’ interests are often closely aligned with both their members and their decision makers;¹⁴
- The autonomy of the sector;¹⁵ and
- The fact that, because the activity is not conducted for profit, but is conducted altruistically and often on a voluntary basis, the sector is more vulnerable to regulatory burdens than in a sector where private self-interest remains a strong offsetting impulse.

These features suggest that the sector should not be heavily regulated. It is also important to recognise that different parts of the sector may already be subject to forms of self-regulation. The public-spirited and mission-oriented nature of the sector, in large part, channels behaviour in desirable ways. NFPs are partly regulated through their accountability to their clients, members, and funders (including government). The sector is highly vulnerable to regulatory burdens. Importantly, the desirable nature of the autonomy of the sector and its foundational role in civil society should result in governments giving organisations wide latitude in the performance of their missions.

The Consultation Paper did not address concepts of self-regulation or co-regulation of NFPs, which is becoming a prominent area of interest in NFP studies abroad, including the recent report of the Association of Chief Executives of Voluntary Organisations (ACEVO) in the UK,¹⁶ and in the

¹⁴ Pascoe, *Regulating the Not-for-Profit Sector*, above n 10, 17.

¹⁵ Panel on Accountability and Governance in the Voluntary Sector, *Building on Strength: Improving Governance and Accountability in Canada’s Voluntary Sector* (February 1999) <http://www.ecgi.org/codes/documents/broadbent_report_1999_en.pdf>, 9-10.

¹⁶ Better Regulation Task Force (UK), *Better Regulation for Civil Society: Making Life Easier for Those Who Help Others* (November 2005) <<http://archive.cabinetoffice.gov.uk/brc/upload/assets/www.brc.gov.uk/betregforcivil.pdf>>, 8-9, 48-49; Association of Chief Executives of Voluntary Organisations (ACEVO), *High Level Report of the ACEVO Taskforce On Better Regulation: Public Impact Centred Regulation for Charities* (2010) <<http://www.acevo.org.uk/Document.Doc?id=733>>, 33.

United States.¹⁷ This work is summarised in the Appendix. Valuable studies have also been conducted by Susan Pascoe and Professor Christine Parker for the State Services Authority.¹⁸

As Parker suggests, there is promise in encouraging forms of self-regulation in conjunction with a national regulator in the sector because of characteristics such as the importance of trust and the pursuit of community benefit. Self-regulatory schemes have significant benefits for a coherent regulatory scheme, including: internalisation of good governance and practices; participation and development by the sector; and promotion of best practice. However, self-regulatory schemes are likely to be more effective in conjunction with state regulation, which can address problems such as opt-out by weak or small organisations, inadequate enforcement, and excessive competition. A national regulator could assess existing and prospective self-regulatory schemes and endorse effective schemes which meet or exceed regulatory requirements, and offer incentives such as exemptions, fast-tracking or information transfer to relieve the regulatory burdens of those involved in such schemes.¹⁹

The key distinction between NFPs and other private sector organisations is that NFPs are ultimately driven by pursuit of public or community benefit, rather than profit. As a result, the regulation of this sector should ultimately be designed to facilitate the sector's achievement of this goal. The Consultation Paper, by suggesting as a goal the "promot[ion] of a strong and sustainable NFP sector", recognises this point. We suggest it is worth emphasising, however, that the ultimate goal of regulating the sector is facilitating the sector to fulfil, in diverse ways, their goals for the public or community benefit.²⁰

The idea of regulation as 'facilitative' rather than 'controlling' appears, at first, to contradict prevailing assumptions that government regulation is not about developing the sector but rather about ensuring the accountability of the sector. The Final Report, for example, concludes that the regulator should not be a 'facilitator or advocate' of the sector.²¹ In part, this concern derives from the traditional focus of regulatory theory on markets, where regulation often seeks to correct 'market failures' or market abuses. In part, this also stems from the traditional image of the State as a sovereign which seeks to 'command and control'. Ultimately, however, the key is to recognise that the foundational purpose of all regulation—including that of the market—is to facilitate the benefits that flow from the activity.

This analysis suggests that a national regulator should focus on two aspects: first, the under-regulated interest of ensuring loyalty to the purposes of the NFP, and effectiveness in achieving its purpose, and second, streamlining regulation to minimise the compliance burden and prevent duplication. By focusing on loyalty to purpose and effectiveness, the regulator will naturally encompass the functions of ensuring the legitimacy of governance arrangements and organisational purposes. These functions can be incorporated into the processes for determining

¹⁷ See, eg, The National Center on Philanthropy and the Law, *Study on Models of Self-Regulation in the Nonprofit Sector* (Independent Sector, 2005) <http://www1.law.nyu.edu/ncpl/resources/rp_report.html>.

¹⁸ Parker, *Self-Regulation and the Not-for-Profit Sector*, above n 10; Pascoe, *Regulating the Not-for-Profit Sector*, above n 10.

¹⁹ See Better Regulation Task Force (UK), *Better Regulation for Civil Society: Making Life Easier for Those Who Help Others*, above n 16, 8-9, 48-49.

²⁰ See also volume 2 of Ontario Law Reform Commission, *Report on the Law of Charities* (1996). This is summarised in Appendix B.

²¹ Treasury, *Final Report: Scoping Study for a National Not-for-Profit Regulator*, above n 4, 16.

tax concessions, satisfying governance requirements for funders, and providing information that can inform donor choice.

From the ultimate goal of facilitation of public benefit by NFPs, a number of second-order goals can be identified:

- The promotion of public trust and confidence in NFPs;
- Ensuring the commitment of NFPs to purposes for the public benefit; and
- Improving the effectiveness of NFPs.²²

Analytically, these goals can be distinguished from ‘third-order’ objectives such as:

- Ensuring appropriate transparency and accountability to donors, beneficiaries, other stakeholders, and the public;
- Promoting compliance with legal obligations;
- Ensuring efficient and effective allocation of resources;
- Preventing abuse, self-dealing or other misuse of NFPs; and
- Ensuring the sustainability of community organisations.

To this familiar list we would add more ‘positive’ objectives such as: promoting capacity building within the sector; and promoting a strategic, enterprising approach to management.²³ An important part of the regulatory context is that the NFP sector is often a locus of social innovation, and a regulatory culture that focuses too heavily on a “law-and-compliance” approach may hamper that innovation.²⁴

It is also analytically important to distinguish these goals and objectives from what are generally good principles of regulatory design which apply to all regulatory contexts. In respect of principles, we draw attention to Karen Spindler’s useful summary that regulation should be:

- The minimum necessary to achieve objectives;
- Not unduly prescriptive;
- Accessible, transparent and accountable;
- Integrated and consistent with other laws;
- Communicated effectively;

²² See Ontario Law Reform Commission, *Report on the Law of Charities*, above n 20, 17. This identifies the last two underlying objectives.

²³ See generally Association of Chief Executives of Voluntary Organisations (ACEVO), *Public Impact Centred Regulation*, above n 16.

²⁴ *Ibid* 15.

- Mindful of the compliance burden imposed; and
- Enforceable.²⁵

This framework (ultimate goal, second-order goals, third-order objectives, and general regulatory principles) is useful because it clarifies the hierarchy of the objectives and principles, and in doing so clarifies their appropriate scope. The third-order objectives must be located within, and judged against, the second-order and ultimate goals of regulation. It is not enough to say that a measure improves accountability; the question is whether an accountability measure assists in promoting trust and confidence, loyalty to purposes, or effectiveness.

However, the government should recognise that there will be a diversity of opinion on the interpretation of these second-order goals, and ensure that latitude is given to organisations in interpreting and pursuing those goals. For example, the question of ‘effectiveness’ is a fraught issue because the impact of an NFP is, by definition, difficult to measure or evaluate. Regulation to improve effectiveness might usefully set minimum standards, but any further regulation must weigh in the balance the need to ensure the autonomy of NFPs, facilitate innovation and respect the diversity of opinion and missions of NFPs. In addition, the principles of regulatory design require measures where the benefit of regulation outweighs the burden.

The goals and framework set out above were discussed in the Final Report of the Scoping Study, which concluded that the “goals articulated in the consultation paper, and elaborated upon in the discussion” should guide the NFP reform process and may inform the mission statement of the NFP regulator.²⁶

IDENTIFYING REGULATORY INTERESTS

This general framework of the goals of regulation of the sector needs to be supplemented by an assessment of the interests of the State that justify regulating the sector. These interests will help define the scope of the regulator. Our research so far suggests that this issue remains under-theorised.²⁷ A starting point is provided by the Ontario Law Reform Commission, which identified four potential interests:

- The regard society has for the charitable intentions of donors: through facilitating charitable activity through appropriate legal forms, and protecting charity from vulnerability to fraud and waste;
- To ensure the legitimacy and authenticity of recipients of state-conferred privileges;
- The concern that the charitable sector will usurp the functions of the state or market, or a related fear that the sector will shelter economic activity from taxing and regulatory powers of the state. The Commission noted that this may still be a valid concern in some respects, although it needed to be questioned;

²⁵ Spindler, *Improving Not-For-Profit Law and Regulation: Options Paper*, above n 10, v, 37.

²⁶ Treasury, *Final Report: Scoping Study for a National Not-for-Profit Regulator*, above n 4, 16.

²⁷ The issue is discussed in detail in Garton, *The Regulation of Organised Civil Society*, above n 13. This is summarised in Appendix B. However, the analysis appears to us problematic in some respects.

- Delivery of government services through the third sector, entailing government responsibility for effectiveness.²⁸

Another useful way of thinking about this is to examine the public aspects of NFP activity that merit regulation. NFPs sit at the intersection of ‘public’ and ‘private’, which has often resulted in a degree of analytical confusion. They are private in that they are privately initiated, privately run and to the extent that funding is private, privately funded.

However, they impact on the public in several ways. It is important to distinguish two aspects of this impact: first, the scope of the ‘public’ involved; and second, the nature of the regulatory interest involved. It is also important to recognise the extent to which these interests are already regulated.

Beneficiaries

The most direct impact of NFPs is upon their beneficiaries and potential beneficiaries. At one end of the spectrum, these beneficiaries may be clearly identifiable and narrow in scope; at the other end of the spectrum, the class of beneficiaries may be broad and indefinite. The class of potential beneficiaries may extend generally to the entire ‘public’ in certain cases and may include future generations (for example, in the case of the preservation of the environment).

While the impact of NFPs on their beneficiaries will usually involve benefit, it may also involve the risk of harm. For example, aged housing and childcare pose obvious risks of harm to the vulnerable. The risk of harm in these cases arises out of the nature of the activity rather than the NFP nature of the organisation. NFPs in this sector should be regulated in respect of these activity-based risks along the same principles as a private sector organisation providing the same service or activity, subject to arrangements to minimise regulatory duplication.

The State clearly has a regulatory interest in ensuring that a NFP is in fact pursuing its activities (and expending its funds) for the benefit of its beneficiaries (ensuring a loyalty of purpose and a degree of effectiveness). The primary means to ensure these outcomes is likely to be through strengthening internal governance and direct accountability relationships with beneficiaries. However, these mechanisms may be less effective for a broader and less coherent or definite class of beneficiaries, or where beneficiaries are vulnerable or have little power. Such beneficiaries may need to be supported by a regulator who could be required to protect this broader public interest. For example, this may need to be supported by a ‘floor’ of minimum governance standards in legislation. This interest is already partly addressed by legal duties imposed upon directors, board members and trustees; by governance requirements in corporations and associations legislation; and by the Attorney-General’s powers in relation to charity proceedings (although the adequacy of this regime is questionable).

Donors

An organisation’s donors form a second class of the ‘public’ on whose behalf the state may seek to regulate. The degree to which the funding is ‘public’ varies. Some organisations may be substantially funded by a large number of individual donors from the public. Some organisations may draw on a diverse pool of individual, foundation or corporate donors. Other organisations are

²⁸ Ontario Law Reform Commission, *Report on the Law of Charities*, above n 20, 14-17.

funded by a more concentrated supporter base or by particular charitable public or private foundations or funds.

The strength and character of an NFP's accountability to donors will therefore vary. Member-based organisations or those with dominant funders are more likely to be held directly accountable to donors. NFPs which draw upon a large pool of small contributors are less likely to be held directly accountable, but such NFPs may be more likely to be held accountable by the media. Further, the degree to which donors will act as an effective proxy for beneficiaries will differ depending on the donor base.

A primary regulatory interest in this context is preventing donors from fraud, misappropriation of funds, and misrepresentation. Additionally, there are interests in ensuring donors' access to information and ensuring organisations use acceptable fundraising practices.²⁹ The regulatory interest is premised on ensuring respect for donors' intentions. This is presently regulated through state and territory fundraising legislation. However, while there is regulatory interest in protecting donors' intentions, it is important to recognise that some superficially attractive measures, such as fundraising ratios, are often misleading; that NFPs, like all other organisations, will incur administrative expenses; and that a balance must be struck between respecting donors' intentions and respecting the NFPs' autonomy in determining its purposes, priorities and methods in allocating money.³⁰

The taxpaying public

The broader taxpaying 'public' are affected to the extent that NFPs receive benefits conferred by the State, including government grants, tax concessions, and the privilege of limited liability. Here, the regulatory interest is in ensuring the legitimacy of the NFP and, as above, in holding the NFP to its purpose so as to facilitate the public benefit that justifies such privileges, concessions or grants. The degree of regulatory interest, however, is affected by the form of State benefit. For example, we suggest that the privilege of limited liability warrants lesser regulation than that of tax concessions (particularly that of tax deductibility for donors).

The interests of the taxpaying public in the NFP sector are already regulated in a number of different ways. Most importantly, the ATO is already responsible for ensuring that tax concessions are only granted to eligible organisations. The Australian Securities and Investments Commission (ASIC) and state consumer affairs bodies are responsible for ensuring the legitimacy of organisations for the purposes of conferring limited liability. The greatest regulatory interest comes with the purchase of services by government which also entails government responsibility for standards and effectiveness for the delivery of those services. This is currently regulated through government contracts.

It is common, however, for conditions in service contracts to extend beyond the scope of the particular services provided and affect the broader aspects of a NFP's purposes, priorities and methods, resulting in over-regulation and a loss of autonomy.

²⁹ G E Dal Pont, *Law of Charity* (LexisNexis Butterworths, 2010) [18.3].

³⁰ See generally *The Pros and Cons of Financial Efficiency Standards* (Brief, No 5, Center on Nonprofits and Philanthropy; Urban Institute Center on Philanthropy, Indiana University) <<http://nccsdataweb.urban.org/kbfiles/521/brief%205.pdf>>; *Getting What We Pay for: Low Overhead Limits Nonprofit Effectiveness* (Brief, No 3, Center on Nonprofits and Philanthropy; Urban Institute Center on Philanthropy, Indiana University) <<http://nccsdataweb.urban.org/kbfiles/311/brief%203.pdf>>.

In this respect, we welcome the Final Report's recommendation that the grant acquittal process could be improved by removing financial and governance reporting, and that consideration be given to bringing acquittals reporting into the ACNC's 'report once, use often' framework.³¹ In practice, the issue of government contracts is very significant and deserves detailed consideration. In particular, the intersections and overlaps between government regulation through service contract conditions and regulation by the national NFP regulator will need careful analysis.³²

REGULATING PARTICULAR ACTIVITIES OR SUBSECTORS

In view of the size and diversity of the NFP sector, it seems likely that different degrees or types of regulation may apply to different subsectors. The purpose, mission or sphere of activity in which the NFP is engaged (eg, education, arts, social disadvantage) greatly influences the following regulatory factors:³³

- Current regulatory frameworks and level of regulation;
- The size and significance of the sector;
- The types of activities conducted and their effect on the public;
- The nature of the 'public benefit' including the way we value the activity, how much we value it, whether the benefit is direct or tangible, and the size and nature of the class of beneficiaries;
- The internal structure of the NFP (between those inside the organisation and its stakeholders), including structures of internal accountability and sources of financing; and
- Its relationship with the government and market, including the appropriate relationship between the State and the NFP organisation; the role of the government as purchaser, competitor or dominant funder; and the role of the market as sponsor or competitor.

This suggests that a regulatory approach focusing on subsectors is likely to be most productive. One option is to confer general regulatory power over the NFP sector on an NFP regulator, and for the regulator to focus on certain subsectors either administratively or through phased commencement, after consultation with that particular subsector.

A key factor in determining the priorities of an NFP regulator is the overall regulatory framework of each subsector. For example, health and education are well-regulated subsectors. Of course, as discussed above, there will continue to be a need for regulation of particular activities, such as health and education, although efforts should be made to minimise duplication of regulatory

³¹ Treasury, *Final Report: Scoping Study for a National Not-for-Profit Regulator*, above n 4, Recs 24-25.

³² Public Interest Advocacy Centre and The Whitlam Institute Within the University of Western Sydney, *A Question of Balance: Principles, Contracts and the Government-not-for-profit Relationship* (July 2009) <http://www.whitlam.org/__data/assets/pdf_file/0020/92090/contracts_paper_final__email_version.pdf>.

³³ For a general discussion of the different characteristics of the subsectors, see Mark Lyons, *Third Sector: The Contribution of Nonprofit and Cooperative Enterprise in Australia* (Allen & Unwin, 2001).

standards. In this regard, we welcome the Final Report's recognition the need for continued activity-based regulation and the adoption of a 'report-once use-often' framework to minimise regulatory reporting.³⁴

Other factors that should be considered in determining the priorities of a regulator include: where the subsector is a significant size, where the subsector has an indirect or intangible effect on a broad class of the public, or where key stakeholders do not have effective voice in governance structures. These factors should be considered together with pragmatic factors such as the willingness and capacity of organisations to participate in early phases of regulation. These factors also suggest that the regulator need not cover the entire field, so that (for example) small unincorporated associations without government funding or significant tax concessions need not be included.

FORM OF REGULATOR

The Final Report concluded that, while a new national NFP regulator would provide the greatest benefits, this required a long process to ensure agreement and cooperation between Australian governments. In the interim, a Commonwealth-only regulator should be established as a separate statutory office within the ATO, reporting directly to Parliament through the Assistant Treasurer. This was envisaged as being "quick and cost effective" and would retain the expertise of the ATO, although the Final Report also expected it to have a "new organisational culture".³⁵

FEDERAL ISSUES

The Final Report did not, however, discuss in detail how a national regulator might operate in the Australian federation. Currently, the Australian states and territories regulate many not-for-profits and related activities such as fundraising, and some tax concessions, while the Commonwealth regulates NFP corporations and provides the most significant tax concessions.

The key advantages of a national regulator are centralisation and a 'one stop shop' agency for NFPs. There may be, however, constitutional, political and pragmatic difficulties in a comprehensive national regulator similar to the Charity Commission model used in England and New Zealand.³⁶

In Canada and the US, the federal tax authority operates as a de facto regulator. However, those examples, while instructive, are not determinative. In Canada, the regulation of charities is, by its Constitution, reserved to the provinces.³⁷ This is not the position in Australia, although there is no distinct head of legislative power that would support charitable regulation by the Commonwealth. The US context is also quite different, as it has many more States and a very large NFP sector, both of which make a national regulator practically very difficult. In any event, the US embraces quite a different regulatory philosophy.

³⁴ Treasury, *Final Report: Scoping Study for a National Not-for-Profit Regulator*, above n 4, 25-26.

³⁵ *Ibid* 67-68.

³⁶ It should, however, be noted that the Charity Commission of England and Wales is not a comprehensive national regulator as two charity regulators have been established for Scotland and Northern Ireland, which previously did not have charity regulators.

³⁷ *The Constitution Act, 1867* (Canada) s 92(7).

The Final Report does not discuss in any detail the constitutional issues involved in a national regulator. A preliminary analysis of these issues is provided here, although it should be emphasised that the constitutional implications ultimately depend upon the regulatory interests that are pursued by a new national regulator and its consequent scope.

The constitutional issues must be considered within the context of the political principles of federalism. In a federal system, there is a need to avoid uniformity for uniformity's sake. The question of 'what matters should be regulated by whom' in Australia has been the subject of recent policy discussion.³⁸

In *Common Cause: Strengthening Australia's Cooperative Federalism* (2009), Professors John Wanna, John Phillimore and Alan Fenna highlight three principles of cooperative federalism: subsidiarity, alignment of responsibilities, and cooperation. The principle of subsidiarity places emphasis on ensuring that decisions are made by the government closest to those affected (or regulated). The principle of assignment of responsibilities "holds that the presumption in favour of diversity may give way to uniformity" in three circumstances: where there are extensive policy spillovers; where the mobility of certain actors has an adverse impact on policy choices; or there are significant economies of scale. The principle of cooperation requires each government to respect each other in the federal framework and cooperate in trust and good faith.³⁹

These principles suggest the following allocation of regulatory responsibilities. First, the principle of subsidiarity suggests that the regulation of incorporated associations and unincorporated organisations should have its primary source at the sub-national level. Such organisations are likely to be of small size and local in scope and effect, and should be regulated by the closest level of government. There do not appear to be significant policy spillovers, sufficient mobility, or significant economies of scale that would justify federal regulation of these smaller organisations. Further, many incorporated associations are sporting clubs or small community associations which may not justify more than a minimal level of regulation, and which may benefit least from a national regulator.

The main driver for national regulation is the desire to reduce the regulatory complexity of multi-jurisdictional regulation. This, however, is not relevant to incorporated associations or unincorporated associations which will largely operate in one jurisdiction.

Second, many, but not all, organisations affected by multi-jurisdictional complexity will already be regulated at a federal level as a corporation. More likely, these organisations are currently subject to de facto regulation by the ATO in its work policing the boundaries of the various tax organisations. They would benefit from more coherent national regulation of NFP functions and

³⁸ See, eg, Alan Fenna, 'The Division of Powers in Australian Federalism: Subsidiarity and the Single Market' (2001) 2 *Public Policy* 175; Anne Twomey, 'Federalism and the Use of Cooperative Mechanisms to Improve Infrastructure Provision in Australia' (2007) 2 *Public Policy* 211; Cliff Walsh, 'The Costs and Benefits of Alternative Approaches to the Provision of Essential Infrastructure and the Regulation of Economic Activity in a Federal System' 2 *Public Policy* 227; Fiona Wheeler, 'Commonwealth Power over Infrastructure: Constitutional Tools for National Economic Regulation' 2 *Public Policy* 195.

³⁹ John Wanna, John Phillimore and Alan Fenna, *Common Cause: Strengthening Australia's Cooperative Federalism* (Final Report to the Council for the Australian Federation, May 2009) <<http://www.caf.gov.au/documents/FP3%20-%20final.pdf>>, Chapter 2.

goals, as well as from support and assistance in education and improvement. For these organisations, the most compelling justification for federal regulation is the need to ensure the legitimacy of federal tax concessions and to hold the organisation to its purpose. Another, possibly less compelling, rationale for national regulation may be that of economies of scale and improved efficiency from a centralised regime.

Focusing on ensuring the legitimacy of taxation benefits and regulating corporations fits well with the constitutional division of powers. The Commonwealth could safely rely upon the taxation power (s 51(ii) of the *Constitution*) and the corporations power (s 51(xx)) together with the existing referral of power by the States and Territories in respect of corporations law (s 51(xxxvii)).

The taxation power under s 51(ii) has been broadly interpreted by the High Court and would enable a broad scope of regulation of tax-exempt entities. For example, in *Fairfax v Federal Commissioner of Taxation* (1965) 114 CLR 1, the legislation was framed so as to remove a tax exemption for superannuation funds where there was insufficient investment in Commonwealth investments. The primary legislative purpose was clearly to encourage greater investment in Commonwealth securities, which was outside Commonwealth legislative power. Nevertheless, the High Court held that the enactment did “not prescribe or forbid conduct” and in both substance and form the legislation imposed an obligation to pay income tax, so that the legislation was squarely a law ‘with respect to taxation’ and within Commonwealth power.⁴⁰ A legislative scheme that requires fulfilment of regulatory obligations as a condition of access to federal tax exemptions would also appear to fall within the taxation power.

The Commonwealth corporations power under s 51(xx) relates only to foreign, trading and financial corporations (‘constitutional corporations’). This power has been expansively interpreted recently in the *WorkChoices* case, which clearly held that any activities of a constitutional corporation could be regulated using that power.⁴¹ In the present case, the greater restriction is the degree to which NFPs could be characterised as ‘trading corporations’. The High Court has interpreted this term liberally so that the current test is whether trade constitutes a sufficiently significant part of the activities of the organisation, notwithstanding governmental or NFP characteristics.⁴² This would likely capture at least some of the larger NFPs. However, the validity of this test has been questioned more recently by the High Court in the *WorkChoices* case.⁴³

Any gaps in the corporations power are likely to be covered by the referral of powers by States in relation to the *Corporations Act 2001* (Cth). The referrals conferred jurisdiction for the enactment of that legislation and also in relation to the “matters of the formation of corporations, corporate regulation and the regulation of financial products and services” in the form of express amendments to the corporations legislation.⁴⁴ To the extent that the regulatory scheme will involve corporate governance issues (namely corporate regulation), this could be achieved by amendment of the *Corporations Act*, relying upon the referral of powers to fill in any gaps in Commonwealth power. This design would effectively capture the organisations that are of

⁴⁰ *Fairfax v Federal Commissioner of Taxation* (1965) 114 CLR 1, 13.

⁴¹ *New South Wales v Commonwealth* (2006) 81 ALJR 34.

⁴² *Commonwealth v Tasmania* (1983) 158 CLR 1.

⁴³ *New South Wales v Commonwealth* (2006) 229 CLR 1, 75, 117, 373.

⁴⁴ *Corporations (Commonwealth Powers) Act 2001* (NSW) s 4.

greatest regulatory interest, namely existing federal corporations and those accessing federal tax concessions.

As the Final Report accepted, there will be significant benefit in a national regulator even if it operated only within the Commonwealth jurisdiction. It will significantly improve the regulation of those organisations of greatest regulatory interest. It also has potential to act as an influence upon state taxation authorities and on general regulatory standards, as well as a hub for connecting government agencies and for driving harmonisation.

If further regulatory powers are desired, this could be achieved at least in part by conferral by States of residual regulatory powers upon a national regulator. In *R v Duncan; Ex parte Australian Iron & Steel Pty Ltd* (1983) 158 CLR 535, the High Court sanctioned the joint establishment of a regulatory body in the context of the coal industry. While subsequent decisions have reduced the scope of such cooperative mechanisms, these decisions would largely affect the oversight and enforcement powers conferred upon Commonwealth officials in a cooperative regulatory scheme.⁴⁵ One approach to avoid this deficiency could be to implement instead a collaborative mechanism where the national regulator would have power to share information and refer matters to be investigated by State authorities. Such a collaborative approach could build on the incentive of Commonwealth grants under s 96 of the Constitution conditioned upon agreement to establish such a regulator. Another practical factor in favour of such an arrangement is the recent introduction of the Australian Consumer Law.⁴⁶ This has reduced the scope of activity of State and Territory fair trading authorities which traditionally regulate incorporated associations.

Extending the scope of the regulator could be further achieved by cooperative mechanisms, rather than centralisation. For example, harmonisation of reporting obligations for NFPs could be achieved through the Council of Australian Governments' work on reducing the regulatory burden on NFPs, and could result in (for example) substantially similar obligations for incorporated associations across jurisdictions through model or mirror legislation.⁴⁷ The two largest states, NSW and Victoria, have recently completed major amendments to their associations legislation,⁴⁸ so could provide significant leadership in this respect.

Other aspects of multi-jurisdictional complexity have been or are in the process of being addressed, such as harmonisation of cooperatives legislation, implementation of the Standard Chart of Accounts,⁴⁹ standardisation of government contracts, and harmonisation of fundraising legislation.

⁴⁵ *Re Wakim* (1999) 198 CLR 511; *R v Hughes* (2000) 202 CLR 535.

⁴⁶ *Competition and Consumer Act 2010* (Cth) Sch 2. This commenced on 2 January 2011, replacing the previous *Trade Practices Act 1974* (Cth).

⁴⁷ See especially Twomey, 'Federalism and the Use of Cooperative Mechanisms to Improve Infrastructure Provision in Australia' above n 38; Wanna, Phillimore, and Fenna, *Common Cause: Strengthening Australia's Cooperative Federalism*, above n 39, Ch 3. These discuss the advantages and disadvantages of other co-operative mechanisms.

⁴⁸ *Associations Incorporation Amendment Act 2010* (Vic); *Associations Incorporation Act 2009* (NSW).

⁴⁹ The Final Report concludes that the NFP regulator should take responsibility for the Standard Chart of Accounts: Treasury, *Final Report: Scoping Study for a National Not-for-Profit Regulator*, above n 4, 50-51.

This philosophical approach broadly accords with the only (dated) analysis we have so far located on the constitutional question in relation to NFPs, namely that of Cullen.⁵⁰ His analysis is summarised in detail in the Appendix. Briefly put, however, Cullen's view is that a patchwork of Commonwealth powers could justify Commonwealth regulation, but that this would violate (at least) the spirit of the federal compact and negotiation and intergovernmental agreement would be a preferable approach.

RELATIONSHIP WITH EXISTING REGULATORY BODIES

As noted above, the Final Report concludes that an interim Commonwealth regulator should be established as a separate statutory office of the ATO, pending the establishment of a single national NFP regulator. We welcome the government's decision to establish eventually an independent national regulator.

However, the establishment of an interim regulator within the ATO poses significant risks. In our view, the ultimate regulatory goal of facilitating the public benefit delivered by the NFP sector (discussed above) does not fit comfortably within the focus and mandate of the ATO. The ATO's primary goal should be to protect the revenue, which puts it in a position of conflict.

This criticism also applies to the other main regulator, ASIC, in spite of the suggested institutional benefits identified by the Productivity Commission.⁵¹ ASIC's predominant focus has been on for-profit and market-oriented behaviour, and Woodward and Marshall's study confirmed that NFPs felt ASIC was inaccessible and focused on for-profit behaviour.⁵²

A very large part of a regulator's success depends upon its relationship with the sector it regulates. The confidence of the sector may well be undermined by the location of the regulator within the ATO, even if it is a temporary measure. There would also doubtless be concern that, if there is not the will now to establish an independent regulator, there will be even less political will once the impetus for reform has vanished.

We welcome, however, the Final Report's concern that the interim regulator should be independent and reflect a "new organisational culture".⁵³ In this regard, the Final Report recommends the regulator should be a separate statutory office which will report directly to Parliament through the Assistant Treasurer. Further, an advisory board is suggested as a way of "help[ing to] ensure independence and an organisational focus on the NFP sector".⁵⁴

A related issue arises as to the relationship between the new regulator and other existing regulators, for example the Office of the Registrar of Indigenous Corporations (ORIC) and the

⁵⁰ Richard Cullen, 'The Australian Constitution and the Regulation of Charitable and Philanthropic Institutions' in Richard Krever and Gretchen Kewley (eds), *Charities and Philanthropic Institutions: Reforming the Tax Subsidy and Regulatory Regimes* (Comparative Public Policy Research Unit, Monash University, 1991) 117.

⁵¹ Productivity Commission, *Contribution of the Not-for-Profit Sector*, above n 8, 148-150.

⁵² Sue Woodward and Shelley Marshall, *A Better Framework: Reforming Not-for-profit Regulation* (Final Research Report, Centre for Corporate Law & Securities Regulation, University of Melbourne, 2004) <<http://cclsr.law.unimelb.edu.au/go/centre-activities/research/reforming-not-for-profit-regulation-project/index.cfm>>, 3.

⁵³ Treasury, *Final Report: Scoping Study for a National Not-for-Profit Regulator*, above n 4, 67.

⁵⁴ *Ibid* 67.

proposed housing regulator. Clearly, it is important not to lose the existing specialist experience, community engagement and expertise in existing regulatory agencies such as ORIC.⁵⁵ A key factor will be the attitude of the Native Title Representative Bodies and other organisations already regulated by ORIC to any proposed transfer. A more attractive option would be for liaison between ORIC and the NFP regulator and an exemption for bodies regulated by ORIC in the establishment phase of a new regulator, with the relationship to be reviewed in the future as necessary.

In respect of this issue, the Final Report observed:

The regulation of Indigenous corporations by ORIC could also be moved to the national NFP regulator, however specific complexities in relation to ORIC may mean that further discussion and further review may be necessary to determine the best way to incorporate these entities without losing the benefits of the specialist skills and expertise in this area, and the relationships developed with the Indigenous community. Moving ORIC into the regulator may also have significant advantages, such as the ability to extend the experience in relation to ORIC to all Indigenous NFPs (including those not currently regulated by ORIC) and allow all NFPs to be regulated in a similar manner.⁵⁶

We welcome this recognition of the specialist skills and expertise of ORIC and the importance of its relationships with the Indigenous community, and the suggestion that the complexities of any such transfer need to be investigated further.

In relation to the proposed housing regulator, similar issues arise. There is room for both a NFP regulator focused on governance and purpose, and an activity-specific regulator in this vital sector, as is the case for education, health and care facilities, provided duplication is minimised through 'one-stop-shop' collaborative working arrangements. An alternative approach could be to exempt housing NFPs from the scope of the NFP regulator, at least in the early stages of establishing the specific housing regulator. The Final Report similarly envisages that the NFP regulator could be responsible for governance issues, with complementary activity-based regulation and arrangements to minimise duplication.⁵⁷

LEGAL FORMS

NFP organisations take several different legal forms: predominantly incorporated associations (regulated by states and territories), companies, usually limited by guarantee (regulated federally), statutory form (subject to their own Act of Parliament), cooperatives (regulated by cooperatives legislation), Indigenous corporations (regulated by the Office of the Registrar of Indigenous Corporations), and unincorporated associations.⁵⁸ Reports have frequently noted the

⁵⁵ Agreements Treaties and Negotiated Settlements Project, *Submission to the Treasury, Scoping Study for a National Not-For-Profit Regulator Consultation Paper* (Submission, 25 February 2011) <http://www.atns.net.au/objects/YFJULNFSHGS/ATNS%20Submission%20to%20National%20NFP%20Regulator%20Scoping%20Study%20_final_.pdf>.

⁵⁶ Treasury, *Final Report: Scoping Study for a National Not-for-Profit Regulator*, above n 4, 25.

⁵⁷ Ibid 25.

⁵⁸ The State Services Authority reported in 2007 that Victoria had 33,478 incorporated associations, 1,645 companies, 748 co-operatives, 64 Aboriginal corporations, and 20 regulated by their own Act of Parliament: State Services Authority (Vic), *Review of Not-for-Profit Regulation: Final Report*, above n 10, xii..

concern that this variety of legal forms leads to fragmentation, inconsistency complexity, and expense.⁵⁹

Proposals have been made in the past to develop a specialist legal form for NFPs that address their specific concerns. This was recommended by the Senate inquiry into the disclosure regimes for NFPs in 2008 and the Industry Commission in 1995,⁶⁰ but was rejected by the Productivity Commission in 2010.⁶¹ Although legislation establishing such a form (known as the Charitable Incorporated Organisation or CIO) has been passed in the UK, the development of the form has taken longer, with the Charity Commission of England and Wales only recently publishing model constitutions for CIOs.⁶² Woodward and Marshall suggest that the UK reforms are worth considering at a later stage following the development of a national regulatory framework.⁶³

While the Project has yet to explore this issue in detail, we suggest that the different legal forms do sometimes reflect important philosophical differences that may warrant different treatment. For example, the focus of cooperatives is mutual benefit, which involves less compelling 'public' interests, and Indigenous corporations have been established to reflect particular concerns specific to Indigenous development. To some extent, as well, the choice of incorporated association or corporation partly reflects variables such as size, activity and jurisdiction as well as the level of regulatory burden.

The two major advantages of a single legal entity form could be more consistent and appropriate reporting obligations and governance requirements, and accountability, through this single legal form, to a single regulator. It is suggested that neither of these advantages is necessarily dependent upon mandating a single specialist legal form. Further, transition costs in moving to a single entity form would be very significant and such a transition is likely to raise difficult issues and costs.

In relation to the first goal, another route would be to compare the obligations and requirements across legal forms, and identify 'core' or 'minimum' obligations that could provide a general framework for tiered reporting. Ensuring broad consistency in the types of regulatory requirements across legal forms, while respecting their different philosophies, may be a more appropriate and feasible strategy.

The second goal of a single national regulator could be achieved through use of the national regulator as the primary agency, which operates through collaborative arrangements and information sharing with other regulators. As discussed earlier, however, a philosophical issue

⁵⁹ See, eg, Spindler, *Improving Not-For-Profit Law and Regulation: Options Paper*, above n 10, 16-17; Productivity Commission, *Contribution of the Not-for-Profit Sector*, above n 8, 124-125.

⁶⁰ Industry Commission, *Charitable Organisations in Australia*, above n 5, Rec 27; Senate Economics Committee, *Inquiry into the Disclosure Regimes for Charities and Not-for-profit Organisations* (2008) <http://www.aph.gov.au/Senate/committee/economics_ctte/charities_08/index.htm>, Rec 7.

⁶¹ Productivity Commission, *Contribution of the Not-for-Profit Sector*, above n 8, 120-126.

⁶² The Charity Commission for England and Wales, *Constitution of a Charitable Incorporated Organisation with Voting Members Other Than Its Charity Trustees* (2011) <http://www.charitycommission.gov.uk/Library/start/assoc_model_cio.pdf>.

⁶³ Woodward and Marshall, *Reforming Not-for-profit Regulation Project*, above n 52, 74.

arises as to whether it is appropriate or desirable for a national regulator to regulate state or territory-based incorporated associations.

A more flexible option is, as set out in this Working Paper, to identify which regulatory interests justify regulation by a national regulator. If, for example, the provision of government grants was one of these, it could be a condition of receiving a grant that the organisation is regulated by the national regulator, or that it meets equivalent standards of disclosure and governance as under the national regime. Similarly, access to particular tax benefits may include similar conditions. This approach would be more flexible, allows organisations choice, limits the burden on the new regulator, avoids major legislative and transition costs, and also more precisely aligns with regulatory goals.

The Final Report suggests instead that a single legal form for NFPs could be achieved through reform of the legal form of company limited by guarantee. It observed that it was “unclear why more NFPs have not chosen this legal structure, particularly given the recent changes to the requirements of this entity type”, and recommended that this structure be reviewed to determine its appropriateness for NFPs.⁶⁴

The advantages and disadvantages of the company limited by guarantee form, as opposed to the (Victorian) incorporated associations form, is helpfully detailed in a factsheet produced by PilchConnect.⁶⁵ The disadvantages of a company limited by guarantee form include:

- The complexity of the Commonwealth regime with a resulting compliance burden and a requirement for suitable expertise;
- The potentially higher costs (depending in part on audit requirements, and also on enforcement and waiver of penalties for late reporting);
- The potentially more onerous duties of directors under the *Corporations Act* (although, as is noted, the common law duties are probably the same);
- The requirement for publicly registering details (although this would likely no longer be an advantage if an NFP regulator requires similar details); and
- Difficulty of amalgamating NFPs.

Further, there are legal and administrative complexities in migrating from one structure to another, including requiring the consent of each member. These are issues that require consideration in any review of the legal form of company limited by guarantee.

FUNCTIONS OF A REGULATOR

The primary function of a regulator is to regulate the governance of NFPs, including as key aspects issues such as reporting obligations and disclosure of information. The issue of fundraising is also separately considered. Finally, a regulator must also enforce the regulatory

⁶⁴ Treasury, *Final Report: Scoping Study for a National Not-for-Profit Regulator*, above n 4, 25.

⁶⁵ PilchConnect, *Fact Sheet: Incorporated Association or a Company Limited by Guarantee?* (2009) <[http://www.pilch.org.au/Assets/Files/IAorCLG290910\(2\).pdf](http://www.pilch.org.au/Assets/Files/IAorCLG290910(2).pdf)>.

regime (including encouraging compliance through education as well as through oversight powers).

GOVERNANCE

The principal purpose of a NFP regulator is to increase accountability and transparency in governance arrangements. This is partly achieved through requiring reports on particular matters and requiring public disclosure of particular information (as discussed separately below). Another core aspect is to regulate the internal governance arrangements of NFPs. Corporations legislation (and incorporated associations legislation) currently prescribe minimum aspects of governance, such as the required officers of the organisation and directors' duties.

In this respect, the Consultation Paper initially proposed some 'core rules' and a regulatory framework relating to the internal governance of NFPs, including decision making and accountability frameworks. It did not make clear, however, whether the intention was to embed these rules and framework in the form of legislation. Nor did it clarify whether the intention was merely to replicate obligations that already exist in current legislation or to adapt or modify those duties in some way.

Several concerns arise from the Consultation Paper's proposal for a regulatory framework. First, such a framework would need to cater for the diversity of the sector. Second, if too detailed, a regulatory, decision-making or accountability framework risks reducing the autonomy of charities to an unnecessary extent. ACEVO's position is that that "charities are best placed to determine institutional detail as long as their reasons are public and they can be challenged".⁶⁶ We suggest it is important that significant latitude be given to charities to pursue their own aims provided they are for the public benefit.

A regulatory framework that is too rigid or detailed runs the risk of hampering innovation and experiments in NFP governance. There is a flourishing literature, especially in the US, on issues of governance and financial management, and the adoption of model frameworks may stifle healthy discussion within the sector itself about its practices.

A NFP regulator has many tools at its disposal to support NFPs in establishing better, and appropriate, governance for their own purposes. For example, guidance or a principle-based code or charter for NFPs defining their obligations in respect of various stakeholders could be useful.⁶⁷ There is merit in the preparation of 'model rules', which can be adopted as a whole or modified by an organisation, which requires the organisation to think about its governance processes. For example, the *Associations Incorporations Act 1981* (Vic), as amended, provides for model rules and requires either adoption of them or adoption of a governing document covering specified matters.⁶⁸

⁶⁶ Association of Chief Executives of Voluntary Organisations (ACEVO), *Public Impact Centred Regulation*, above n 16, 14.

⁶⁷ See, eg, the code developed by the Panel on Accountability and Governance in the Voluntary Sector, *Broadbent Report*, above n 15, 24.

⁶⁸ *Associations Incorporation Act 1981* (Vic) ss 4-6, 54.

We therefore welcome the Final Report's finding that a "principles-based approach", rather than an overly prescriptive approach, should be adopted by the regulator.⁶⁹ This approach should also "take into account the size of the organisation, the risks it presents by virtue of its activities and turnover as well as the level of government support an organisation receives", as well as "consider the existing frameworks applied by ASIC and the ATO and the rules governing trusts".⁷⁰

REPORTING

Another major function of a regulator would be to streamline reporting obligations for NFPs. As noted above, the Final Report has endorsed the use of a 'report-once, use-often' model. Such a model would use the primary report to the national regulator as the basis of reporting obligations to other regulatory bodies. The information in this report could then be used to fulfil other reporting obligations, although of course additional requirements may need to be imposed to reflect the interests of those other bodies.

Such a model is clearly welcome. There are obvious benefits in terms of reducing administrative burdens for organisations, as well as ensuring comparability and consistency of information across agencies. The burden imposed by regulatory duplication is one of the most consistent themes of past inquiries into the sector. The implementation of the Standard Chart of Accounts by the NFP regulator is a welcome development which will assist this process.

There are valuable lessons to be learned from the United Kingdom's recent and continuing reform of this process. The United Kingdom has recently released a report on cutting red tape for NFPs.⁷¹ The UK Government has also previously considered these matters.⁷² The United Kingdom, for example, set up an online system for the charitable sector to identify regulatory overlaps for simplification.⁷³ The ACEVO report (2010) proposed that the principal regulator and the sector can identify overlaps together and also suggested the possibility of a 'super-complainant' approach which gave priority to complaints by certain bodies such as national umbrella bodies.⁷⁴ There has also been discussion in the United Kingdom about the form of reporting by the sector.⁷⁵

⁶⁹ Treasury, *Final Report: Scoping Study for a National Not-for-Profit Regulator*, above n 4, 60.

⁷⁰ Ibid 60.

⁷¹ Lord Hodgson, *Unshackling Good Neighbours* (Task force established to consider how to cut red tape for small charities, voluntary organisations and social enterprises, 2011) <<http://www.cabinetoffice.gov.uk/sites/default/files/resources/unshackling-good-neighbours.pdf>>.

⁷² See, eg, Better Regulation Task Force (UK), *Better Regulation for Civil Society: Making Life Easier for Those Who Help Others*, above n 16.

⁷³ Ibid 9.

⁷⁴ Association of Chief Executives of Voluntary Organisations (ACEVO), *Public Impact Centred Regulation*, above n 16, 28-29.

⁷⁵ See, eg, Ibid 40.

REGISTRATION AND INFORMATION PORTAL

An important aspect of improving the accountability of NFPs is to require registration and public disclosure of key information. These functions were fully endorsed by the Final Report and received significant support across the sector.⁷⁶

The maintenance of a public register of NFPs is indeed one of the most important functions of the national regulator. This promotes all of the 'second-order' regulatory objectives, namely promotion of public confidence and trust, ensuring loyalty to the 'mission' of the organisation, improving the effectiveness of the organisation and educating the public about the NFP sector. The maintenance of such a register will also foster sector development by improving the collection of information and statistics etc about the sector, which will inform policy developments and improve networks within the sector.

Ideally, this should build upon existing online databases of NFP organisations, such as *The Australian Directory of Not for Profit Organisations*⁷⁷ and *The Guide to Australia's Not-for-Profit Organisations*.⁷⁸ We note that a portal is not necessarily linked to a national regulator, as the Charities Directorate in Canada,⁷⁹ and the Internal Revenue Service in the US also operate online databases,⁸⁰ but these are clearly less detailed than the equivalent portals in the United Kingdom or New Zealand.

The Register on the Charity Commission for England and Wales website is an excellent model for such a portal. It provides clear and accessible information on:

- Activities;
- Sphere of operation;
- Income and expenditure;
- Financial history;
- Contact details and trustees;
- Governing documents; and
- Annual reports, trustees' reports, and summary information returns.

⁷⁶ Treasury, *Final Report: Scoping Study for a National Not-for-Profit Regulator*, above n 4, 29-30, 55-56.

⁷⁷ Pro Bono Australia, *Guide to Giving: The Australian Directory of Not for Profit Organisations* <<http://www.probonoaustralia.com.au/directory>>.

⁷⁸ Pathways Australia, *Guide to Australia's Not-For-Profit Organisations* <http://www.pathwaysaustralia.com.au/Guide_About.asp>.

⁷⁹ Canada Revenue Agency, Government of Canada, *Charities Listings* (15 September 2010) <<http://www.cra-arc.gc.ca/chrts-gvng/lstngs/menu-eng.html>>.

⁸⁰ Internal Revenue Service, *Search for Charities* <<http://www.irs.gov/charities/article/0,,id=96136,00.html>>.

Similar information is provided in the New Zealand portal.⁸¹ In this respect, we welcome the Final Report's conclusion that the information portal should be based on overseas models, including the New Zealand and English models.⁸²

We note, however, that there may be a need to keep some information private, such as where the information may prejudice the organisations' competitiveness in tenders in cases where private sector organisations would not be required to disclose similar information.⁸³ The Regulator could prepare and issue guidelines on such issues in consultation with the sector.

FUNDRAISING

State and territory fundraising legislation is currently being harmonised through the Council of Australian Governments. This project is welcome because of the complexity of the present legislative framework.

However, it seems premature to consider the role of the regulator in relation to fundraising. Some state fundraising legislation, for example, is not restricted to NFP collections, and if the harmonisation proceeds in this manner it may be difficult to justify regulating fundraising of NFPs separately from for-profit fundraising. A decision in this respect also depends upon matters such as the capacity and expertise of the current state offices in relation to fundraising, the number of national fundraisers, the regulatory burden on organisations even with harmonised legislation, the desire of the states to save resources, and the model of the regulator in respect of its constitutional powers.

For these reasons, we welcome the recommendation in the Final Report that there should be coordination between the Ministerial Council for Consumer Affairs conducting the harmonisation project and any national NFP regulator, and that both projects need to be considered in conjunction with each other. Clearly, both projects will affect each other and should be considered together as they progress.⁸⁴

EDUCATIONAL AND COMPLIANCE INITIATIVES

As stated above, the ultimate goal of regulation is to facilitate the NFP sector in achieving public benefit. Educational and compliance initiatives clearly promote that goal. Such initiatives are now a commonplace part of the regulatory toolkit, and should form a core part of the NFP regulator's functions.

Such a function is undertaken by overseas NFP regulators. The Charity Commission of England and Wales and the Charities Commission of New Zealand both publish a significant range of practical guidance and educational materials on their respective websites. The Charities Directorate section of the Canada Revenue Agency also conducts a range of innovative compliance initiatives. In 2009-2010, for example, it conducted 102 information sessions across

⁸¹ *Charities Commission (New Zealand)* <<http://www.charities.govt.nz/>>.

⁸² Treasury, *Final Report: Scoping Study for a National Not-for-Profit Regulator*, above n 4, 55.

⁸³ Panel on Accountability and Governance in the Voluntary Sector, *Broadbent Report*, above n 15, 32.

⁸⁴ Treasury, *Final Report: Scoping Study for a National Not-for-Profit Regulator*, above n 4, 44.

Canada, produced 21 webinars and a videocast series, and funded a range of NFPs to deliver educational and compliance resources to the sector.⁸⁵

The Final Report endorses a similar role for the new NFP regulator. It recommends that the regulator should issue guidance materials similar to those provided by overseas regulators, and referral services for organisations requiring external advice.⁸⁶

Importantly, the Final Report also recognises the need for these educational activities to complement existing resources and activities.⁸⁷ A range of organisations in Australia already provide educational and sector development activities, such as PilchConnect, Philanthropy Australia, the Associations Forum and the Australian Institute of Community Practice and Governance. The recently established Office for the Community Sector in Victoria also provides a welcome focus on education and sector development. The continued professionalisation of the NFP sector and the growth of the sector point to a growing demand for such activities. This is confirmed by Woodward and Marshall's 2004 survey (summarised in Appendix B) which showed significant support for advice and training as functions of a potential regulator.

As noted above, there is a debate about the extent of the educational activities a regulator should be engaged in.⁸⁸ For example, the Productivity Commission has suggested that the regulator should not have a role in "sector development", but should rather focus on compliance with legal requirements.⁸⁹ Ultimately, however, if the regulatory goal is to facilitate the sector, there is no bright line between the two types of activities. The Final Report, however, appeared to strike the appropriate balance when it stated that "the regulator should not provide advice or educative support that would compromise its regulatory role".⁹⁰

OVERSIGHT POWERS

An effective regulator requires sufficient supervisory and enforcement powers. The Charity Commission of England and Wales has an extensive suite of supervisory powers, including powers to: institute inquiries; suspend or remove trustees; give directions in relation to charity property; give advice and guidance; make schemes; and participate in charity proceedings. The NFP regulator should be conferred with similar powers, provided these are exercised in a proportional manner. In particular, coercive powers enabling withdrawal of registration as an NFP, leading to a loss of tax-exempt status or other privileges, are required but should be exercised with caution and in defined circumstances (set out in law or binding regulations).

We therefore welcome the Final Report's recommendations that a regulator should be given the following powers:

- Asset protection;

⁸⁵ Charities Directorate, 'Facts and Figures on the Work of the Charities Directorate in 2009-2010'4 , *Charities Connection*, 2010 <<http://www.cra-arc.gc.ca/chrts-gvng/chrts/cmmnctn/nwslttrs/cnnctn/cnnctn04-eng.html>>.

⁸⁶ Treasury, *Final Report: Scoping Study for a National Not-for-Profit Regulator*, above n 4, 39.

⁸⁷ *Ibid* 39.

⁸⁸ See, eg, Garton, *The Regulation of Organised Civil Society*, above n 13, 219.

⁸⁹ Productivity Commission, *Contribution of the Not-for-Profit Sector*, above n 8, [116]-[117].

⁹⁰ Treasury, *Final Report: Scoping Study for a National Not-for-Profit Regulator*, above n 4, 39.

- Suspension and/or replacement powers;
- Deregistration of NFPs;
- Enforcement of governance rules;
- Investigations;
- Dispute resolution processes; and
- Enforcement powers including information gathering powers, supervisory powers and penalties.⁹¹

In particular, we welcome its reference to the power to implement *proportional* compliance activities (emphasis added).⁹² We also welcome the recommendation in the Final Report that similar review and appeal procedures, including review by the Administrative Appeals Tribunal and appeal to the federal courts, should apply to these powers.⁹³

Finally, however, we observe that the key issue of enforcement is likely to be that of resourcing rather than the availability of statutory powers. This was the case with the UK Charity Commission for much of its history.

FUNDING

Finally, an important practical issue is whether, and to what extent, NFP entities should contribute to the cost of the regulator. While budgetary realities may require a level of contribution from the sector, it is important to recognise the significance of the NFP's sector to Australian social and economic life. In the end, the costs borne by the sector are in the end borne by the community, and the level of contribution required should reflect this fact. It is also crucial to recognise that NFPs are highly sensitive to financial burdens, and a minimal contribution would facilitate the success of the regulator. Lower costs for smaller NFP entities, perhaps tied to differential reporting obligations, are clearly desirable.

It is, however, premature to assess an appropriate level of contribution given the many variables in play: the scope of the regulator, the types of entities regulated, its powers or functions, its location, and of course the availability of public funding.

The Final Report canvasses both a fully funded and a model of co-contribution by the sector, but does not recommend either. Instead, it recommends that the government should consider the co-contribution model and the possibility of replacing existing fees. We welcome, however, its recommendation that if co-contribution is adopted, such an approach should be tiered to reflect the resourcing constraints of smaller NFP entities.⁹⁴

⁹¹ Ibid 61.

⁹² Ibid 61.

⁹³ Ibid 29.

⁹⁴ Ibid 72.

CONCLUSION

This Working Paper addresses the broader principles and issues that arise concerning the establishment of a NFP regulator. The Not-for-Profit Project will continue work on this aspect as work on this important reform progresses. While there are many philosophical and design issues to be considered in the establishment of the regulator, there is no doubt that the establishment of such a regulator is a welcome and overdue reform for this vital sector of our economy and society.

Please contact for further information the project investigators of the Not-for-Profit Project:

Associate Professor Ann O'Connell

+61 3 8344 6202 | a.o'connell@unimelb.edu.au

Ann is Co-Director of Taxation Studies and teaches taxation and securities regulation at the Law School. She is also Special Counsel at Allens, Arthur Robinson and is a member of the Advisory Panel to the Board of Taxation.

Associate Professor Miranda Stewart

+61 3 8344 6544 | m.stewart@unimelb.edu.au

Miranda is Co-Director of Taxation Studies and teaches tax law and policy at the Law School. She is an International Fellow of the Centre of Business Taxation at Oxford University and is on the Tax Committee of the Law Council of Australia. She has previously worked at New York University School of Law, US and as a solicitor and in the Australian Taxation Office.

Associate Professor Matthew Harding

+61 3 8344 1080 | m.harding@unimelb.edu.au

Matthew is an Associate Professor at the University of Melbourne. His published work deals with issues in moral philosophy, fiduciary law, equitable property, land title registration, and the law of charity. Matthew has also worked as a solicitor for Arthur Robinson & Hedderwicks (now Allens, Arthur Robinson).

Dr Joyce Chia

+61 3 9035 4418 | j.chia@unimelb.edu.au

Joyce is the Research Fellow on the Not-for-Profit Project. She has worked at the Australian Law Reform Commission, the Federal Court of Australia, and the Victorian Court of Appeal.

More information on the project can be found on the website of the [Melbourne Law School Tax Group Not-for-Profit Project](#).

APPENDIX—RELEVANT WORK ON REGULATION AND NFPs

This summarises major work done on regulation in the NFP sector which has been consulted by the Project. It does not claim to be comprehensive. The resources are listed in reverse chronological order.

ACEVO, PUBLIC IMPACT CENTRED REGULATION FOR CHARITIES (2010)

A high level taskforce for ACEVO (the professional body for third sector executives in the UK) released a report in 2010 on better regulation of the NFP sector.⁹⁵ It proposes three ‘headline agendas’: the enterprise agenda (designed to increase the effectiveness of enterprise activity), the professionalisation agenda (designed to rebalance regulation towards a more co-regulatory approach); and the impact, transparency and accountability agenda (designed to reduce the need for top down regulation).

Regulatory Principles

The report agrees with the general principles of non-duplication of regulation, and a risk-assessment based approach focused on outcomes. It believes an “increasingly professional, transparent and enterprising sector requires less top down regulation”, and notes that any unnecessary diversion of cost or time takes away from public benefit outcomes.⁹⁶

It emphasises three further general principles. First, regulation should be “designed to maximise the public benefit of organisations within this sector” and that organisations should take responsibility for reasoned public disclosure as part of overall public benefit mission reporting.⁹⁷ Second, charities are best placed to determine institutional detail as long as their reasons are public and they can be challenged.⁹⁸ Third, the regulatory culture needs to be changed away from a “law-and-compliance culture resulting in risk aversion” to a more strategic approach.⁹⁹

In relation to the enterprise agenda, the report recommends that regulatory intervention should be warranted only if there is reasonable expectation that harm will otherwise be done to the public benefit mission and core values of the sector. This would enable organisations to decide how to pursue its public benefit and whether to undertake trading activities in pursuit of its core mission.¹⁰⁰ Specifically, it recommended more encouraging guidance by the Charity Commission on financing,¹⁰¹ and encouragement of trading activities.¹⁰²

In respect of the professionalization agenda, the report argued the regulator should “see leading and shaping the sector’s public impact culture as a cost efficient source of high impact regulation”. It suggested the possibility of the principal regulator and the sector identifying commonly required information to reduce duplication in reporting. It also proposed a ‘super-

⁹⁵ Association of Chief Executives of Voluntary Organisations (ACEVO), *Public Impact Centred Regulation*, above n 16.

⁹⁶ Ibid 14.

⁹⁷ Ibid 14.

⁹⁸ Ibid 14.

⁹⁹ Ibid 15.

¹⁰⁰ Ibid 18.

¹⁰¹ Ibid 19-26.

¹⁰² Ibid 26-28.

complainant' approach where complaints by certain bodies on regulatory overlap, such as national umbrella bodies, could be prioritised and fast-tracked through a resolution process.¹⁰³

The report suggested ways in which the sector could be effectively co-regulated, such as a sector-based board to peer review civil society organisations; a more formal training or development programme; or professional standards; and in particular suggested peer review of impact reporting.¹⁰⁴

The report also recommended re-thinking the recent introduction of a 'management test', requiring managers to be 'fit and proper persons'. It suggested the new definition provided an unwelcome degree of uncertainty and imposed a new bureaucratic burden.¹⁰⁵

In relation to the 'impact, transparency and accountability agenda', the report recommended radically reformatted, streamlining and making more transparent the publication and regulatory filing of sector information. It believed disclosure was the most effective form of regulation, and the most relevant information was based on their public benefit impact and how they achieve it.¹⁰⁶

JONATHON GARTON, *THE REGULATION OF ORGANISED CIVIL SOCIETY* (2009)

This is an academic book adapted from a PhD thesis which aims to answer two questions: first, in what circumstances, and for what reasons, is it appropriate for the state to regulate the activities of organised civil society in a sector-specific way? Secondly, when it is appropriate to regulate, do the peculiar characteristics of these activities make one type of regulation more appropriate than another?¹⁰⁷

Purposes of Regulation

Garton ultimately concludes that regulation can be justified by reference to (a) the need to prevent anti-competitive practices; (b) externalities resulting from unfettered political campaigning; (c) the need to ensure accountability; (d) the need to co-ordinate the sector; (e) the need to respond to philanthropic failures; and (f) the need to prevent erosion of key CSO structural characteristics.¹⁰⁸

Garton comes to this conclusion by reviewing both traditional microeconomic theories of regulation and social theories of regulation and examining their applicability to the NFP sector. The microeconomic theories justify regulation where a market is not perfectly competitive for the following reasons:

Monopoly or cartel power of one firm;

Excessively competitive practices threaten to undermine market;

Product is a public good;

¹⁰³ Ibid 28-29.

¹⁰⁴ Ibid 33.

¹⁰⁵ Ibid 37.

¹⁰⁶ Ibid 40.

¹⁰⁷ Garton, *The Regulation of Organised Civil Society*, above n 13, 1.

¹⁰⁸ Ibid 119.

Externalities result from production of a particular good or service;

Information deficits prevent consumers from making rational choices; or

Nature of market means that production is naturally irregular.¹⁰⁹

Applying these to the activities of civil society organisations (CSOs), Garton concludes:

- The rationale of monopoly power is only relevant to professional associations, trade unions, and unique ideological belief systems,¹¹⁰ but potentially relevant in relation to specific activities where organisations have ‘first-mover’ advantages.¹¹¹
- The rationale of excessive competition does not apply, because price competition would probably be self-regulating.¹¹²
- As public goods are a strong presence in civil society, it is probably not apt to justify regulation, and CSOs are often better placed than state to determine quality and quantity of public goods provision.¹¹³
- The rationale of externalities may apply to certain types of activity,¹¹⁴ such as where there is a potential for harm to vulnerable parties.¹¹⁵
- The rationale of information deficits may justify regulation to prevent the exploitation of trust that the CSOs operate on a NFP basis, or to maintain the mission of for-profit CSOs.¹¹⁶ There is also potential for misuse through for example the inflating of costs, self-dealing or ignorance.¹¹⁷
- The rationale of irregular production applies, because philanthropic insufficiency and particularism will encourage sidestepping of activities.¹¹⁸

Garton then examines traditional social justifications for regulation. First, he considers the argument for regulation of ‘undeserved’ windfalls or economic rent, and suggests that it may be justified if an organisation operates where resources comparatively plentiful,¹¹⁹ but is not relevant in the case of redistribution of wealth or paternalism.¹²⁰ He rejects an argument justifying regulation to cure philanthropic insufficiency and amateurism.¹²¹ Finally, he considers rationales based on preserving its characteristics of independence, organisation, volunteerism

¹⁰⁹ Ibid 92.

¹¹⁰ Ibid 95.

¹¹¹ Ibid 96.

¹¹² Ibid 98.

¹¹³ Ibid 99.

¹¹⁴ Ibid 100.

¹¹⁵ Ibid 101.

¹¹⁶ Ibid 104-105.

¹¹⁷ Ibid 106.

¹¹⁸ Ibid 109.

¹¹⁹ Ibid 110-111.

¹²⁰ Ibid 112.

¹²¹ Ibid 113-114.

and non-profit distribution, and argues that the strongest argument for regulation is in respect of preserving its independence.¹²²

Garton rejects a justification of ‘modernising’ the sector as vague, and also rejects a rationale of encouraging the sector, suggesting that leads to over-proliferation of legal rules, and may be contradictory.¹²³

Scope of regulation

Garton argues there is no reason why regulation should be confined to the charitable sector, noting that CSOs falling outside the scope of the common law definition share structural characteristics and social functions.¹²⁴ He recommends that the scope of regulation should be broadly regulated through a structural/operational definition developed by the John Hopkins Comparative Project,¹²⁵ with the regulator having power to determine marginal cases.¹²⁶

Regulatory design

Garton considers the executive agency (rather than the legislature or judiciary) as the appropriate regulatory body, combining institutional efficiency, broader policy considerations, and a wider range of tools. This should be supplemented by courts regulating through the control of maladministration.¹²⁷

Garton notes but does not consider in detail modes of self-regulation, observing four perceived advantages: 1) greater expertise; 2) greater efficiency; 3) independence from central government; and 4) lower cost.¹²⁸

In examining strategies of regulation, Garton suggests ‘command and control’ (in the sense of prohibitions) as best suited to preventing anti-competitive tactics, controlling campaigning, and maintaining structural characteristics.¹²⁹ He argues that regulation by contract has serious weaknesses, because of 1) a lack of regulatory coordination where there are different contractual authorities, including private sector; 2) serious threats to independence; 3) potential to undermine volunteerism; and 4) high compliance costs.¹³⁰ He views information disclosure as a paradigm for tackling information asymmetry, which doesn’t threaten independence but depends upon donors having the time and inclination to make use of register.¹³¹ Garton also noted that while some observers had thought there was a conflict of interest because of the ‘soft’ tools of education and advice, as used by the Charity Commission in the UK, the Strategy Unit

¹²² Ibid 114-115.

¹²³ Ibid 118-119.

¹²⁴ Ibid 143, 164.

¹²⁵ See generally Lester M Salamon, *Defining the Nonprofit Sector: A Cross-National Analysis* (Manchester University Press, 1997). This major comparative project defined the not-for-profit sector using five elements: 1) organized; 2) private; 3) self-governing; 4) non-profit-distributing; and 5) non-compulsory.

¹²⁶ Garton, *The Regulation of Organised Civil Society*, above n 13, 195-197.

¹²⁷ Ibid 198-199.

¹²⁸ Ibid 202-203.

¹²⁹ Ibid 209.

¹³⁰ Ibid 216-217.

¹³¹ Ibid 217.

had concluded it should retain this role and as long as it clearly distinguished between advice and instructions.¹³²

SUSAN PASCOE, *REGULATING THE NOT-FOR-PROFIT SECTOR* (2008)

This report by the Commissioner of the State Services Authority (Vic), investigated the regulation of the Not-for-Profit (NFP) sector from theoretical and empirical perspectives, reviewed regulatory theory, detailed the context of NFPs in Victoria, and provided an overview of regulatory practice in several jurisdictions. It drew particularly on the work of Christine Parker (extracted below) and the State Services Authority's 2007 review of regulation in the NFP sector (extracted below).

Regulatory design

The review of regulatory theory noted some key conclusions:

- attempting to regulate to avoid all potential community risks is impossible and extremely costly, therefore regulation should only be imposed if it is necessary;
- regulation should be principles-based, flexible and responsive to industry need, so it can achieve its objectives at the lowest possible cost; and
- self-regulation should be used where possible, as successful self-regulation combines flexibility with a reduction in the regulatory burden and encourages industry to take ownership of the regulatory objectives.¹³³

The report recommended a co-regulatory approach to NFP regulation, in recognition on the strong focus of NFPs on member and client interests, and close links between members and decision makers which created a natural level of self-regulation. It also noted benefits such as reducing the regulatory burden, and more responsive regulatory approaches which preserved the unique characteristics of NFPs. Co-regulation was also seen as avoiding some of the pitfalls of pure self-regulatory approaches, including that self-regulators act in the public interest, it avoids anti-competitive practice, requires adequate transparency, avoids the zealous operators who increase their own burden, and evaluates the effectiveness of the approach.¹³⁴ The report also concluded that, in respect of government contracting, there was a strong argument for light touch regulation because of the close alignment between government and NFP objectives, and the natural level of self-regulation within the sector.¹³⁵

CHRISTINE PARKER, 'SELF-REGULATION AND THE NOT-FOR-PROFIT SECTOR' (2007)

Regulatory goals

In this study of the role of self-regulation in regulating the NFP sector, commissioned by the Victorian Government, Professor Parker argues that the primary objective of regulation is to change behaviour to meet objectives. She suggests relevant objectives for NFPs as: "sustainable community organisations that are faithful to their missions, support for community activities, confidence and trust in the sector, high quality service delivery, appropriately informed donors,

¹³² Ibid 219.

¹³³ Pascoe, *Regulating the Not-for-Profit Sector*, above n 10, 3.

¹³⁴ Ibid 17.

¹³⁵ Ibid 19.

and efficient expenditure of funds”.¹³⁶ Regulation should also meet the criteria of efficiency, effectiveness and legitimacy.¹³⁷

Regulatory design

Parker was commissioned to discuss whether her concept of ‘open self-regulation’ could apply to the NFP sector. She described this concept as “an ideal situation in which the entity goes about its business in its normal way while meeting publicly defined standards, objectives or values applicable to that activity”.¹³⁸ The following principles must be included: consultation with stakeholders; policies and procedures allowing stakeholders to contest decisions affecting them; public disclosure of information; possibility of greater coercion or sanctions for self-regulator; and regular self-evaluation or ‘triple loop’ learning.¹³⁹

The concept envisages government as helping to shape the self-regulation of the sector. She identifies several risks of self-regulation: 1) motivating entities to regulate in accordance with publicly defined standards; 2) making it open and accountable enough to count as open self-regulation; 3) avoiding costly and overly burdensome self-regulation; and 4) determining whether regulation is actually efficient.¹⁴⁰ She discusses the concept of the ‘enforcement pyramid’ by Ayres and Braithwaite, and the concept of ‘earned autonomy’, which refers to ‘the idea that entities must earn the right to be trusted’.¹⁴¹

Parker identifies a number of strategies for meta-regulation, such as government roundtables with industry; providing advice and guidance; official endorsement of codes of conduct; contract requirements; requiring standards or participation in self-regulatory scheme participation as a condition of licensing or registration; and mandatory industry codes.¹⁴²

In relation to whether self-regulation could work in the NFP sector, she cites the following factors in its favour: 1) the internal values of NFPs mean they are more likely to be receptive to regulating in accordance with public values and less susceptible to market pressures; 2) there is a high level of community trust; 3) generally a lighter regulatory burden imposed on NFPs; 4) it is consonant with partnership with government in service delivery; 5) there is recognition of distinctiveness and contribution of NFP sector; 6) and there should parity of treatment with new forms of regulation of for-profit sector.¹⁴³

However, she cautions that: 1) competitive pressures that may divert them from internal values; 2) their ideology may be out of kilter with public standards; and 3) very small organisations which have little capacity to self-regulate.¹⁴⁴ One option is for small associations to join up with broader sector-level regulatory association, or have different ‘tracks’ of organisations.¹⁴⁵ She also

¹³⁶ Parker, *Self-Regulation and the Not-for-Profit Sector*, above n 10, 4.

¹³⁷ *Ibid* 4.

¹³⁸ *Ibid* 1.

¹³⁹ *Ibid* 12-13.

¹⁴⁰ *Ibid* 5-6.

¹⁴¹ *Ibid* 7.

¹⁴² *Ibid* 9-10.

¹⁴³ *Ibid* 15-16.

¹⁴⁴ *Ibid* 17-18.

¹⁴⁵ *Ibid* 17.

observes that some organisations may be so committed to values that they cannot respond reasonably or even abuse the trust.¹⁴⁶

She suggests a principle-based approach is more flexible and focuses more appropriately on outcomes, although at a cost to certainty. She notes that the UK National Compact embeds such principles in funding and procurement, and suggests that this could also apply in relation to fundraising legislation and corporate governance principles.¹⁴⁷

She suggests a model of a single legislative framework for all registration/licensing requirements or the creation of a single 'hub' within government. She concludes with the observing the need to establish better base networks, provide education, training, and advice to support self-regulation.¹⁴⁸

RECOMMENDATION CM/REC(2007)14 OF THE COMMITTEE OF MINISTERS TO MEMBER STATES ON THE LEGAL STATUS OF NON-GOVERNMENTAL ORGANISATIONS IN EUROPE (2007)

This recommendation sets out some basic principles in relation to non-governmental organisations within the Council of Europe. Relevantly, these include:

28. The rules governing the acquisition of legal personality should, where this is not an automatic consequence of the establishment of an NGO, be objectively framed and should not be subject to the exercise of a free discretion by the relevant authority.

29. The rules for acquiring legal personality should be widely published and the process involved should be easy to understand and satisfy.

30. Persons can be disqualified from forming NGOs with legal personality following a conviction for an offence that has demonstrated that they are unfit to form one. Such a disqualification should be proportionate in scope and duration.

31. Applications in respect of membership-based NGOs should only entail the filing of their statutes, their addresses and the names of their founders, directors, officers and legal representatives. In the case of non-membership-based NGOs there can also be a requirement of proof that the financial means to accomplish their objectives are available.

32. Legal personality for membership-based NGOs should only be sought after a resolution approving this step has been passed by a meeting to which all the members had been invited.

33. Fees can be charged for an application for legal personality but they should not be set at a level that discourages applications.

34. Legal personality should only be refused where there has been a failure to submit all the clearly prescribed documents required, a name has been used that is patently misleading or is not adequately distinguishable from that of an existing natural or legal person in the state

¹⁴⁶ Ibid 17.

¹⁴⁷ Ibid 18-20.

¹⁴⁸ Ibid 22-23.

concerned or there is an objective in the statutes which is clearly inconsistent with the requirements of a democratic society.

35. Any evaluation of the acceptability of the objectives of NGOs seeking legal personality should be well informed and respectful of the notion of political pluralism. It should not be driven by prejudices.

36. The body responsible for granting legal personality should act independently and impartially in its decision making. Such a body should have sufficient, appropriately qualified staff for the performance of its functions.

37. A reasonable time limit should be prescribed for taking a decision to grant or refuse legal personality.

38. All decisions should be communicated to the applicant and any refusal should include written reasons and be subject to appeal to an independent and impartial court.

39. Decisions on qualification for financial or other benefits to be accorded to an NGO should be taken independently from those concerned with its acquisition of legal personality and preferably by a different body.

40. A record of the grant of legal personality to NGOs, where this is not an automatic consequence of the establishment of an NGO, should be readily accessible to the public.

41. NGOs should not be required to renew their legal personality on a periodic basis.

...

43. NGOs should not require approval by a public authority for a subsequent change in their statutes, unless this affects their name or objectives. The grant of such approval should be governed by the same process as that for the acquisition of legal personality but such a change should not entail the NGO concerned being required to establish itself as a new entity. There can be a requirement to notify the relevant authority of other amendments to their statutes before these can come into effect. ...

47. NGOs should ensure that their management and decision-making bodies are in accordance with their statutes but they are otherwise free to determine the arrangements for pursuing their objectives. In particular, NGOs should not need any authorisation from a public authority in order to change their internal structure or rules

...

62. NGOs which have been granted any form of public support can be required each year to submit reports on their accounts and an overview of their activities to a designated supervising body.

63. NGOs which have been granted any form of public support can be required to make known the proportion of their funds used for fundraising and administration.

64. All reporting should be subject to a duty to respect the rights of donors, beneficiaries and staff, as well as the right to protect legitimate business confidentiality.

65. NGOs which have been granted any form of public support can be required to have their accounts audited by an institution or person independent of their management.

BETTER REGULATION TASK FORCE, *BETTER REGULATION FOR CIVIL SOCIETY* (2005)

This UK report focused on three priorities to improve regulation: focusing on the impact on the volunteer, the impact on social innovation, and meeting need.¹⁴⁹

It considered that self regulation and co-regulation should be used more widely, such as through recognition of 'kitemarks' as defining service levels, identifying regulatory requirements that become unnecessary when a self-regulatory standard is achieved, and adopting kite marks in risk assessments.¹⁵⁰

It made a series of specific recommendations relating to regulatory overlap and in relation to specific organisations. Of particular interest, it suggested that the obligation to diversify assets in relation to endowed charitable trusts may discourage people from establishing such trusts, and recommended the legislation be changed to remove that obligation within the lifetime of the settler.¹⁵¹

PANEL ON THE NONPROFIT SECTOR, STRENGTHENING TRANSPARENCY, GOVERNANCE AND ACCOUNTABILITY OF CHARITABLE ORGANIZATIONS (2005)

The Panel was convened on the encouragement of the US Senate Finance Committee, and brought together the nonprofit sector in this discussion. It developed eight overarching principles to guide its recommendations:

- A vibrant charitable community is vital for a strong America.
- The charitable sector's effectiveness depends on its independence.
- The charitable sector's success depends on its integrity and credibility.
- Comprehensive and accurate information about the charitable sector must be available to the public.
- A viable system of self-regulation and education is needed for the charitable sector.
- Government should ensure effective enforcement of the law.
- Government regulation should deter abuse without discouraging legitimate charitable activities.

¹⁴⁹ Better Regulation Task Force (UK), *Better Regulation for Civil Society: Making Life Easier for Those Who Help Others*, above n 16, 4.

¹⁵⁰ *Ibid* 8-9, 48-49.

¹⁵¹ *Ibid* 28.

- Demonstrations of compliance with high standards of ethical conduct should be commensurate with the size, scale, and resources of the organisation.¹⁵²

Its recommendations included:

- Increasing resourcing of the Internal Revenue Service (IRS) and state regulators of NFPs;¹⁵³
- Improvement of annual information returns to the IRS;
- The IRS should not implement periodic review of NFP's tax-exempt status but rather focus on examining current returns, but board members should be encouraged to review their governing documents and policies at least once every five years;
- Require audits for organisations with at least \$1 million in annual revenue, and independent reviews by accountants for those with revenues of between \$250,000 and \$1 million;
- Organisations should as best practice report more detailed data, but this should not be required by government;
- Requirements to disclose remuneration paid to board and five highest paid employees;
- Minimum of three members on a governing board to qualify for tax-exempt status, and at least a third to be independent if a public charity, but no maximum number;
- Disclosure of independent board members;
- Prohibition on individuals barred from service on corporate boards or convicted of crimes related to breaches of fiduciary duty;
- Encouragement of separate audit committees and financially literate board members as best practice; and
- Adoption of a conflict of interest policy, to be disclosed to the IRS.¹⁵⁴

NATIONAL CENTER FOR PHILANTHROPY AND THE LAW, STUDY OF MODELS OF SELF-REGULATION IN THE NONPROFIT SECTOR (2005)

This report was commissioned by the Panel for Nonprofit Sector and examines structures where another organisation sets standards for, oversees, accredits or regulates other organisations. It focused on categorizing the available models,¹⁵⁵ drawing on descriptions of such regulatory entities.

It suggested the following factors had an impact on effectiveness in self-regulation:

¹⁵² Panel on the Nonprofit Sector, *Strengthening Transparency, Governance, Accountability of Charitable Organizations* (June 2005) <<http://www.nonprofitpanel.org/Report/final/Index.html>>, 4.

¹⁵³ Ibid 4-5.

¹⁵⁴ Ibid 7-8.

¹⁵⁵ The National Center on Philanthropy and the Law, *Study on Models of Self-Regulation in the Nonprofit Sector*, above n 17. Note there are no page numbers for this resource.

- Availability of legal or other enforceable sanctions;
- Value of accreditation, including to funders and members;
- Specificity of sector or subsector, or activity, regulated;
- Transparency in the form of dissemination of standards and disclosure of processes;
- Other factors such as ratio of regulatory staff and budget; pre and post-certification processes; and immediacy of threat of government regulation.

KAREN SPINDLER, OPTIONS FOR IMPROVING NOT-FOR-PROFIT REGULATION (2005)

This paper by the Allen Consulting Group was commissioned by the Victorian Government to consider improvements to NFP regulation.

Regulatory Objectives

Spindler examined the regulatory purposes from different perspectives. From the perspective of the sector, the purposes were: to provide a corporate structure; to set out minimum standards of governance; and to provide government support. Ultimately these served to protect community support vital to the sector.¹⁵⁶

The community's interest in regulation was to facilitate the capacity of sector to engage in society and to ensure accountability. The interest of the government was to facilitate NFP activities; ensure accountability; and to provide concessions and support.¹⁵⁷

The rationale for government intervention in terms of both accountability and support was identified as market failure, such as the inability of donor to monitor adequately the use of money, the fact that governments could not rely solely on self-discipline to ensure appropriate use of money; and the fact that the benefits of NFP activity extend beyond immediate beneficiaries.¹⁵⁸

Regulatory Principles

The following were identified as key regulatory principles, from a wide range of key regulatory sources. Regulation should be:

- the minimum necessary to achieve objectives;
- not unduly prescriptive;
- accessible, transparent and accountable;
- integrated and consistent with other laws;
- communicated effectively;
- mindful of the compliance burden imposed; and

¹⁵⁶ Spindler, *Improving Not-For-Profit Law and Regulation: Options Paper*, above n 10, 4.

¹⁵⁷ *Ibid* 5.

¹⁵⁸ *Ibid* 6.

- enforceable.¹⁵⁹

Assessing current regulation against these criteria, the paper concluded that it did not satisfy the principles in three main areas: accessibility, transparency, and accountability; integration and consistency with other laws; and the compliance burden on the sector.¹⁶⁰

Regulatory Design

The report suggested significant risks in trying to pursue national uniformity as the only path to reform, and preferred instead the development of ‘model’ legislation in areas such as incorporation and fundraising, together with reciprocal recognition, through existing forums.¹⁶¹

It proposed as various options for improving regulation:

- sector-specific regulation and tools—such as specific corporate forms, exemptions from corporate law provisions on the basis of size, and tailored guidance, model constitutions and a best practice reporting framework;
- developing a closer relationship between regulators and the sector—improving individual institutional links; improving regional and cross-border links through existing forums, such as inviting sector representatives to attend Ministerial councils; by nominating a Minister to have prime responsibility for the NFP sector; or through a joint government/sector working group; and
- establishing a dedicated regulatory function for the not-for-profit sector, either through: co-ordination of regulators (or a ‘virtual centre of regulation’); or a dedicated regulator for the sector.¹⁶²

WOODWARD & MARSHALL, REFORMING NOT-FOR-PROFIT REGULATION (2004)

This report included a major survey of NFP organisations. Its key findings included that

- just over half thought summary financial information should be enough, 39% thought the information should be fully audited, and 9% thought no information should be public;
- the majority wanted a new regulator but did not think ASIC was the appropriate regulator, and were concerned about regulatory duplication;
- the needs of NFPs differ in their reliance on volunteers, the availability of tax concessions, and the greater complexity of their stakeholder relationships.

Purposes of regulation

The report identified several arguments ‘for’ and ‘against’ disclosure by NFPs, set out in the below table (at p. 193 of the report).

¹⁵⁹ Ibid v, 37.

¹⁶⁰ Ibid vii.

¹⁶¹ Ibid x.

¹⁶² Ibid xi.

Table 1: Policy considerations - disclosure by NFP organisations

For	Against
<ul style="list-style-type: none"> the 'public' are a stakeholder even in member organisations because tax forgone is 'public' money 	<ul style="list-style-type: none"> implementation of the principle of 'freedom of association' should mitigate against excessive regulation
<ul style="list-style-type: none"> donor confidence relies on a high degree of accountability - there cannot be this accountability without disclosure 	<ul style="list-style-type: none"> disclosure can add considerable time and expense, especially for organisations relying on volunteers and/or irregular, limited funding
<ul style="list-style-type: none"> there are 'for-profit' agencies that charge for access to information databases about NFP organisations - this demonstrates donor demand for information, not currently being met by statutory requirements 	<ul style="list-style-type: none"> there will always be some 'bad apples' and greater disclosure does not prevent this
<ul style="list-style-type: none"> standardisation of the information that is disclosed aids comparability between organisations 	<ul style="list-style-type: none"> better to rely on grant-makers (government and non-government) and sponsors - they can/should insist on, and monitor, disclosure

Functions of Regulator

A majority of those surveyed suggested the regulator should combine compliance, determination of charitable status, advice, sector advocacy and training. The survey showed greater enthusiasm for advice (86%) and advocacy (69%) than for tax determinations and compliance, or training.¹⁶³ The authors noted respondents may have indicated a need for all of these functions, but not necessarily in one body,¹⁶⁴ and observed that in the United Kingdom the major peak body, the NCVO, had advocated a separation of the taxation and advisory functions of the Charity Commission.¹⁶⁵

Location of Regulator

54% of the respondents in the survey believed ASIC was inaccessible to non-business people and 70% believe the *Corporations Act* was more suited to for-profit companies.¹⁶⁶ The authors, however, recommended a new independent advisory body rather than a consolidated regulator, in view of feedback from the sector and drawing on experience.¹⁶⁷

Regulatory Proposals

The report suggested modifying the *Corporations Act* requirements with respect to: including a sliding scale fee structure; requiring information to be disclosed to stakeholders rather than shareholders; including a NFP-specific accounting standard; requiring forms of auditing; inserting a plain language guide; inserting objects clauses and directors' duty to pursue objects; making a non-distribution of profits clause compulsory; and improving clarity and remedies for breach of

¹⁶³ Woodward and Marshall, *Reforming Not-for-profit Regulation Project*, above n 52, 88.

¹⁶⁴ *Ibid* 89.

¹⁶⁵ *Ibid* 89.

¹⁶⁶ *Ibid* 3.

¹⁶⁷ *Ibid* 3-4.

objects.¹⁶⁸ The authors also recommended considering a single, specialist NFP legal structure in light of the UK specialist structure.¹⁶⁹

PANEL ON ACCOUNTABILITY AND GOVERNANCE IN THE VOLUNTARY SECTOR, *BUILDING ON STRENGTH* ('BROADBENT REPORT') (1999)

This was a major Canadian independent report, initiated by the Voluntary Sector Roundtable, which produced recommendations for government and the sector itself.

Regulatory Context

The “starting point” was the consensus that “the social importance and value of the sector is enormous.”¹⁷⁰ Five basic principles guided the Panel:

- The voluntary sector’s role in building a sense of trust and social co-operation should be strengthened;
- A diverse and active voluntary sector promotes a healthy democracy and should be encouraged;
- A healthy and accountable voluntary sector requires capacity and this needs to be strengthened;
- The autonomy and self-governance of the sector must be recognised; and
- The diversity of the sector should be respected.¹⁷¹

Independent regulator

The Panel proposed a “quasi-independent” Voluntary Sector Commission to supplement the audit role of Revenue Canada. Its functions would be:

- to provide support, information and advice about best practices related to governance and accountability to voluntary organisations;
- collect and provide information to the public;
- recommend whether new applicants should be granted charitable/public benefit status;
- assist organisations to maintain compliance with Revenue Canada’s regulatory requirements by working collaboratively with them;
- recommend deregistration in cases where organisations are persistently unwilling to comply with regulations;
- and investigate public complaints.¹⁷²

¹⁶⁸ Ibid 4.

¹⁶⁹ Ibid 5.

¹⁷⁰ Panel on Accountability and Governance in the Voluntary Sector, *Broadbent Report*, above n 15, 9.

¹⁷¹ Ibid 9-10.

¹⁷² Ibid vii.

In its advisory capacity, it would be open to any organisation but its regulation would focus on registered charities. Members would be appointed by the government in a “genuine partnership model”.

The regulator should have certain features. It should:

- have expertise from the sector in its leadership and staff;
- enhance the functions of intermediary and other voluntary organisations;
- avoid being either large or bureaucratic in nature;
- work through partnerships with the sector and others;
- be accessible to the sector and the public;
- have secure and stable funding;
- be insulated from political interference; and
- be sufficiently flexible to evolve over time.¹⁷³

The report blended features of several model in its blueprint. In its view, the Commission should have an arms'-length relationship with government and the sector; have between 5-7 independent Commissioners with at least a third having experience in the sector; it would report through a Minister and table an annual report; it would be funded federally; it should work closely with the sector and Revenue Canada; it should be decentralised and have a small staff. It noted that it was similar to the Charity Commission but differed because a federal commission alone would be more restricted in its role.¹⁷⁴

Self-regulation

The Panel considered the option of mandatory accreditation as a form of self-regulation, but considered there were several practical barriers to adopting this more widely. It did suggest, however, self-assessment against clear standards of governance as an option.¹⁷⁵

Regulatory Requirements

The Panel's view was that registered charitable organisations (who have access to tax concessions) should:

- provide certain information to the government about its governance, programs and finances;
- adhere to a code of ethical fundraising; and
- practise transparency by responding appropriately to requests for information.¹⁷⁶

¹⁷³ Ibid 63.

¹⁷⁴ Ibid 64.

¹⁷⁵ Ibid 34.

¹⁷⁶ Ibid v.

The information all organisations should provide to Revenue Canada (and cross-filed with the independent regulator) included:

- description of the organisation's mission, programs and intended results;
- financial statements, as approved by the board;
- description of fundraising activities over the past year including amount of revenues raised and amount spent on raising them;
- description of basic governance structures, including size of board and methods for selecting board members;
- disclosure of the code of ethical fundraising to which the organisation adheres;
- description of the organisation's approach to responding to complaints; and
- how to get further information directly from the organisation.¹⁷⁷

Larger organisations (with annual revenue of above \$200,000) should additionally be required to specify how the elements of good governance are met.¹⁷⁸ In a competitive bidding process, private firms should be required to disclose similar information as charitable organisations.¹⁷⁹ For-profit commercial fundraisers should be licensed and bonded with provincial governments.¹⁸⁰

While supporting the principle of outcome-based reporting, the Panel was quick to note this should not be done in a simplistic way or without investment in adequate capacity.¹⁸¹

It also recommended, relevantly:

- greater consistency in accounting practices;
- implementation of intermediate sanctions (measures other than deregistration) for non-compliance;
- development of a new nonprofit corporation bill and greater collaboration between provinces to deal with organisational laws; and
- review and limits on personal liability for directors.¹⁸²

Governance

The report also developed a code of good governance practices, focusing on eight key tasks:

- steering toward the mission and guiding strategic planning;

¹⁷⁷ Ibid 31.

¹⁷⁸ Ibid v, 31.

¹⁷⁹ Ibid 32.

¹⁸⁰ Ibid v.

¹⁸¹ Ibid v.

¹⁸² Ibid vii.

- being transparent, including communicating to members, stakeholders and the public and making information available upon request;
- developing appropriate structures;
- ensuring the board understands its role and avoids conflicts of interest;
- maintaining fiscal responsibility;
- ensuring that an effective management team is in place and overseeing its activities;
- implementing assessment and control systems; and
- planning for the succession and diversity of the board.¹⁸³

Statutory Definition

The Panel also recommended that a ‘charity-plus’ model be adopted, where the common law criteria would remain but additional categories would be proposed by a government sector task force and legislated, subject to periodic review.¹⁸⁴

ONTARIO LAW REFORM COMMISSION, *REPORT ON THE LAW OF CHARITIES (1996)*, VOLUMES 1 AND 2

Purposes of regulation

This Report, considering the regulation of charities and other NFPs in Canada, identified the following as reasons to regulate charities:

- The regard society has for the charitable intentions of donors: through facilitating charitable activity through appropriate legal forms, and protecting charity from vulnerability to fraud and waste.
- To ensure legitimacy and authenticity of recipients of state-conferred privileges.
- Concern that the charitable sector will usurp the functions of the state or market, or a related fear that the sector will shelter economic activity from taxing and regulatory powers of the state. It noted that this may still be a valid concern although it needed to be questioned, and suggested that concerns that charitable organisations were ‘too large’ really reflected a concern that they were no longer truly charitable.
- Delivery of government services through the third sector, entailing government responsibility for effectiveness.¹⁸⁵

The Commission also observed that regulation should not be based on the narrow premise that “charities are doing the work of government” and that tax concessions are therefore “state subsidies” or “state incentives”. The tax expenditure analysis did not “do justice to the diversity

¹⁸³ Ibid 24.

¹⁸⁴ Ibid vi.

¹⁸⁵ Ontario Law Reform Commission, *Report on the Law of Charities*, above n 20, 14-17.

of the sector”, did not apply to a very large number of charities, and undermined the sector’s self-understanding.¹⁸⁶ Rather, it should be based on the general premise that the sector is a “third order of organisation” motivated predominantly by altruistic purposes, so the role of the state is to facilitate and protect.¹⁸⁷

Regulatory objectives

It observed that two common regulatory objectives underlay these concerns: 1) to ensure both a certain loyalty to purpose; 2) and a certain level of effectiveness.¹⁸⁸

Independent regulator

The Commission recommended the establishment of a new provincial body, the “Nonprofit Organizations Commission”. This would cover all nonprofit entities. It would have five main divisions, each headed by a commissioner: registrations, fundraising, audits and investigations, education, and chair. It would have administrative, educational and investigative powers.¹⁸⁹

Functions

Its functions would include:

Administering a computerised registration database covering all nonprofit corporations, charitable trusts and charitable associations;¹⁹⁰

Reviewing registered fundraising campaign documents for compliance with the law;¹⁹¹

Conducting inquiries, audits and investigations; and

Providing advice and counsel to charitable fiduciaries.¹⁹²

KARLA SIMON, THE PRINCIPLES OF NOT-FOR-PROFIT REGULATION (1998)

Regulatory principles

This statement from the then President of the International Center for Not-for-Profit Law sets out some basic global principles of NFP regulation:

- The law should “embody principles of clarity, simplicity and administrability”, and there should be relatively few legal rules, and avoidance of redundancy and overlap;
- The regulatory structure should embody legal traditions but also be open to other countries for ideas, and in particular that in common law countries legal form should not guide regulation;
- The legal structure should recognise that such organisations are both social and economic, public and private, so should not be too tightly regulated but should be subject to state control where they provide needed services, probably at the local level;

¹⁸⁶ Ibid 333-334.

¹⁸⁷ Ibid 334.

¹⁸⁸ Ibid 17.

¹⁸⁹ Ibid 563.

¹⁹⁰ Ibid 564.

¹⁹¹ Ibid 565.

¹⁹² Ibid 566.

- Laws and regulations should ensure transparency and accountability of NFPs and of the government regulating them, including annual reporting of financing and activities, fundraising and tax filings, to ensure public trust in the sector;
- The choice of regulatory body depends on the competence of those bodies, with national bodies offering standardised and therefore fairer treatment of NFPs;
- National tax exemption and deductibility issues should be determined by a national body with the necessary knowledge and expertise, and local and regional decisions can be tied into national decisions;
- There should be clearly defined rules regulating NFPs, including issues of organisation, registration, and governance;
- There should be a right of appeal to an independent judiciary of all adverse decisions by a regulator;
- The state should recognise and confirm in legislation state support of the NFP sector, including direct and indirect subsidies; and grants should be competitively awarded on the basis of well-defined standards;
- Tax laws should differentiate between public benefit and mutual benefit organisations, on the basis that the former provide greater public service;
- Public scrutiny of organisations with tax subsidies is natural but should not be so intrusive as to undermine independence, and should be focused on protecting the public trust.¹⁹³

CULLEN, 'THE AUSTRALIAN CONSTITUTION AND THE REGULATION OF CHARITABLE AND PHILANTHROPIC INSTITUTIONS' (1991)

In this conference paper, Cullen considered the effect of the *Constitution* on the regulation of the NFP sector. He suggested that, while some charitable and financial institutions could be considered 'trading and financial' institutions under a current activities test to be regulated under the corporations power, this would be "hazardous" and "highly challenging". He rejected the use of the interstate commerce provision, and suggested the possibility that trans-Tasman regulation could be an option under the external affairs power.¹⁹⁴

He considered that the High Court had "roundly endorsed" the use of taxation power as instrument for regulating behaviour beyond the bounds of ordinary taxation, but it had not been used to construct a system of general regulation, because the mechanisms it allowed for regulating were limited. He considered other possible heads of power as bankruptcy and insolvency; invalid and old age pensions; and provision of other listed social welfare benefits.¹⁹⁵

¹⁹³ Karla W Simon, *Principles of Regulation for the Not-for-Profit Sector* (International Center for Not-for-profit Law, 1998) <<http://www.icnl.org/knowledge/pubs/PrinciplesRegulation.pdf>>.

¹⁹⁴ Cullen, 'The Australian Constitution and the Regulation of Charitable and Philanthropic Institutions' above n 50, 121-123.

¹⁹⁵ Ibid 125-126.

Ultimately, while Cullen thought that it would be constitutionally possible to implement a virtually comprehensive national scheme based on heads of power, he argued that this would be flawed in terms of political strategy and political morality. It would violate the federal compact and generate unnecessary High Court litigation, and a negotiated national scheme and intergovernmental cooperation was preferable.¹⁹⁶

¹⁹⁶ Ibid 132.