

# **A Better Framework**

reforming not-for-profit regulation

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# EXECUTIVE SUMMARY

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## Context

The not-for-profit (NFP) sector plays a vital role in our society. In economic terms alone:

- s Australians give \$2.8 billion annually to NFP organisations
- s NFPs contribute 4.7% of GDP and account for 6.8% of total employment
- s in comparative terms, NFPs add more to GDP than the mining industry.

The underlying health of the NFP sector is at risk. The regulatory framework that underpins the sector is complex and riddled with inconsistencies. It is time for some preventative medicine. The relevant laws and regulatory bodies need to be fair, consistent and clear in order to promote NFPs that are transparent, accountable and credible. If these fundamentals are 'right', then growth and innovation are more likely to occur.

Currently, there is a myriad of possible legal structures for NFPs – companies, associations, foundations, co-operatives, church auspice, aboriginal corporations, Royal Charter and more. Combined with this is a confusing mix of State and Federal regulation and regulators, and a lack of nationally consistent reporting obligations. These factors provide significant impediments to accountability and could jeopardise donor confidence. Disclosure by NFPs should be directed to the special needs of NFP stakeholders. Regulation should also help entrench a culture of accountability.

While the views of business have been canvassed before any corporate law reforms have been implemented, the views of NFPs have been overlooked. To obtain the views of those involved in a wide range of NFPs, a detailed survey was sent to all of the 9,800 companies limited by guarantee on the public register maintained by ASIC (the Australian Securities and Investments Commission) as at 1 March 2002 (virtually all of which are NFPs). Over 1,700 completed replies were received. The data collected gives, for the first time, a national snap shot of those NFPs that are registered as companies limited by guarantee.

## National survey

The survey sought a wide range of information about:

- the organisation's profile - size, principal activity, number of volunteers, member-serving vs public-serving, tax status
- why a company structure had been chosen instead of, say, an incorporated association and whether or not this structure had met the organisation's needs
- who were regarded as the organisation's key stakeholders and what reporting was made to them
- the composition and experience of the Board of Directors – Board size, age, gender and skills, whether fees are paid to non-executive directors, how Board members are chosen, Board independence etc
- the procedures and structures of the Board – what is seen as the organisational role of the Board, frequency and conduct of meetings etc
- whether the current regulatory framework is working – views on what information (if any) should be disclosed to the public, what is the attitude of NFPs to their dealings with ASIC, should there be a new specialist regulator for NFPs.

This Report details the findings of the survey and explores any significant differences between the responses of NFPs based on, for example, their tax status, principal activity or member-serving vs public-serving.

This Report makes several recommendations for reform and identifies some areas for further deliberation. For a summary of these recommendations, together with a summary of some of the supporting findings, see pages 3 -10.

## Key findings

- Respondents indicated that they chose a company structure because: it better suits national or multi-state organisations (34% of respondents); the scale of trading activities (40%); a preference for dealing with ASIC rather than State regulators (31%); and public perception or status (52%) (such as the view that 'serious' or 'more sophisticated' NFPs use this structure rather than the incorporated associations' regime). These responses highlight that the State and Territory based incorporated associations regime does not meet the needs of many NFPs, such as peak bodies or small but national organisations.

- On public disclosure, a startling 9% of respondents thought that no information should be made available to the public, while only 39% agreed with fully audited accounts being disclosed (as is currently required by the Corporations Act), and just over half thought summary financial information should be enough.
- Respondents clearly thought that the Corporations Act and the way it is implemented by ASIC is more appropriate to 'for-profits' than for them. The majority were in favour of a new regulator to oversee NFPs, as recommended by the Charity Definition Inquiry, but concerned to avoid duplication. Better regulation, rather than simply more regulation, is the key.
- NFPs and their needs differ from 'for-profits' in several ways, for example
  - s they rely heavily on volunteers,
  - s they enjoy exemption from income tax
  - s they have more stakeholders to consider (members, volunteers, grant makers etc - not just shareholders interested in 'the bottom line').
- Nearly a third of NFPs reported difficulty recruiting directors and for some types of NFPs, the figure was significantly higher.

## Recommendations

The particular needs of the NFP sector have been overlooked in the company law reform process, and the dual State/Federal regime is causing problems. Increasingly, even very small NFPs operate on a national basis, and this is not facilitated by the existing State based incorporated associations' regime. After a decade of a dual regime – companies governed by a national scheme and associations governed by varying State/Territory based legislation – it is time to combine the best elements of each of these with new ideas. The sector needs a national regulatory framework based on sound public policy, rather than disclosure requirements that vary vastly depending on jurisdiction and the nature of the legal structure adopted.

Arising out of the data, key recommendations for regulatory reform include:

- a single Commonwealth regulatory regime (this could be achieved by a referral of powers as recently occurred in the company law model)
- ASIC becoming the new regulator for all incorporated NFPs (companies and associations), at least until any new NFP regulator is introduced
- the establishment of a specialist NFP unit within ASIC
- plain language guide and replaceable rules for NFP organisations.

The survey results also demonstrate a need for additional support services for NFPs. A new independent NFP advisory body should be established to meet this need. A range of support services could be provided at low or no cost – for example, auditing, financial and taxation advice, legal advice, training for Board members, dispute resolution and mediation for stakeholders. This body could make a significant difference, particularly for small NFPs. Such an advisory body would be able to generate at least some of its funding from fees for service.

Recommendations are also made about minimum public disclosure requirements and the need for an NFP-specific accounting standard. Even member-serving organisations that do not receive direct government funding typically get income tax exemption, and therefore have the benefit of public funds through tax foregone. The corresponding responsibility needs to be a minimum level of public disclosure. Additional disclosure requirements should apply to larger NFPs. At the moment there is duplication, and often the disclosure that is required does not meet the needs of NFP stakeholders.

If important reforms are to take place, the sector itself will need to lobby for change, through individual NFPs, through peak organisations, and through bodies such as the newly established National Nonprofit Round Table. By getting the underlying regulatory framework 'right', accountability and confidence in the sector generally will be improved, and NFPs will have more time to concentrate on the important services that they provide to the community.

*This Report is available (in colour) on-line at <<http://cclsr.law.unimelb.edu.au/activities/not-for-profit/>>*

# SUMMARY OF RECOMMENDATIONS

The following are all the recommendations made in the Report and some issues that have been highlighted as requiring further deliberation. There is a cross reference in each recommendation to the relevant Chapter of the Report. The recommendations are grouped under the headings of Regulatory Framework, Legal Structures, Disclosure, Stakeholders and Boards. In order to give some context, there is a brief introduction to each recommendation.

## 1. REGULATORY FRAMEWORK

The regulatory framework underpins accountability, which in turn underpins confidence in the sector. It is a core issue that needs to be considered even before the related issue of disclosure. The existing two-tiered regulatory system (State/ Territory-based incorporated associations and a Federal company law regime) is inefficient, costly and does not meet the needs of small or large NFPs. The special needs of NFPs that are incorporated as companies limited by guarantee have been overlooked in changes to the *Corporations Act*. Their particular needs have sometimes been prejudiced by changes made at the behest of, or for the benefit of, business. Improvements in the legislative regime are long overdue.

### Recommendation 1: Single regulatory regime

A single Commonwealth statutory regime should be introduced for all corporate bodies (that is, 'for-profit' companies, NFP companies and incorporated associations) by referrals of power from the States to the Commonwealth, along the lines of what has been achieved for company regulation. Such a referral would enable a national approach to NFP regulation, with responsibility for registration and on-going regulation being conferred on ASIC.

*Report Reference: Chapter 4, Regulatory Framework*

In terms of who should be the regulator of NFP organisations, the survey identified that there is dissatisfaction with ASIC's performance as a regulator of NFP companies. For example, 54% of respondents believe it is inaccessible to non-business people and 70% of respondents believe that the *Corporations Act* and the way it is implemented by ASIC is more appropriate to 'for-profit' than NFP companies. In view of these (and other) findings, it appears that dissatisfaction with ASIC derives principally from the fact that ASIC is not a specialist NFP regulator.

### Recommendation 2: ASIC's role

As long as ASIC continues to regulate companies limited by guarantee, it should take steps to make itself more friendly to NFP users. Such steps might include:

- the establishment of a specialist unit within ASIC to deal with NFP companies, with further training for ASIC officers about the particular needs of NFP company stakeholders;
- a sliding fee structure for NFP companies, based on size
- a plain-language guide for NFP companies.

If ASIC assumes jurisdiction over all incorporated NFP organisations, as recommended in this Report, the need for these steps would be even greater.

*Report Reference: Chapter 4, Regulatory Framework*

Chapter 4, Regulatory Framework also considers the proposal for a completely new NFP regulator (such as recommended by the Charity Definition Inquiry), and its possible role(s). The Report discusses whether or not providing advice and training, ensuring compliance with regulatory requirements (such as disclosure obligations), determining charitable status (for taxation and other purposes) and providing advocacy on behalf of the NFP sector, should be combined in one body.

In view of feedback from the sector and drawing on experience in the UK, the Report concludes that these roles should not be combined. However, there is a clear need for NFP organisations to be able to draw on specialist, independent advice in a range of areas. This assistance should be provided by a new, independent advisory body, whether or not a new administrative body is established as recommended by the Charity Definition Inquiry. This body would be able to generate at least some of its funding from fees for service. Any shortfall could be met from a combination of funding from philanthropic sources and government.

The establishment of a new, independent advisory body would be of particular benefit to small to medium NFPs and would serve to strengthen the accountability and capacity of the sector.

### **Recommendation 3: Establish an independent NFP advisory body**

An independent NFP advisory body should be established to provide a range of support services for NFP organisations. This would create a centre of expertise in the specialised needs of these organisations. It would also underpin improved accountability and corporate governance practices within the sector. The body should be separate from, and independent of, government and the regulators (including any administrative body established to determine charitable status). The types of services that could be provided at low cost or possibly even 'no cost' to some organisations are:

- auditing
- financial and taxation advice
- legal advice
- training
- dispute resolution and mediation services for NFP stakeholders.

*Report Reference: Chapter 4, Regulatory Framework*

## 2. LEGAL STRUCTURES

The related goals of improved accountability and good corporate governance must be supported by the underlying legal structure(s) adopted by NFPs. If the legal structure meets the needs of the organisation, then it will be easier to build consistent and appropriate reporting obligations. In turn, these are the cornerstone of accountability.

There were several interesting findings about why a company limited by guarantee had been chosen as the legal structure. While a significant number were formed at a time when there was effectively no other option (and they have not subsequently chosen to transfer to the incorporated associations' regime), others have chosen the structure because of factors such as public perception and status, the scale of their trading activities and because they are a national or multi-State organisation. While the existing company limited by guarantee legal structure seems to be meeting the overall needs of many NFPs, the structure could be improved within the current regulatory framework.

There is a strong argument for tailoring the nature of what is disclosed and the fees payable to meet the different needs of NFPs.

### **Recommendation 4: Modify existing Corporations Act requirements**

While the existing company limited by guarantee structure has proved satisfactory in the main, some aspects need reform. These include:

- the fee structure should be revised to provide a sliding scale based on size
- information required for disclosure should be tailored to the needs of NFP stakeholders rather than to 'shareholders', and this needs to be supported by an NFP specific accounting standard
- the requirement to lodge audited accounts needs to be reconsidered for small NFP organisations
- a plain-language guide summarising the provisions/obligations relevant to NFP companies (along the lines of the Small Business Guide contained as Part 1.5 of the Corporations Act 2001(Cth)) should be available
- all NFP companies should be required to have an objects clause and the directors should have a duty to pursue those objects
- all NFP companies should be required to have a 'non-distribution' clause
- the remedies available for a breach of the objects clause need to be clarified and strengthened.

*Report Reference: Chapter 3, Legal Structure; Chapter 7 Stakeholders*

The current myriad of legal structures under which NFP organisations operate (incorporated association, company limited by guarantee, proprietary company, trust, cooperatives, Royal Charter, special Act of Parliament, aboriginal corporations) are confusing and hamper

accountability, particularly when combined with the dual Federal/State regime. In Chapter 3, Legal Structure, the Report looks briefly at some interesting reforms in the UK where two new types of company structure are being pursued. Neither the incorporated associations model nor the company limited by guarantee model is entirely satisfactory, especially for smaller, national, membership based organisations.

### **Recommendation 5: Future NFP legal structures**

A national regulatory regime should be implemented. It would be appropriate at that time to reconsider the range of existing legal structures used by NFP organisations. This would be with a view to introducing a single, specialist NFP legal structure. Whilst maintaining some level of choice is desirable, the current myriad of legal structures leads to confusion and inefficiencies in regulation. Consideration should be given to combining the best aspects of the corporations law and the incorporated associations regimes. The work being done by the UK government would be useful to explore. Any new structure should meet the needs of both small and large NFP organisations, and the issue of converting from existing forms should be addressed in a simple and no-cost way.

*Report Reference: Chapter 3, Legal Structure*

## **3. DISCLOSURE**

Public disclosure requirements are linked to an organisation's legal structure. The myriad of structures under which NFPs operate has resulted in inconsistencies and significantly disparate disclosure obligations, that are not based on any sound, overall public policy agenda.

Accountability relies on relevant, accurate and up-to-date disclosure. Without accurate information, members and other stakeholders are unable, when necessary, to consider action to constrain the Board or influence the direction of the organisation generally. Perhaps more importantly, if the NFP sector is not seen as accountable, public confidence will be jeopardised and donations put at risk.

The survey data (reported in Chapter 8, Disclosure) shows that the respondents are of the opinion that the current reporting obligations are excessive. This is not, of itself, reason to reduce disclosure. In fact, the Report recommends greater disclosure on some issues such as description of activities, directors' remuneration and related party transactions. However, the key is the nature of the disclosure - what is required to be disclosed and by whom - rather than a blanket call for more information.

The concessional taxation treatment enjoyed by almost all respondents and the reliance on donations from the public, mean that even very small NFPs and those that are primarily member serving, should have a requirement to make some public disclosure. Any disclosure in addition to such a 'minimum requirement' needs to be carefully targeted and proportionate to risk - both to the risk of abuse and also to the risk of damage to public confidence. In general, this means that regulation of small organisations, where the sums of money involved are modest, should be lighter than regulation of large organisations, which handle large sums and may also have a disproportionate impact on public confidence. With this principle in mind, the Report recommends a distinction between large and small NFP companies in determining what ought to be disclosed to ASIC. Small business gained concession several years ago, and it is now time for the NFP sector to demand some attention to their special needs.

### **Recommendation 6: Reform of Corporations Act disclosure requirements**

The current disclosure obligations required by the Corporations Act 2001 (Cth) (in particular the requirement for audited accounts by small NFP companies limited by guarantee) do not achieve the appropriate balance between legitimate public and stakeholder interest in disclosure, on the one hand, and the relative cost to the size of the organisation, on the other. A sliding scale of disclosure requirements based on size should be developed for NFP organisations, and be tailored specifically to the needs of stakeholders. There should be a minimum disclosure standard required of all NFP organisations, regardless of size, and this should include:

- summary or concise financial statement, based on an NFP specific accounting standard
- a description of the activities that have been carried out, and how they meet the objects of the organisation
- disclosure of whether or not directors have received remuneration.

For larger organisations, further information should be supplied. This could include:

- audited accounts
- disclosure of the amount (and possibly sources) of public funding.

Small organisations might be defined as organisations whose annual income or total annual expenditure is less than \$100,000. However, further consideration needs to be given to the criteria for determining size. ASIC, or a certain percentage of members, should have the residual power to require any organisation to be audited.

*Report Reference: Chapter 8, Disclosure*

There have been several calls for an NFP sector-specific accounting standard (for example, 1995 Industry Commission Report on Charitable Organisations in Australia, 2001 Charity Definition Inquiry Report, and 2003 Chartered Accountants of Australia Review of Not-for-Profit Financial and Annual Reporting).

Interestingly, the majority of survey respondents (56%) were in favour of lodging only 'summary financial information' whereas the current requirement for companies limited by guarantee is for audited accounts. However, if the obligations regarding financial reports were tailored to meet the needs of NFPs, their members, donors and other stakeholders, then a requirement to lodge them under the Corporations Act should not be regarded as too onerous. In any event, the burden on organisations would be justified by the public benefit.

### **Recommendation 7: Introduce a NFP-specific Accounting Standard**

The 1995 Industry Commission's recommendation that the Australian Accounting Standards Board and Public Sector Accounting Standards Board develop suitable accounting standards for NFP organisations, should be implemented. Consideration should be given to elements from which it would be appropriate to exempt small organisations.

*Report Reference: Chapter 8, Disclosure*

The 1995 Industry Commission Report on Charitable Organisations identified the following problems with the current system of accountability by NFP organisations:

- lack of consistent data collection processes
- lack of public access to information
- lack of standardisation of financial reporting and other information.

Almost a decade later, these are still key issues. It needs to be a proactive, Federal and State 'whole of government' approach and it needs to occur before there is any particular need to 'react'.

### **Recommendation 8: Review overall NFP disclosure obligations**

The survey data demonstrates that a review of the overall reporting obligations for NFP organisations is required. The data shows that current disclosure requirements:

- are not well tailored to the needs of the NFP sector and its stakeholders
- entail considerable duplication
- have an overall load that is too onerous for most small NFP organisations.

The current reporting requirements for fundraising are State-based, irregular and often duplicate the taxation and corporations law requirements. This duplication places an unnecessary administrative burden on NFP organisations, which often rely on volunteer labour. The reporting obligations under various Acts - including the Corporations Act 2001 (Cth) and various State Fundraising and Collection Acts - should be unified. Multiple filings should be avoided and low-cost, online searching facilities should be available so as to maximise transparency. It is desirable that the reporting obligations should, as much as possible, constitute a 'one-stop' report that would satisfy the needs of various bodies.

A review of NFP disclosure requirements should include consultation with the NFP sector and their stakeholders. The review will also need to have regard to the sometimes competing concerns of a range of organisations such as funding bodies, the Australian Taxation Office, State departments administering the Fundraising/Collection Acts and peak accountant bodies, with a view to minimising the current duplication of disclosure obligations.

*Report Reference: Chapter 8, Disclosure*

## Summary of Recommendations

There is no standardisation of reports or accounting standards that allows potential or recurrent donors, members or other stakeholders to easily compare similar NFP organisations. This information would also be useful to the NFP organisations themselves, as they examine their management practices and benchmark against other NFPs. Standardised reports would assist policy makers to examine where money has been spent and what kinds of programs have been run. This would help them track the kinds of overall effects these programs have had. It would be a useful addition to the current data that is available to (and from) the Australian Bureau of Statistics. It would be an important first step in any longitudinal study of the effectiveness of the programs of NFPs. On the other hand, there are important reasons to be cautious about the introduction of standardised reports and these are discussed in Chapter 8, Disclosure (see headings 5.9.3 and 5.12.3).

### **Issue for further deliberation: Standard Information Return**

Consideration should be given to the desirability of developing a Standard Information Return, similar to the Annual Return proposed by the NZ Working Party on Registration, Reporting and Monitoring of Charities (see Appendix 4).

Consideration should be given to whether organisations should be asked to disclose their main purposes and activities. Matters for disclosure might include the number of years the activity has been carried out, in what geographical areas, and how those activities furthered the objects of the organisation. The Return might also include questions about how accountability to stakeholders is achieved.

*Report Reference: Chapter 8, Disclosure*

Unlike non-executive directors of 'for-profit' companies, it is not common practice for non-executive directors of NFP organisations to receive remuneration, or other benefits. Only 8% of respondents said that directors were remunerated. Disclosure in the case of directors that are remunerated is important. Stakeholders (members, donors and creditors, in particular) have an obvious interest in knowing if non-executive directors are paid, and if senior management are paid more than the market demands for managers of NFPs. Information about the remuneration of senior management may also be desirable.

The rules regarding disclosure of related party transactions (as contained in Chapter 2E of the Corporations Act 2001 (Cth)) are applied differently to companies limited by guarantee depending upon whether or not they hold a name licence. Those that hold a licence to omit the word 'limited' from their name (a name licence) are not bound to comply with the related party transaction provisions. Those that do not hold a name licence, are subject to the provisions affecting related party transactions. For all companies (name licence, no name licence, limited by guarantee or proprietary), excessive remuneration may constitute oppressive or unfair conduct under Part 2F.1 of the Corporations Act and/or a breach of directors' duties. Inconsistency in the application of the related party transaction provisions does not seem desirable. There does not appear to be any sound policy reason why a sub-group of NFP companies should be exempt from reporting, and gaining member approval, for example when a relative of a director is going to receive a payment that is in excess of what can be regarded as 'reasonable remuneration'. It also seems desirable that organisations should report payments to trustees or Board members of NFPs, by related parties.

### **Issue for further deliberation: Disclosure of payments to directors**

Where directors, trustees or committee members or related parties (that is, relations or associates) receive benefits of any kind (including salaries, fees, honoraria, and in-kind compensation), these should be publicly disclosed. Consideration should be given to the application of Chapter 2E of the Corporations Act 2001 (Cth) (related party transactions), or possibly new conflict of interest type-provisions, to all NFP companies. That is, removing the existing exemption for companies limited by guarantee that hold a licence to omit the word 'limited' from their name. This would be in addition to finding the most effective way of ensuring that all NFP organisations disclose remuneration of directors and officers.

*Report Reference: Chapter 8, Disclosure; Chapter 5, Board Size, Composition, Remuneration and Experience*

Only 24% of survey respondents thought 'marketing expenditure compared with fundraising receipts' should be disclosed, although there were some interesting variations between respondents based on size and principal activity. There is currently no requirement under the Corporations Act to disclose this information and there is considerable inconsistency between the Fundraising and Collection Acts of the States and Territories. While there does not seem any great degree of support from across the sector to make this information publicly available, it is being increasingly demanded by the public and grant makers. There are, however, a number of problems in attempting to compare fundraising costs. These costs can vary widely, largely due to factors beyond the organisation's control, such as the popularity of the cause.

#### Issue for further deliberation: Fundraising accounting standards

Further consideration should be given to the way revenue from fundraising, gifts, memberships, dues and association fees, and the sale of goods and services, is disclosed. This is in addition to disclosure of moneys spent on administration, advertising, promotion and the like. This matter requires further consideration by the Australian Accounting Standards Board, as comparability between organisations is a vexed issue. Consideration should be given to including an estimate of the number of volunteer hours donated to the organisation, because the donation of time and labour is an important and unique aspect of the NFP sector.

Report Reference: Chapter 8, Disclosure

## 4. STAKEHOLDERS

The survey findings showed that, as expected, there are a greater *number* of stakeholders in NFP companies than in 'for-profit' companies. The data also provides some surprising insights into the *types* of stakeholders that those working in NFP organisations identify as their principal stakeholders. Both the number and the type of stakeholders relevant to NFP organisations are (in the words of one respondent) 'alien' to the reporting requirements of the *Corporations Act 2001* (Cth). But there are wider implications. The data on stakeholders highlights a fundamental difference between NFP organisations and 'for-profit' companies. The primary reason that NFP and 'for-profit' stakeholders differ is because the objects or mission of the organisation differ. NFP organisations are generally established with the object or mission of serving the interests of certain stakeholders, whether they are the members of a club or the clients of a welfare organisation. Any consideration of NFP accountability must include an assessment of the extent to which the NFP objects or mission have been met.

It is necessary to provide remedies for members in an NFP organisation as an accountability mechanism so that they can ensure that the organisation continues to pursue its mission. However, a fine balance needs to be achieved. The range of accountability mechanisms are more limited in NFP organisations than in 'for-profit' companies, particularly in large listed companies where additional mechanisms are in force. In contrast, the financial resources of an NFP organisation are often limited. It is not in the public good for these limited resources to be expended defending vexatious legal actions by members. These issues are discussed in Chapter 7, Stakeholders.

### Recommendation 9: Reform of members' remedies

The special position of members in NFP companies should be considered further in the context of remedies. Members of NFP organisations do not have the same economic power as members of 'for-profit' companies. Nor do they have recourse to a range of shareholder remedies such as selling their shares. Thus members' ability to constrain the actions of Board members and officers of the company, or to ensure that action is taken following a breach of the constitution, is limited. In addition, one of the unique characteristics of NFP organisations is the range of stakeholders with a legitimate interest in the organisation. The public, donors, clients and volunteers all have special stakes in ensuring that the mission of the NFP organisation is pursued and that the organisation's funds are not distributed to members.

The consequences of a breach of NFP objects should be reconsidered, as their mission is what drives NFP organisations. In this regard we suggest that the following specific reforms be considered:

- All NFP companies should be required to have a 'non-distribution' clause.
- Objects clauses should be compulsory for all NFP companies (not just those holding a licence to omit the word 'limited' from their name).
- The directors should have a specific duty to ensure that the company pursues these objects.
- A breach of the objects clause should be an express ground for bringing an action under s 232 of the *Corporations Act 2001* (Cth) (the oppression remedy) and, possibly, also under s 236 (the statutory derivative action). Modification of s 232 in this way would also enable ASIC to initiate action under s 234 on the basis of a complaint by a member or other stakeholder, for example, if it were considered to be in the public interest.

*Report Reference: Chapter 7, Stakeholders*

Given that the nature of tension and disputes between stakeholders in NFP organisations is often different to those experienced in 'for-profits', the need for access to low-cost alternative dispute resolution procedures such as mediation is important. It is also a practical way of increasing access and preventing limited resources being used to resolve disputes with stakeholders such as members.

### Recommendation 10: Other remedies

It is desirable that NFP organisations and their members have access to expert, low-cost alternative dispute-resolution procedures. This is a valuable role that could be undertaken by the independent NFP advisory body recommended in this Report (see recommendation 3).

*Report Reference: Chapter 7, Stakeholders*

## 5. BOARDS

In Chapters 5 and 6 there is considerable data about Board size, composition (for example, gender, age, executive/non-executive split), remuneration, skills and experience, structure (for example, the existence of a smaller management group within the Board), meeting procedures (for example, frequency and use of technology) and organisational role. Overall results are reported as well as any significant differences between respondents based on key factors such as size, member-serving vs public-serving, tax status and principal activity.

The data shows that the average NFP company Board size is 8 directors. However, further analysis shows that, particularly for large organisations, the Board can be quite large (10 or more directors). Sometimes there may be very good reasons for a larger Board and the typical 'Top 100', 'for-profit' company model should not be assumed to be the best model for NFP organisations. However, NFP organisations need to be mindful of this issue especially in the light of the legal duties and liabilities that all directors face.

**Recommendation 11: Board size**

As a 'best practice' guideline, Boards need to periodically review their size to make sure they are small enough to work effectively as a group, but large enough to contain an appropriate mix of skills and perspectives. While there is no ideal size for Boards, it is unlikely that very large Boards work effectively or efficiently. One popular method among NFP organisations for dealing with the problem is the establishment of a smaller management group. However, this option can be problematic. Directors who are insufficiently involved and informed expose themselves to potential risks under their liabilities as a director. NFP organisations with very large Boards need to consider whether there are more effective ways of involving stakeholders in the organisation. Options such as involving experts or stakeholders as specialist advisors on an advisory panel might usefully be explored by such Boards. This is an issue that it would be appropriate for the independent NFP advisory body recommended in this Report (see recommendation 3) to develop.

*Report Reference: Chapter 5, Board Size, Composition and Experience*

The survey shows that the vast majority of NFP company Boards comprise a majority of non-executive directors. Thus, at least in theory, they are likely to be more independent and objective monitors of managerial behaviour. Indeed, NFP companies fared better overall than the 'Top 100' listed companies in this respect.

Although NFP Boards might be independent of management, NFP bodies might still consider how they can actively increase the pool of potential directors. Our study shows that it is often difficult for NFP companies, especially smaller ones, to recruit Board members. Further, the profile of NFP directors is quite narrow. Younger people, women and people from non-English speaking backgrounds are under-represented on Boards, despite the important contribution they might potentially make to NFP bodies. The pool of potential Board members might be widened by advertising and other recruitment methods.

Periodic assessment of whether the Board is constituted so as to provide the right balance of expertise and skills is important. To this end, Boards need to consider whether the current appointment process leads to the right mix of skills, experience and perspectives. It may be possible, and indeed desirable, to foster the skills of other volunteers so they have the skills and confidence to serve effectively on the Board. Alternatively, co-option or other methods can be used to fill gaps in terms of skill or experience on the Board

**Recommendation 12: Board recruitment methods**

There is a demonstrated need for training materials and other assistance for NFP Boards in their recruitment of Board members, as well as an ongoing assessment of the directors' mix of skills, experience and perspective. In general, NFP company Boards are currently composed of people from a narrow demographic. Many NFP organisations could benefit from the broader range of the skills and experience that are available in the general community. Assistance with this issue would be a useful role for the NFP advisory body recommended in this Report (see recommendation 3).

*Report Reference: Chapter 5, Board Size, Composition and Experience*

The data shows that many Board characteristics vary with the size of the organisation. For example, the size and complexity of the structure of the Board tends to increase with organisational size, and so does the support available for Board members. For example, only 60% of small organisations provide new directors with strategic and business plans compared with 84% of large organisations.

**Recommendation 13: Board training**

Support for Board members with training and induction is required. Smaller NFP organisations, in particular, should be targeted as they do not receive the same level of introductory material and training as their larger cousins. Consideration should be given to reaching and assisting the Boards of small NFP organisations. This is an area that would benefit from the advisory and training body recommended in this Report (see recommendation 3).

*Report Reference: Chapter 6, Board Structure, Procedures and Role*

# CHAPTER 1: PROJECT OVERVIEW

## SUMMARY OF THIS CHAPTER

- The Project has been conducted by members of the Centre for Corporate Law and Securities regulation at The University of Melbourne. It has been funded over the three-year period by an Australian Research Council grant and has received in-kind support from Philanthropy Australia Inc.

### Project aims

- The key project aims have been to:
  - s Obtain a national profile snapshot of NFP companies limited by guarantee for the first time.
  - s Obtain the views of those working in the NFP sector.
  - s Identify what is working in the current regulatory regime and what is not. For example: Is a company limited by guarantee the most appropriate legal structure? What type of information should be disclosed and to whom? Who is the most appropriate regulator for NFP organisations?
  - s Make law reform recommendations and engender further debate.
- The principal method of data collection has been a detailed written survey. A questionnaire was sent to the Chief Executive Officer of all registered companies limited by guarantee as appeared on the public register at 1 March 2002. A good response rate (estimated to be 39%) was achieved.

### Purpose of this Report

- The main purpose of this Report has been to make recommendations for reform and to identify areas requiring further deliberation. An important feature has been to record the results of the survey comprehensively so that we, and others, can use it for future research. We hope that in this way the data will form a useful snapshot of the NFP companies that can be referred to and used for a variety of purposes by policy makers and the NFP sector itself. More detailed analysis of particular issues has or will be covered in articles published elsewhere (and, in some instances, reproduced on the Project website), or taken up in future projects.
- In addition to this Report, the Project website has other materials that might interest those working in the NFP sector, policy makers and those providing advice to NFP companies, see <http://cclsr.law.unimelb.edu.au/activities/not-for-profit/>.

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### 1. PROJECT BACKGROUND

The 'Accountability and Corporate Governance of Not-for-Profit Companies Project' (the Project) was conducted from March 2001 to December 2003. The earliest genesis of the Project was years spent teaching students about a company law regime that did not seem to fit the not-for-profit (NFP)<sup>1</sup> context. For example, dividends and reductions of share capital are concepts with no relevance to a company formed to meet the needs of a NFP organisation. Experience on NFP Boards, as well as anecdotal evidence, also informed us of problems with the complexity of legal structures and disclosure requirements. These cause considerable difficulties for those working in the NFP sector. There is evidence suggesting that the number of NFP companies is increasing gradually, however, NFP companies still represent a small proportion of all registered companies.<sup>2</sup> This fact, combined with the absence of a strong sector lobby group, means that the particular needs of NFP companies have often been overlooked.<sup>3</sup>

In this Project we have used both our considerable corporate law expertise, and our combined academic and personal experience in the NFP sector (see Appendix 3). The experience and profile of our collaborative partner, Philanthropy Australia (see Heading 3) has also significantly benefited the Project. The results should be of particular interest to policy makers concerned with corporate governance and accountability in the NFP sector.

The Project has been funded for the three-year period by an Australian Research Council (Department of Education, Training and Youth Affairs) grant under the Council's 'Strategic Partnerships with Industry - Research and Training Scheme' (SPIRT Grant). Our industry partner, Philanthropy Australia, has provided in-kind support during this period.

### 2. RESEARCH TEAM

The chief investigators have been Ms Susan Woodward and Professor Ian Ramsay from the Centre for Corporate Law and Securities Regulation (CCLSR) at The University of Melbourne. Research assistance has been provided by Ms Shelley Marshall (from January 2003 to September 2003).

Other people have been involved in a variety of capacities during the course of the Project: Mrs Sally Sievers (member CCLSR) provided specialist input at various times; data entry (in relation to the survey) was undertaken by Mr David Rose; Mr Bruce Smyth and Mr Malcolm Anderson have, from time to time, provided expert statistical advice and analysis; Mr Michael O'Neill provided research assistance May 2001–December 2002; some administration assistance was provided by Ms Amy Kirwan, Ms Jacqui Zaleberg and Ms Eleanor Jackson; and Ms Rhonda Black has provided editorial assistance with this Report. Brief profiles are provided in Appendix 3 for Ms Woodward, Professor Ramsay, Ms Marshall and Mrs Sievers.

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<sup>1</sup> We have used the term 'not-for-profit' to cover the broad range of organisations operating for social or community purposes, such as those providing charity, recreation, advocacy, art or religion. The main characteristic of such organisations is that funds or profits are used by the organisation solely to further its social/public purpose, rather than being distributed to members or officers (known as the non-distribution constraint). The term is intended to be much broader than the traditional, legal definition of a 'charity'. The term 'not-for-profit' has been preferred to 'non-profit' because it more explicitly recognises that these organisations, and indeed the sector, often make (substantial) profits, even though they are not distributed to members. The independent Charities Definition Inquiry recommended the use of the term 'not-for-profit' for similar reasons (*Report of the Inquiry into the Definition of Charities and Related Organisations*, 2001, pp. 91–6). One person who provided feedback on the Summary of Preliminary Findings (March 2003) suggested that the term 'not-for-distribution' would be a more accurate term but, although we think there is merit in the suggestion, we have used the more widely used term 'not-for-profit'.

<sup>2</sup> On the basis of figures provided to us by ASIC, from 1 March 2002–1 March 2003, there were an additional 197 companies limited by guarantee registered by ASIC. However, there are over a million proprietary companies limited by shares compared with just over 10,000 companies limited by guarantee.

<sup>3</sup> See S. Woodward, 'Not-for-Profit Companies - Some Implications of Recent Corporate Law Reforms', 1999, 17 *C&SLJ* 390; and M. McGregor-Lowndes, 'Regulatory Infrastructure for Nonprofit Organisations', Working Paper No. PONC 97, August 2000, Queensland University of Technology. The formation in June 2002 of a National Nonprofit Round Table (initially called the 'Third Sector Round Table') may mean that in future there is a sector group able to represent the needs of NFP companies in the way that organisations like the Business Council of Australia represents 'for-profit' interests: 'Non-Profit Groups Link up to Present United Front', *Financial Review*, 26 June 2002, p. 11 and E. Cham, National Director Philanthropy Australia Inc, 'A New Focus for Australia's Non-Profits', 2002, 50 *Australian Philanthropy Journal* 3.

This Report has been written by Ms Woodward and Ms Marshall. This Report includes material available as at 31 August, 2003, unless otherwise expressly stated.

### 3. COLLABORATIVE PARTNER: PHILANTHROPY AUSTRALIA

Philanthropy Australia has, as our 'industry partner', provided valuable in-kind support for the Project. Philanthropy Australia is the national membership organisation for grant-making trusts and foundations. Its mission is to promote and protect the interests of family, private, corporate and community giving in Australia. Its members have an overarching interest and concern to ensure that grants made by them are distributed to well-managed NFP organisations. Philanthropy Australia has also been instrumental in the formation of the National Nonprofit Round Table - a new group whose primary focus will be to represent the NFP sector to government and the broader community. See <http://www.philanthropy.org.au/>.

### 4. PROJECT AIMS

Put simply, the key aims of the Project have been to:

- Obtain national baseline data on NFP companies limited by guarantee for the first time.
- Obtain the views of those in the NFP sector, particularly those working in NFP companies.
- Identify what is working in the current regulatory regime and what is not. For example, is a company limited by guarantee the most appropriate legal structure? What type of information should be disclosed and to whom? Who is the most appropriate regulator for NFP organisations?
- Make law reform recommendations and engender further debate.

### 5. IMPORTANCE OF THE SECTOR

Official estimates suggest that NFP institutions contribute almost \$21 billion or 3.3% of Gross Domestic Product (GDP) in 1999 to 2000. When imputed wages for volunteer services are included, the contribution of NFP institutions increases to 4.7% of GDP. They also make a significant contribution to employment, accounting for 6.8% of total employment in 1999 to 2000. In comparative terms, NFP institutions add more to GDP than the mining industry. Even without an imputation for volunteer services, the NFP sector is larger than both the communications sector and utilities sectors.<sup>4</sup> Given its size and the nature of the many services it provides, it is clear that a strong NFP sector is vital for Australia's long-term economic prosperity. Increasingly the sector's importance is being recognised worldwide, but in Australia there has been only limited research into NFP companies.<sup>5</sup>

<sup>4</sup> See 'Non-profit Institutions Satellite Account', ABS Cat. No. 5256.0 released 28 November 2002. See also earlier figures from the Australian Nonprofit Data Project (a collaborative project between the Centre for Australian Community Organisations and Management (University of Technology (Sydney) and the Australian Bureau of Statistics) as reported in M. Lyons & S. Hocking, *Dimensions of Australia's Third Sector - Report of the Australian Nonprofit Data Project*, Centre for Australian Community Organisations and Management (CACOM) University of Technology, Sydney, 2000, especially p. 81.

<sup>5</sup> For earlier Australian studies see C. McDonald, *Board Members' Involvement in Nonprofit Governance* Working Paper No. 16, Program on Nonprofit Corporations, Queensland University of Technology, 1993 (Qld); J. Radbourne, *Recruitment and Training of Board Members for the 90's and Beyond*, Working Paper No. 24, Program on Nonprofit Corporations, Queensland University of Technology, 1993, and P. Steane and M. Christie, 'Nonprofit Boards in Australia: A Distinctive Governance Approach', 2001, 9 *Corporate Governance* 48.

## 6. SOME LEGAL ISSUES AFFECTING NFP ORGANISATIONS

An outline of the main legal issues that were considered by the Project follows:

### 6.1. Myriad of possible legal structures

The legal nature of NFP organisations is even more varied than in the ‘for-profit’ sector. This complexity has important implications for accountability, governance and regulation of the NFP sector.

Many, particularly smaller organisations, are incorporated under State-based associations legislation<sup>6</sup> - an option not available to ‘for-profit’ organisations. By contrast, many of the large welfare organisations are church-sponsored and have no clearly defined identity of their own. They receive their legal status by Acts of Parliament that allow their sponsoring denomination to hold property. In order to determine the exact legal nature of each organisation within a church’s umbrella, it is often necessary to work through a complex (and largely confidential) combination of legislation, trusts, incorporated associations and companies.<sup>7</sup> It is not even possible to identify the total number of NFP companies in Australia. The Australian Securities and Investments Commission’s (ASIC) records do not separately identify this group. Neither the Australian Nonprofit Data Project<sup>8</sup> nor the recently released ABS Satellite Accounts<sup>9</sup> distinguish the number of NFP companies from other forms of organisation. However, it seems their number is on the increase, if only very gradually.<sup>10</sup>

First, the Industry Commission (now known as the Productivity Commission) in its report *Charitable Organisations in Australia* noted a trend towards the use of companies limited by guarantee as the preferred legal structure for newer organisations, even for those within the church-sponsored group.<sup>11</sup>

Second, several of the State Associations Incorporation Acts have given the Registrars of incorporated associations power to direct associations incorporated under their Act to instead register as companies limited by guarantee under the *Corporations Act*.<sup>12</sup> In Victoria at least, many associations have received such a direction.<sup>13</sup>

Third, there are a variety of legislative provisions which effectively require certain NFP organisations to incorporate as companies, either to obtain grants or for licensing. For example, the *Aged Care Act 1997* (Cth),<sup>14</sup> the *Aged or Disabled Persons Care Act 1954* (Cth)<sup>15</sup> and the *Registered Clubs Act 1976* (NSW).<sup>16</sup>

Last, in addition to companies registered as companies limited by *guarantee*, there is a significant group of other companies (that is, companies limited by *shares*) that also fall within the general term, NFP companies. For example, it is increasingly common to find NFP organisations with

<sup>6</sup> For example, *Associations Incorporation Act 1984* (NSW) and *Associations Incorporation Act 1981* (Vic).

<sup>7</sup> See Industry Commission 1995, *Charitable Organisations in Australia*, Report No. 45, AGPS, 1995, Appendix C, pp. 10–13, 16–17 and 204. A general insight into the relative distribution of organisations by form of legal entity was given by the Industry Commission in this report: see p. 17 and Appendices C and D. See also Charity Definition Inquiry, *Report of the Inquiry into the Definition of Charities and Related Organisations*, 2001, available at <<http://www.cdi.gov.au>> p. 278.

<sup>8</sup> M. Lyons & S. Hocking, *Dimensions of Australia’s Third Sector - Report of the Australian Nonprofit Data Project*, Centre for Australian Community Organisations and Management (CACOM) University of Technology, Sydney, 2000, especially p. 81.

<sup>9</sup> See ABS ‘Non-profit Institutions Satellite Account’, ABS Cat. No. 5256.0 released 28 November 2002, Glossary p. 43.

<sup>10</sup> The growth in the number of incorporated associations is much greater. For example, in Queensland alone the average number of new incorporations is between 600 and 1000 per annum. See also n. 2.

<sup>11</sup> Industry Commission 1995, n. 7, Appendix C, p. C11.

<sup>12</sup> See A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand*, The Federation Press, 1996, pp. xvi, 100–1.

<sup>13</sup> The survey highlighted some examples. One respondent stated that the ‘GST pushed [an] earlier Incorporated Association “over the line”’: response no. 731. Another stated that the Victorian Government ‘was pushing larger incorporated associations from the state jurisdiction’: response no. 210. In New South Wales, the Department of Fair Trading advised one organisation that it was unable to be an incorporated association due to the scale of its turnover: response no. 185.

<sup>14</sup> Section 8(1).

<sup>15</sup> Section 7(3)(c).

<sup>16</sup> Section 10(1)(b).

trading offshoots. These offshoots are companies limited by shares that operate as ‘for-profit’ subsidiaries of the NFP, parent organisation.<sup>17</sup> However, as previously noted, ASIC statistics do not identify the number of NFP companies on the register, or whether they are companies limited by guarantee or companies limited by shares.

The myriad of legal structures for NFP organisations results in disclosure and other requirements differing for organisations that carry out the same type of activities. For example, a sporting association that is, for historical reasons, a company limited by guarantee, will have different legal requirements to meet than an equivalent organisation that has been established as an incorporated association. Thus, variation in the disclosure required will be based on this rather arbitrary distinction, rather than a more logical one, such as size.

## 6.2. Directors’ duties

The *Corporations Act* and the general law impose duties on directors and officers of all companies, regardless of whether they are NFP or ‘for-profit’ companies. It is clear (at least since the important decision of *Commonwealth Bank of Australia v Friedrich* (1991) 5 ACSR 115; 9 ACLC 946) that being an honorary director will not of itself be sufficient to exonerate a director from liability. In that case, J. Tadgell stated:

There is nothing in the Code [now *Corporations Act*] to suggest that the standard to be expected of a part-time non-executive director of a company not for profit is different from the standard expected of any other director of a profit-making company: both are required...to exercise a reasonable degree of care and diligence in the exercise of their powers and the discharge of their duties.<sup>18</sup>

One can easily appreciate the policy reasons for this approach. There should be a high degree of accountability for directors of NFP organisations receiving donations from the public and/or government funding (as was the situation in the *Friedrich’s case*).<sup>19</sup> Directors’ legal duties are one accountability mechanism. Indeed, their importance is arguably greater in the context of a NFP company because many of the other accountability mechanisms (for example, stock exchange regulation, dividends/returns to members and the influence of institutional investors) do not apply.<sup>20</sup>

## 6.3. Board selection

NFP companies may experience difficulty in attracting Board members on a *voluntary basis* who are both:

- people with the financial, legal and corporate management expertise required for the organisation to operate successfully in a competitive funding environment (that emphasises a corporate management framework and accountability standards); *and*
- people who have experience or skills with the service provided by the company; government and non-government grant makers often make it a condition of their grants that the recipient has ‘client’ or ‘consumer’ directors on its Board.

## 6.4. Multiple accountability

The voluntary nature of NFP Boards combined with their multiple and complex accountability foci (for example, their accountability to grant makers, members, clients and regulatory bodies), have been identified by several socio-legal academics as significant impediments to good corporate governance practices in NFP organisations.<sup>21</sup> It is common practice for Board members to be

<sup>17</sup> See also Charity Definition Inquiry, n 1, pp. 93–7.

<sup>18</sup> *Commonwealth Bank of Australia v Friedrich* (1991) 5 ACSR 115 at 197. Although the court was not prepared to use its discretionary powers under s 535 of the *Companies Code* (now s 1318 of the *Corporations Act 2001* (Cth)) to relieve the non-executive director in that case (Mr Eise) from liability, J. Tadgell did treat the voluntary nature of his position as a relevant factor.

<sup>19</sup> *Commonwealth Bank of Australia v Friedrich* (1991) 5 ACSR 115 at 198. See also M. McGregor-Lowndes, ‘Nonprofit Corporations – Reflections on Australia’s Largest Nonprofit Insolvency’, 1995, 5 *AJCL* 417.

<sup>20</sup> See D.A. DeMott, ‘Self Dealing Transactions in Nonprofit Corporations’, 1993, 59 *Brooklyn Law Review* 139.

<sup>21</sup> For example, D. Leat, ‘Voluntary Organizations and Accountability: Theory and Practice’ in H.K Anheier and W. Seibel (eds), *The Third Sector: Comparative Studies of Nonprofit Organizations*, Walter de Gruyter, New York, 1990. For a summary of the arguments see C. McDonald, ‘Board Members’ Involvement in Nonprofit Governance’, Working Paper No. 16, Program on Nonprofit Corporations, Queensland University of Technology, 1993. See also A. Twaits, ‘The Duties of Officers and Employees in Non-Profit Organisations’, 1998, 10 *Bond Law Review* 320.

recruited to maximise one particular type of focus, for example, to consumers. While that Board member may possess characteristics uniquely suited to maximising that focus, it has been argued that the capacity for NFP companies to recruit and retain Board members possessing the characteristics that address *all* types of accountability is severely limited.<sup>22</sup>

### 6.5. Conflicts of interest

Board members of NFP companies may be appointed as nominees for sectional interests. For example, they may believe their role is to represent a particular constituency and to influence the Board in their favour. Or, in the case of a peak body, they may be there with the view to representing a State or divisional group. Such nominee directors may find themselves in a position of conflict - a conflict between the interests/concerns of their nominators and their legal duties to act in the best interests of the company.

The statutory provisions are more onerous for public companies than private companies<sup>23</sup>. Bearing in mind that a company limited by guarantee is a public company,<sup>24</sup> the issue of compliance with these statutory provisions will be pertinent to NFP companies. However, the concerns of NFP companies may not be consistent because, even within the category of companies limited by guarantee, there is differential treatment. In particular, companies limited by guarantee and holding a licence to omit the word 'limited' from their name<sup>25</sup> (a name licence) are not bound to comply with the related party transaction provisions contained in Chapter 2E of the *Corporations Act 2001* (Cth).<sup>26</sup>

## 7. RESEARCH METHODOLOGY

### 7.1. Data collection

The principal method of data collection for the Project was a written survey. We considered this approach to be the most useful way to obtain a relatively accurate cross-sectional snapshot of NFP companies. This was an important factor given the paucity of even the most basic profile data on this group. The survey was also seen as an effective way of obtaining large-scale empirical evidence as to whether existing companies regulation is perceived by NFP companies (or at least the predominant group of them) as adequately meeting their needs. In particular, for structural suitability, disclosure and accountability. The written survey had the advantage of allowing respondents to remain anonymous. It was also relatively cost-effective and enabled data to be collected on a national basis. Other advantages (and the disadvantages) of this form of data collection are discussed more fully in Appendix 1.

In addition to the survey, feedback was obtained from a variety of sources. In March 2003, a Summary of Preliminary Findings<sup>27</sup> was distributed to all survey respondents who had indicated that they wanted to receive the results. The accompanying request for feedback on the initial recommendations for reform was met with an enthusiastic response, and a number of respondents emailed or wrote to us with their opinions concerning the Preliminary Findings.

The Summary of Preliminary Findings was also distributed widely to the media, the original trialists, relevant the government departments (for example, the Department of Family and Community Services, relevant Departments/Registrars for incorporated associations in each State/Territory, the Federal Treasurer) and other contacts. We obtained some media coverage<sup>28</sup> and this generated further feedback. Several presentations have been made to a variety of audiences (both academic and those working in the NFP sector).<sup>29</sup> This too provided an

<sup>22</sup> See C. McDonald, n. 21, p. 3.

<sup>23</sup> See, for example, *Corporations Act 2001* (Cth), s 194 (replaceable rule, proprietary companies) compared with s 195 (public companies) on the issue of a director voting on matters involving a material personal interest.

<sup>24</sup> See *Corporations Act 2001* (Cth), s 112(1).

<sup>25</sup> See *Corporations Act 2001* (Cth), ss 150–1.

<sup>26</sup> This follows from para. (b) of the definition of 'public company' contained in the *Corporations Act 2001* (Cth), s 9.

<sup>27</sup> A copy of this Summary is available on the Project website at <<http://cclsr.law.unimelb.edu.au/activities/not-for-profit/>>.

<sup>28</sup> ABC Radio National interview at 8.15am on 4 March 2003; 'Non-profits may get new rules', *The Age*, 28 February, 2003; 'Donors query executive pay', *Australian Financial Review*, 5 May 2003.

<sup>29</sup> Presentations by Ms Woodward include: *Building Better Boards A Dialogue for Nonprofit Organisations*, July, Sydney, organised by Nonprofit Governance & Management Centre (inaugural conference attended by more than 400 people); seminar for the Centre for Philanthropy and Nonprofit Studies at the University of Queensland, September 2002; *Doing Well*, bi-annual ANZTSR (Australian and New Zealand Third Sector Research Association) research conference, Auckland, November 2002 (conference paper published on conference website at <<http://www.uws.edu.au/ashs/anztsr/>>); Annual ACROD (National Industry Association for Disability Services) Conference, a conference for the Chief Executive Officers of their member organisations (approx 200 people) Canberra, 19 May 2003; seminar for the pro bono clients of Freehills, solicitors, Sydney, 17 June 2003; and

opportunity for useful feedback. On two occasions organisations with an interest in the Preliminary Findings recommendations gathered feedback from their constituents to inform their positions.<sup>30</sup> This feedback was subsequently provided to us and has helped inform the recommendations made in this Report.

## 7.2. Survey group

A questionnaire addressed to the Chief Executive Officer (CEO) was mailed to every company limited by guarantee (except those recorded as superannuation trustee companies and those under external administration). The survey/Project was also advertised widely within the sector. The questionnaire was divided into six main parts: (A) general company profile, (B) legal structure, (C) stakeholders, (D) Board composition and experience, (E) Board structure and procedures, and (F) regulatory framework. The confidential questionnaire, with a detachable covering letter, was posted on 13 March 2002 to the registered office of these companies recorded on the national register maintained by ASIC at 1 March 2002. A follow-up letter was sent on 11 April 2002. The total number of returns was 2089, of which 1736 were completed returns. A follow-up telephone survey of non-responders was conducted in August 2002. No markers of sample bias were found. Taking into account non-receipts, the response rate is estimated to be 39%. This was a very pleasing response given the length of the survey (ten pages),<sup>31</sup> the detailed knowledge of the organisation required to complete it, and the fact that the vast majority of NFP companies rely on volunteers. Having the imprimatur of The University of Melbourne and Philanthropy Australia, as well as the earlier advertising within the sector, seems to have contributed to the response rate.

There is a more detailed discussion of the research methodology in Appendix 1.

## 8. SIGNIFICANCE OF SURVEY RESULTS

The survey has netted important profile data: it is the first national, large-scale snapshot of the nature of this NFP companies. The data is important for three reasons:

- i. Since the company law simplification reforms,<sup>32</sup> ASIC does not have data on the nature of the business conducted etc. ASIC's records cannot tell us if all companies limited by guarantee are NFP organisations.
- ii. Previous NFP data collection exercises,<sup>33</sup> including large-scale ones such as the Australian Nonprofit Data Project,<sup>34</sup> have not distinguished the legal nature of the organisations.
- iii. An understanding of the nature of the group being regulated is essential prior to deciding how and by whom the group should be regulated.

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*Piercing it together – equity, empowerment & change*, ACOSS (Australian Council of Social Service) Annual Congress, Canberra 13 November, 2003.

<sup>30</sup> At the ACROD conference following the speech given by Ms Susan Woodward, note 29, ACROD asked participants to fill out a survey. A workshop was held at the Freehills seminar note 29, after Ms Woodward's presentation, during which participants discussed the recommendations made, and generated group views on their value for the sector.

<sup>31</sup> A copy of the survey form is contained in Appendix 3.

<sup>32</sup> *First Corporate Law Simplification Act 1995* (Cth) and *Company Law Review Act 1998* (Cth).

<sup>33</sup> For earlier Australian studies see C. McDonald, *Board Members' Involvement in Nonprofit Governance* Working Paper No. 16, Program on Nonprofit Corporations, Queensland University of Technology, 1993. (This was a study that involved the analysis of 242 questionnaires collected from 1218 NFP organisations registered under the *Collections Act 1966* (Qld), however, the legal nature of the organisations was not discussed); J. Radbourne, *Recruitment and Training of Board Members for the 90's and Beyond*, Working Paper No. 24, Program on Nonprofit Corporations, Queensland University of Technology, 1993, (a study that involved surveys, interviews and observations of Board meetings of thirteen Queensland arts organisations; the organisations 'were selected randomly and represented a variety of art forms and legal structures', p. 7); and P. Steane and M. Christie, n. 5 (a study that involved the analysis of one hundred and eighteen questionnaires collected from three hundred and fifty NFP organisations; again there was no distinction as to the legal nature of the organisations).

<sup>34</sup> Lyons & Hocking, n. 8.

While there have been extensive consultations with business groups about law reform proposals,<sup>35</sup> our survey can be regarded as the first real attempt to obtain the views of the NFP sector, and to identify any difficulties they may have in navigating the company law regulatory regime.

## 9. PURPOSE AND STRUCTURE OF REPORT

### 9.1. Purpose

Given the good response rate to the Project survey, we have been put in the enviable position of having rich and 'deep' data. For example, it has been possible for us to make both general observations about the profile of the respondents as well as being able to 'drill down' further. We have been able to see if there were variations based on company size, principal activity, tax status, receipt of government income, member vs. public-serving etc. Given the extent of our Project's funding, the 'downside' of such rich data is that this Report cannot go into the level of analysis that many of the sections warrant.

The main purpose of this Report has been to make recommendations for reform and to identify areas requiring further deliberation. Also important has been the comprehensive recording of the results of the survey so that we, and others, can use it for future research. We hope that the data will form a useful baseline that can be referred to and used for a variety of purposes. More detailed analysis of particular issues has or will be covered in articles, or taken up in future projects.

### 9.2. Structure

This Report is divided into eight chapters covering the different sections of the survey:

- introduction
- profile data
- regulatory framework
- legal structure
- Board size, composition, remuneration and experience
- Board structure, procedures and role
- stakeholder
- disclosure.

There is also a Summary of Recommendations and Appendices (containing further information about the methodology (Appendix 1), profiles of the research team members (Appendix 2), a copy of the survey form (Appendix 3) and standardised disclosure forms from the UK, NZ and Canada (Appendix 4) and a comparative table of the incorporated associations legislative regime (Appendix 5)).

Within each chapter, we have followed the pattern of:

- s stating the survey question
- s giving the basic results for that question (that is, overall frequencies)
- s reporting any statistically significant differences between the responses based on a range of key factors such as the respondent's principal activity, size, taxation status (PBI<sup>36</sup> or non-PBI), whether or not the company is primarily member serving or public serving, and whether or not the company receives any government funding
- s making observations on the results, where appropriate
- s making recommendations for law reform or indicating areas for further investigation in some instances.

There is a summary of key findings section at the beginning of each Chapter. We hope this enables readers to quickly identify which Chapters will be of interest to them and, within each Chapter, what they want to read in more detail.

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<sup>35</sup> For example, the Business Regulatory Advisory Group that has given input on reforms proposed as part of both the Simplification Program and the Corporate Law Economic Reform Program. This group is comprised of representatives of peak business (that is, 'for-profit') groups such as the Australian Institute of Company Directors, the Australian Stock Exchange and the Business Council of Australia. See also McGregor-Lowndes 'Regulatory Infrastructure for Nonprofit Organisations', n. 3.

<sup>36</sup> PBI means Public Benevolent Institution. This is a term used in the *Income Tax Assessment Act*.

## 10. OTHER PROJECT MATERIALS

In addition to this Report, the Project website provides other materials which may be of interest to the SFP sector and policy makers..

See <http://cclsr.law.unimelb.edu.au/activities/not-for-profit/>. One of the refereed journal articles can be downloaded in PDF format: *'Not-for-profit motivation in a for-profit company law regime —baseline data'* S Woodward (2003) 21 *Companies & Securities Law Journal* pp. 102–33. The *Law Reform Submission* to the NSW Department of Fair Trading in response to their Consultation Paper, 'Review of the Associations Incorporations Act NSW, S Woodward, S Sievers and S Marshall (June 2003) can also be downloaded in PDF format. The Project website was set up (within the Centre for Corporate Law and Securities Regulation, Law School, The University of Melbourne website) in March 2003 primarily as a location for the publication of the *Summary of Preliminary Findings*. This summary was directed mainly towards informing survey respondents who had indicated a desire to be notified about the results of the research. (These respondents were emailed with directions to the site or sent a copy by mail). Interest in the Project, up to 7 December 2003, has been shown by the Project's website title page receiving 3,456 hits.

## CHAPTER 2: PROFILE DATA

### *What does an NFP company look like?*

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#### SUMMARY OF KEY FINDINGS IN THIS CHAPTER

##### 'Typical' respondent

The typical respondent to the questionnaire was a CEO (59%) of a NFP company that:

- was member-serving as opposed to public-serving: 56%
- was income tax exempt but did not have tax deductibility status: 91% were income tax exempt; 48% had tax deductibility status
- did not hold a licence to omit the word 'Limited' from its name: only 25% said they held a name licence, 54% did not have such a licence and 21% responded 'don't know'
- was not part of a group structure: only 14% had subsidiary or related entities
- received no income from government sources: 59%
- relied on volunteers: 86% had at least one volunteer.

##### Size

- Respondents ranged from very small organisations (annual income of less than \$500) through to large NFP organisations (income of more than \$10 million and assets of more than \$10 million), with a good spread of all sizes.
- Seventy-two per cent of respondents had fewer than 20 employees, 62% had fewer than 20 volunteers and 60% had fewer than 100 members.
- There was no clear relationship between the number of employees and the number of members or volunteers. For example, a large membership base did not necessarily mean a large number of volunteers or employees.
- There was a strong correlation between the size of a respondents income, assets and liabilities. For example, the higher the income typically the greater the assets and the higher the liabilities.

##### Small or large?

- When the s 45A *Corporations Act 2001* (Cth) test was applied to the survey data, it showed that 88% of NFP companies in the sample would have been classified as 'small' for their last financial year. References elsewhere in this Report to small and large companies or organisations are based on this s 45A test.
- If the vast majority of NFP companies limited by guarantee chose to be proprietary companies they could, because of their size, avoid certain company law disclosure and other requirements. In particular, as small proprietary limited companies, they would not be required by the *Corporations Act 2001* (Cth) to have their accounts audited or to lodge them with ASIC.

##### Significance of profile data

- This profile data represents the first national, large-scale snapshot of the nature of NFP companies.
- In later Chapters, this profile data has been cross-tabulated with findings about stakeholders, disclosure and opinions about a new regulator. This was an attempt to discern whether any differences in opinion related to the profile of the organisation.
- This profile data highlighted significant differences between NFP companies and 'for-profits' (such as the high reliance on volunteers, taxation benefits and size). The way these differences need to be taken into account in deciding how best to regulate NFP organisations is developed in the following Chapters.

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## 1. INTRODUCTION

This Chapter outlines the profile data collected about the respondents in Part A of the survey which was titled 'General Company Particulars'.<sup>1</sup> This data confirmed that the companies were NFP organisations, and that they represented a fair spread of different types of NFP organisations - that is, not only small ones, and not deriving from one main activity group.

The profile data also provides necessary background to the subsequent Chapters. It has allowed us to distinguish between organisations based on their principal activity, size and primary purpose in our analysis of the legal structure chosen by NFP organisations, the discussion of their stakeholders, their Boards and their views concerning the regulatory framework. As will be seen in the subsequent Chapters, these distinctions are important when considering possible reforms to the laws regulating the NFP sector.

## 2. ARE THEY NFP ORGANISATIONS?

### 2.1. Survey question

- 1.1 Is the company a not-for-profit organisation? (Note: a not-for-profit organisation may make profits and have surplus funds, but its constitution prohibits the distribution of any profits to its members.)
- yes (please proceed with the rest of the questionnaire)
  - no (please complete question 1.2 only and then return the questionnaire in the enclosed reply paid envelope without completing the other remaining questions)

Number of respondents = 1736

- 1.2 If 'no', what is the company's principal activity? (please specify).....

Number of respondents = 48

### 2.2. Survey results

The survey asked the respondents to identify whether the company is a NFP organisation. It has generally been assumed that companies limited by guarantee are NFP organisations<sup>2</sup> because, without working capital, they are not suitable for commercial enterprises. The data confirmed that this assumption is largely correct. While some respondents (2%) were clearly confused about the legal status of their organisation,<sup>3</sup> the vast majority of respondents (98%) indicated that they were an NFP organisation. Forty-eight respondents (out of 1736) responded that they were 'for-profit' and therefore did not complete the rest of the questions. Despite the explanatory note and the nature of the main activity, it appears that many of these respondents were, in fact, NFP companies (that is, they thought that because they made a profit they were not an NFP organisation).<sup>4</sup>

The survey data in this Report is based on responses from 1688 NFP companies. Because not all respondents answered all questions (or all parts of every question), we have indicated the relative number of respondents next to each question.

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Note: All references in this Report to small and large organisations or companies are based on the definition of "small" and "large" (proprietary companies) as contained in s 45A of the *Corporations Act 2001* (Cth), unless detailed otherwise: see heading 8.5.1.

<sup>1</sup> A copy of the complete survey form is contained in Appendix 3.

<sup>2</sup> M. McGregor-Lowndes, 'Australia' in T. Silk (ed.), *Philanthropy and Law in Asia: A Comparative Study of the Non-Profit Legal Systems in Ten Asia Pacific Societies*, 1999.

<sup>3</sup> Out of n = 1688 NFP responses, about 26 seemed confused about their legal status.

<sup>4</sup> A NFP organisation may have a business arm and/or make profits and/or have surplus funds, but its constitution must prohibit distributions to members and these funds must instead be used to further its NFP objects.

### 3. PRINCIPAL ACTIVITY

#### 3.1. Survey question

- 1.3 If yes, please indicate the principal nature of the company's activities by ticking ONE of the following boxes and (where necessary) printing a description of the activity. (The classification of activities is based on that used in the Australian Nonprofit Data Project.)

*Number of respondents = 1646*

The questionnaire asked respondents to tick the (one) box<sup>5</sup> that best reflected the company's principal activity - forty-eight options were given based largely on the categories used by the Australian Nonprofit Data Project,<sup>6</sup> and modified as a result of comments from the trial group.

The questionnaire included twelve main category headings, with subheadings to further define the type of organisation. These categories were as follows:

- 1) Community services - these include some of the best known NFPs or charities, as well as very small community-based organisations and many organisations in between. The subcategories include:
  - a) child care
  - b) accommodation for the aged
  - c) disability services
  - d) youth services
  - e) other residential care
  - f) other non-residential care
  - g) specified other community service, that is, respondents were asked to name the type.
- 2) Health - the subcategories include:
  - a) not-for-profit private hospital
  - b) not-for-profit public hospital
  - c) nursing home
  - d) primary care service
  - e) specified health agencies, that is, respondents were asked to name the type.
- 3) Education - Lyons & Hocking estimate that 'nonprofit organisations educate about one third of Australian children'.<sup>7</sup> This category is divided into a number of subcategories which include:
  - a) preschool
  - b) school
  - c) university
  - d) specified other education, that is, respondents were asked to name the type.
- 4) Education-related - Lyons & Hocking<sup>8</sup> note that the education industry is served by or linked to several significant groups of NFP organisations; those engaging in research or in serving the needs of students and staff. The category includes:

<sup>5</sup> While the question asked for only one box to be ticked, some respondents ticked more than one box or no box at all. In this case, the rule adopted was to read ahead and where possible choose the most appropriate option. If this was not possible, the response was given a separate error code. After applying this rule, there were only 36 respondents for whom their principal activity was not classified.

<sup>6</sup> See Australian Nonprofit Data Project (a collaborative project between the Centre for Australian Community Organisations and Management [University of Technology (Sydney)] and the Australian Bureau of Statistics) as reported in M. Lyons & S. Hocking, *Dimensions of Australia's Third Sector - Report of the Australian Nonprofit Data Project*, Centre for Australian Community Organisations and Management (CACOM), University of Technology, Sydney, 2000.

<sup>7</sup> See n. 6, p. 32.

<sup>8</sup> See n. 6.

- a) research
  - b) parent association
  - c) university union.
- 5) Other human services - NFP organisations in this category seek to serve people who are disadvantaged. While many organisations in community services sector also provide several of these services, for the organisations included in this category, it is their main activity. This category includes:
- a) housing
  - b) community transport
  - c) employment service
  - d) specified other human services, that is, respondents were asked to name the type.
- 6) Religious organisations - Lyons & Hocking describe this category as organisations doing two things. They facilitate worship and control the content or belief and practices of the members of their particular religion.<sup>9</sup> Religious organisations predominantly carrying out community services are gathered under this category.
- 7) Philanthropic - this category includes:
- a) trustee of self-administered charitable trust
  - b) volunteer referral centre
  - c) fundraising intermediary
  - d) grant-making charitable trust of institution.
- 8) Arts and culture - this category includes:
- a) library, museum, art gallery
  - b) parks and gardens
  - c) performing arts
  - d) film and video production
  - e) radio and television
  - f) specified other arts or culture, that is, respondents were asked to name the type.
- 9) Sport and recreation - this category includes:
- a) sport
  - b) social club
  - c) specified other recreation/hobby, that is, respondents were asked to name the type.
- 10) Environment.
- 11) Interest group (including peak bodies) - this category includes:
- a) labour
  - b) peak body
  - c) business or professional
  - d) specified other interest group, that is, respondents were asked to name the type.
- 12) Other
- a) business services
  - b) accommodation (for example, youth hostel)
  - c) books and publishing
  - d) emergency services
  - e) not otherwise specified, that is, respondents asked to specify.

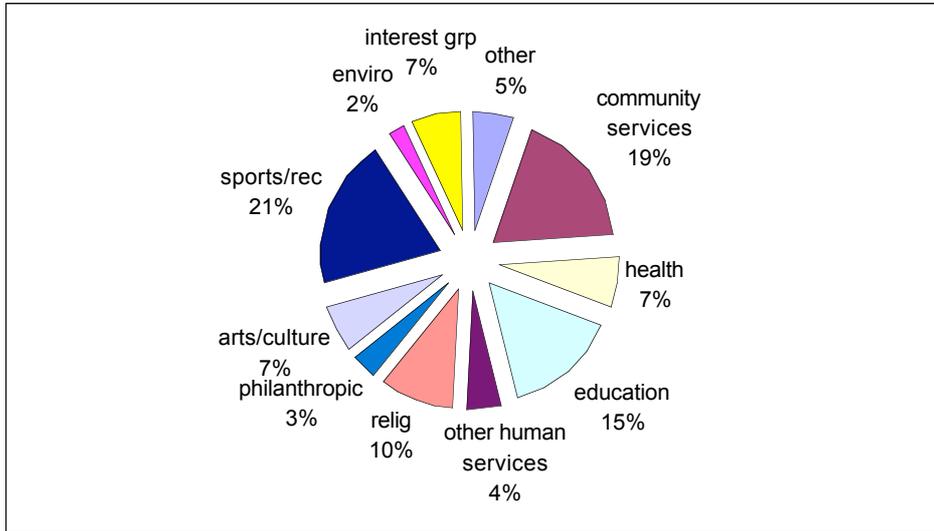
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<sup>9</sup> See n. 6.

### 3.2. Survey results

There was a good spread amongst the respondents for every one of the forty-eight options. The largest group of respondents were Sports and Recreation (21%), Community Services (19%) and Education and Education-Related (15%), followed by Religious (10%). There was a fairly even spread of other categories. Figure 1 shows the percentage of responses for each of the main categories.

Figure 1: Principal activity



A more detailed breakdown is shown in Table 1.

Table 1: Principal nature of company's activities

Type of organization	No.	%
<b>Community Services</b>		
child care	15	0.9
accommodation for the aged	42	2.5
disability services	73	4.3
youth services	23	1.4
other residential care	3	0.2
other non-residential care	3	0.2
other community service	126	7.5
<b>Health</b>		
NFP private hospital	7	0.4
NFP public hospital	7	0.4
nursing home	18	1.1
primary care service	11	0.7
health agency	54	3.2
<b>Education</b>		
pre-school	7	0.4
School	88	5.2
University	17	1
other education	100	5.9
<b>Education Related</b>		
Research	21	1.2

## Chapter 2 - Profile Data

<b>Type of organization</b>	<b>No.</b>	<b>%</b>
University union	5	0.3
parent association	3	0.2
<b>Other human services</b>		
housing	30	1.8
employment service	24	1.4
community transport	1	0.1
legal	5	0.3
other human service	10	0.6
<b>Religious organisation</b>	145	8.6
<b>Philanthropic</b>		
trustee of self-administered charitable trust	15	0.9
fundraising intermediary	12	0.7
grant making charitable trust or institution	22	1.3
<b>Arts and culture</b>		
library, museum, art gallery	28	1.7
parks and gardens	2	0.1
performing arts	40	2.4
film and video production	1	0.1
radio and TV	8	0.5
other arts or culture	26	1.5
<b>Sport and recreation</b>		
sport	237	14.1
social club	56	3.3
other recreation/hobby	30	1.8
environment	25	1.5
<b>Interest group</b>		
business or professional	45	2.7
peak body	49	2.9
other interest group	12	0.7
<b>Other</b>		
business services	60	3.6
accommodation	7	0.4
books and publishing	7	0.4
emergency services	7	0.4
not otherwise specified	121	7.2
indeterminate organisation	36	2.1

## 4. WHO DO THEY SERVE?

### 4.1. Survey question

- 1.4 Is the company's primary purpose to:
- serve its members and supporters
  - OR (please tick only one box)**
  - serve the public

Number of respondents = 1599

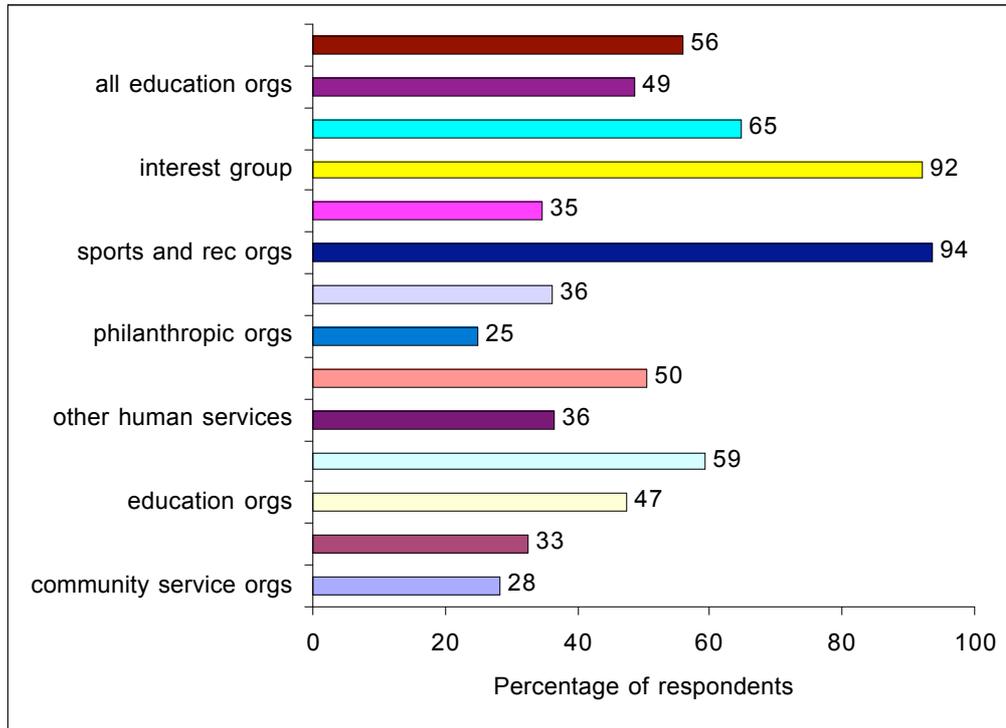
### 4.2. Survey results

An example of a member-serving organisation would be a sports club and a public-serving organisation would be a public hospital. More than half (56%) of NFP companies reported that their primary purpose was to serve their members. This information is relevant to a discussion about the information that should be available to the public and other stakeholders.<sup>10</sup>

### 4.3. Significant differences between respondents

Further analysis of this data was carried out comparing the principal activity of the organisation if the respondent said it was primarily member-serving. Figure 2 shows that the data follows the expected pattern, with Sports and Recreation and Interest Group organisations almost entirely member serving (93% and 92% respectively). The majority of Educated-Related organisations (60%) and Other groups (67%) also defined themselves as primarily member-serving.

**Figure 2: Primarily member-serving, based on principal activity**



<sup>10</sup> See Chapter 7, Stakeholders, and Chapter 8, Disclosure.

#### 4.4. Observation

This feature of NFP companies - that they serve members of the public - is one of the many characteristics that differentiates NFPs from 'for-profit' companies. Whilst 'for-profit' companies may serve their members (or shareholders), the relationship of NFP companies to their members is in many ways more complex. Members may also be clients, or clients may be an extra group that has an important stake in the company. This theme is explored in subsequent Chapters.

## 5. NAME LICENCES

### 5.1. Survey question

- 1.5 Does the company hold a licence to omit the word 'Limited' (or 'Ltd') from its name.
- yes
  - no
  - don't know

Number of respondents = 1638

### 5.2. Survey results

Under s 150 of the *Corporations Act 2001* (Cth), a company limited by guarantee can, subject to certain restrictions,<sup>11</sup> obtain a licence to omit the word 'Limited' from its name. Historically, a name licence was seen as important - it distinguished 'charities' from business. Without such a licence, the fear was that donations would dry up. To a very large extent, since the introduction of ACNs and ABNs,<sup>12</sup> this is no longer an important consideration.<sup>13</sup> The name licence group no longer comprise the majority of companies limited by guarantee. Twenty-five per cent said they held a name licence, 54% did not have such a licence and 21% 'didn't know'. The last figure is alarming as there is a significant penalty for failing to use the company's correct name on public documents - \$1,000 and/or three months' imprisonment.<sup>14</sup>

### 5.3. Significant differences between respondents

We examined the percentage of small and large companies saying they held a name licence. The definition of small and large is in accordance with s 45A of the *Corporations Act 2001* (Cth), and is not necessarily the best one to apply to NFP companies (see Heading 8).<sup>15</sup> It does, however, demonstrate a trend. The data shows that 49% of large companies have name licences, compared to only 29% of small companies.

<sup>11</sup> The restrictions state that the company's constitution (a) requires the company to pursue charitable purposes only and to apply its income in promoting those purposes; (b) prohibits the company making distributions to its members and paying fees to its directors; and (c) requires the directors to approve all other payments the company makes to directors.

<sup>12</sup> Australian Company Number and Australian Business Number.

<sup>13</sup> See M. McGregor-Lowndes & K. Levy, 'Name Licences: the Company Name You Have When You are Not Having a Commercial Company Name' 4 *Current Commercial Law* 12, 1996 and S. Woodward, 'Not-For-Profit Companies - Some Implications of Recent Corporate Law Reforms, 17 *C&SLJ* 390 at 393, 1999.

<sup>14</sup> If there is no name licence, *Corporations Act 2001* (Cth) s 148(6) makes it a strict liability offence not to include the word 'Limited' in a limited public company's name. See also *Corporations Act 2001* (Cth), Sch. 3, item 14.

<sup>15</sup> The *Corporations Act 2001* (Cth) s 45A(2) states: 'A proprietary company is a small proprietary company for a financial year if it satisfies at least 2 of the following paragraphs: (a) the consolidated gross operating revenue for the financial year of the company and the entities it controls (if any) is less than \$10 million; (b) the value of the consolidated gross assets at the end of the financial year of the company and the entities it controls (if any) is less than \$5 million; (c) the company and the entities it controls (if any) have fewer than 50 employees at the end of the financial year.'

## 6. TAX STATUS

### 6.1. Survey question

1.6 Is the majority of the company's income exempt from income tax?

- yes  
 no

*Number of respondents = 1651*

1.7 Are donations to the company (or any fund administered by the company) tax deductible?

- yes  
 no

*Number of respondents = 1616*

14.3.7 Is the company a 'Public Benevolent Institution? (PBI) for taxation purposes?'

- yes  
 no  
 don't know

*Number of respondents = 1631*

14.3.8 Is the company a 'charity' in the narrow, legal sense?

- yes  
 no  
 don't know

*Number of respondents = 1638*

### 6.2. Survey results

To profile the tax status of companies, several tax status markers were examined. Figure 3 combines answers to a series of questions on the company's taxation status.

Respondents were given a 'don't know' option for the last two of these questions which many chose (12% and 17% respectively). While some would argue that this significant 'don't know' group is not surprising given the complex taxation regime applying to NFP organisations, we found it disturbing that such a large number of respondents have no real understanding of their legal/taxation status.<sup>16</sup> In this regard, we note feedback on the results received from a senior officer of a well-respected NFP company who fears that these results represent 'a familiar attitude of we have a right to a tax break and we can do what we like'.

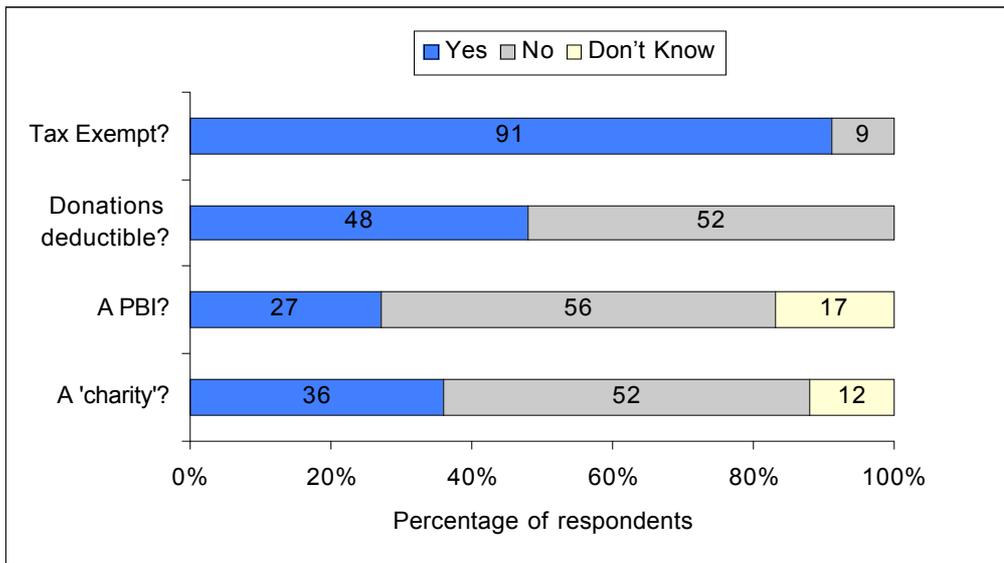
Of those aware of their taxation status, the majority of respondents were not 'charities' or PBIs<sup>17</sup>. While almost half (48%) enjoy tax deductibility status, the vast majority believe their income is tax exempt (91%). Again, this figure is relevant when considering what public-reporting obligations should exist for these organisations. If an organisation has (as a minimum) the privilege of income tax exemption, what should its corresponding disclosure/reporting obligation be, and to whom?<sup>18</sup>

<sup>16</sup> As well as confusion about taxation status, there were also 2% of respondents who were confused as to whether or not they were a company limited by guarantee (see Heading 2.2) and 21% who did not know whether they held a name licence or not (see Heading 5.2).

<sup>17</sup> Public Benevolent Institution is not a term defined in the *Income Assessment Act 1936* (Cth) but there is a substantial body of case law on its meaning. For a clear summary of the meaning of the term see Charity Definition Inquiry n. 6, Appendix B.

<sup>18</sup> See Chapter 8, Disclosure.

Figure 3: Tax status



### 6.3. Significant differences between respondents

Figure 4 shows that companies with PBI status are more likely to be exempt from income tax than those that do not (96% vs 89%), although the difference is not significant. Public-serving companies are more likely than member-serving companies to be exempt from income tax (94% vs 88%).

Figure 4: Majority of the company's income exempt from income tax, based on key indicators.

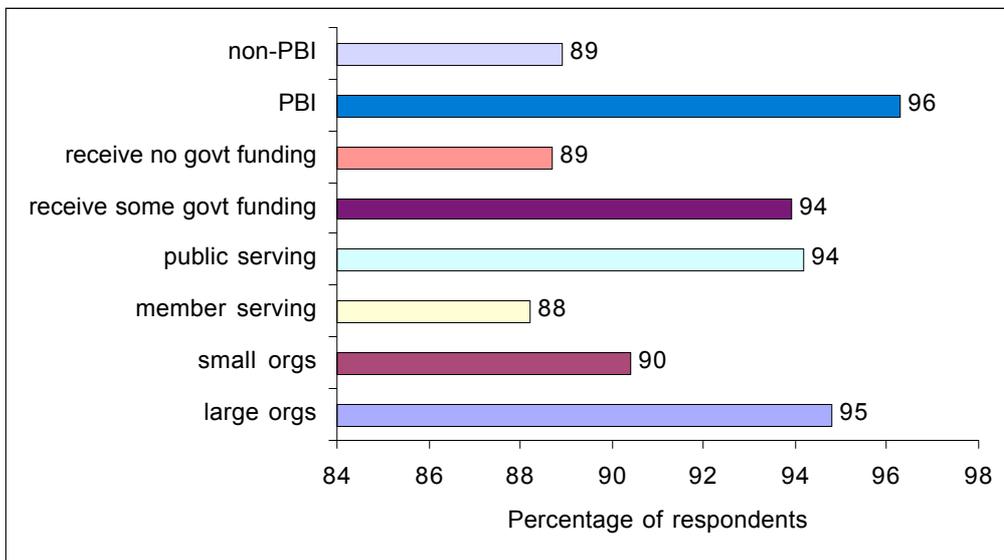
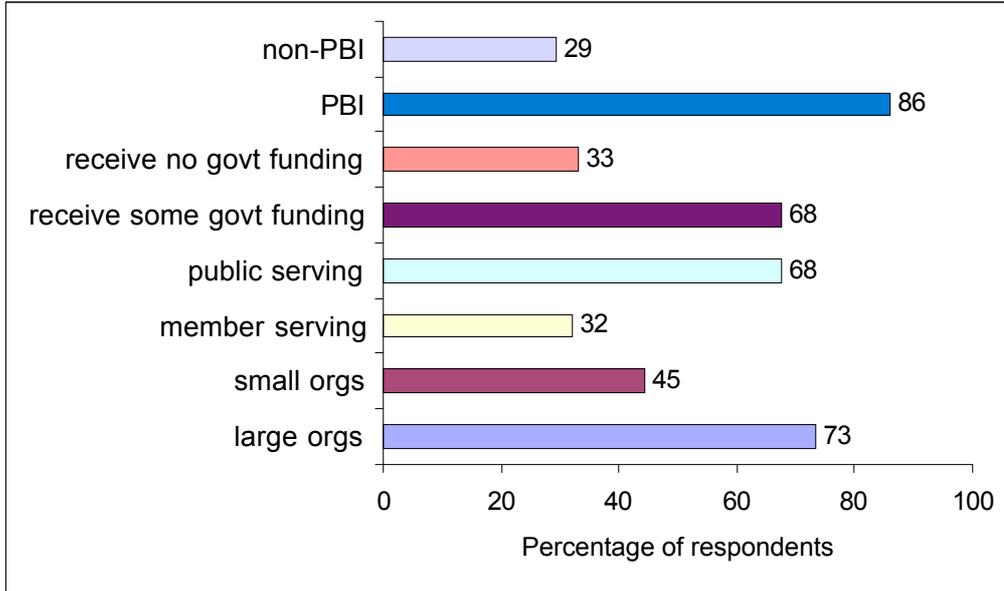


Figure 5 shows that companies with a PBI status are significantly more likely have tax deductible donations than those that do not (86% vs 29%), with a difference of 57%. Likewise, companies that are public-serving are far more likely than member-serving companies to have tax-deductible donations (68% vs 32%) - a difference of 37%. Companies receiving government funding are also much more likely than companies not receiving government funding to have tax deductibility on donations (a difference of 37%).

Figure 5: Donations to the company are tax deductible, based on key indicators



## 7. MEMBERS, EMPLOYEES AND VOLUNTEERS

### 7.1. Number of members

#### 7.1.1. SURVEY QUESTION

##### 2.1.1 Members

How many members did the company have at 1 March 2002? (We mean ‘members’ in the legal sense, that is, those people or organisations named in the register of members kept by the company pursuant to its obligations under the Corporations Act.)

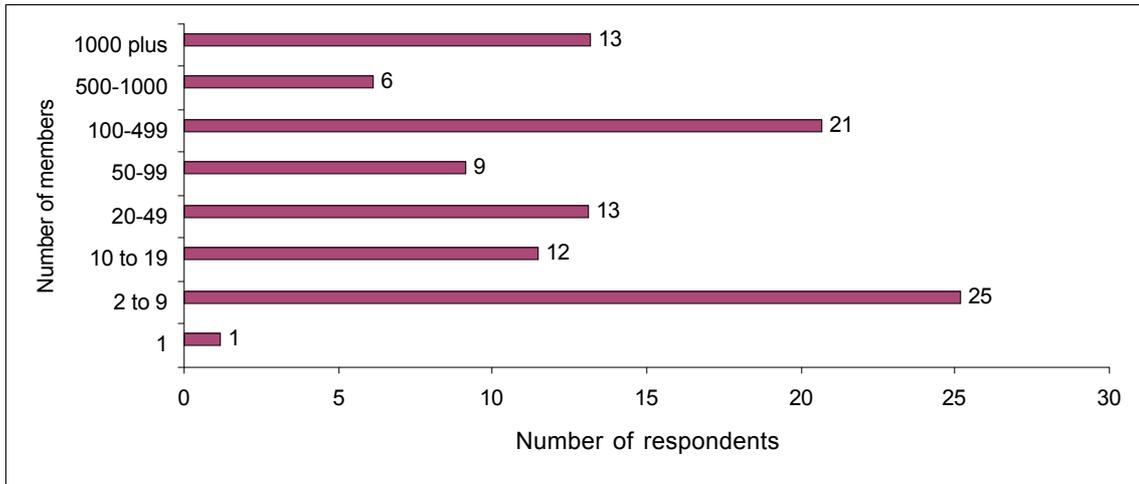
- none
- less than 5
- 5–less than 20
- 20–less than 50
- 50–less than 100
- 100–less than 1,000
- more than 1,000.

*Number of respondents = 1646*

#### 7.1.2. SURVEY RESULTS

There was a wide variety in the responses to this question, varying from only a few members to over a thousand members. Figure 6 shows that 25% of respondent companies had 2–9 members, and 21% of respondents had between 100 and 499 members. Forty per cent of all respondents had 100 or more members.

Figure 6: Number of members

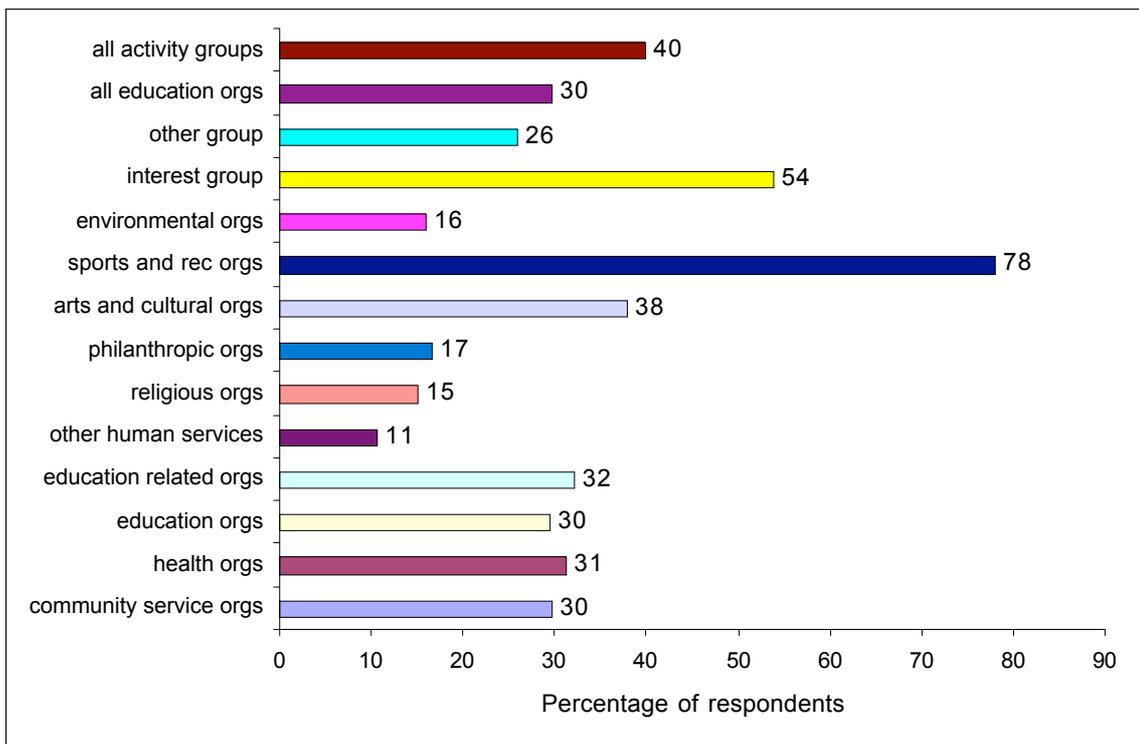


7.1.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Non-PBI status organisations are 15% more likely to have more than a hundred members than those without. Organisations not receiving government funding are also considerably more likely than those receiving government funding to have 100 or more members (48% vs 30%). As might be expected, member-serving organisations are more likely to have 100 or more members than public-serving organisations (55% vs 21%).

Figure 7 shows that Sports and Recreation organisations have by far the greatest number of members - 78% have 100 or more members. In contrast, only 11% of Other Human Services organisations have 100 or more members. Perhaps the most surprising result is that only 16% of Environmental organisations surveyed have 100 or more members. This low figure may be because respondents were asked to say how many members they have in a legal sense. That is, those people or organisations named in the register of members kept by the company pursuant to its obligations under the *Corporations Act 2001* (Cth). Environmental organisations often sign people up as 'members/supporters', and this does not mean 'member' in the legal sense.

Figure 7: Companies with one hundred-plus members, based on principal activity



## 7.2. Are the members individuals or organisations?

### 7.2.1. SURVEY QUESTION

2.1.2 Of the total number of members as at 1 March 2002, approximately how many were: (please print a number, or zero, on each line)

individuals...

Number of respondents = 1607

organisations...

Number of respondents = 1614

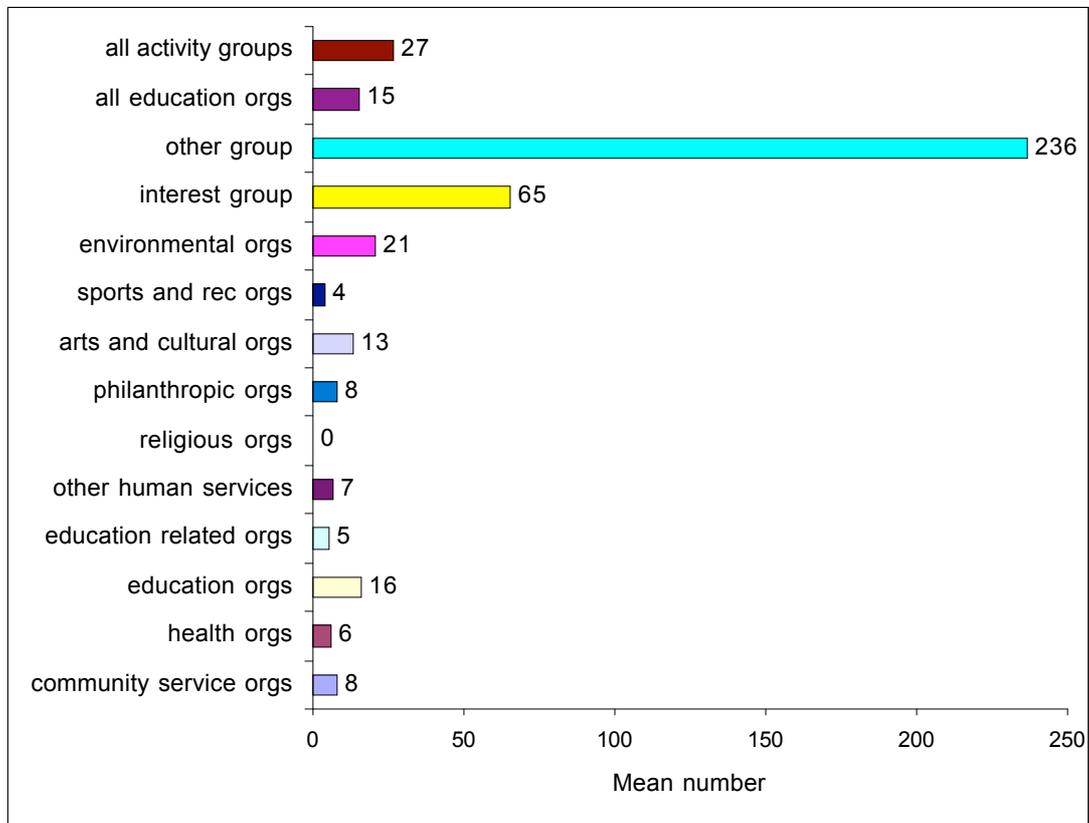
### 7.2.2. SURVEY RESULTS

Seventy-five per cent said that that they did not have any members that were organisations. However a small number (4%) had 100 or more members who were other organisations (not individuals).

### 7.2.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

This data was further analysed on the basis of the principal nature of its activities. Figure 8 shows the mean number of members that were organisations for each activity group. Interest-Group organisations, which include labour organisations, business and professional organisations, peak bodies and other interest groups rated second most highly, with an average of 65 members that were organisations. One 'Other groups' organisation said they had 12,300 members that were organisations, another said they had 2200 members that were organisations. The presence of these two respondents in the data pool skewed the result for 'Other Groups', pushing the mean number for this activity group up to 236.

Figure 8: Mean number of members that were organisations, based on principal activity



### 7.3. Number of employees

#### 7.3.1. SURVEY QUESTION

##### 2.2 Employees

How many employees (whether full or part-time) did the company have at 1 March 2002?

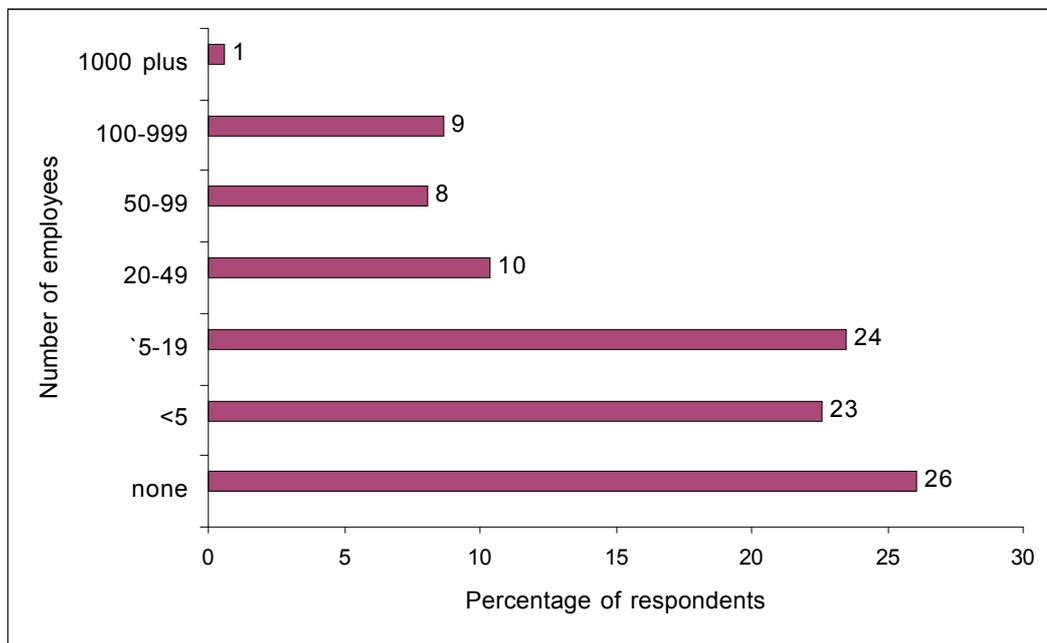
- none
- less than 5
- 5–less than 20
- 20–less than 50
- 50–less than 100
- 100–less than 1,000
- more than 1,000.

*Number of respondents = 1675*

#### 7.3.2. SURVEY RESULT

Overall, the number of employees employed by the NFP companies surveyed was very low. Only 28% of all organisations reported having more than 20 employees, whereas almost half the organisations (49%) had between 1 and 19 employees. Interestingly, not all NFP organisations employ even a part-time person who might, for example carry out the activities of the organisation or coordinate volunteers. Twenty-six per cent of respondents reported that their organisation had no employees.

**Figure 9: Number of employees**



#### 7.3.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

The data was broken down further on the basis of principal activity. This revealed a considerable variety between types of organisations. More than a third of Health (43%), Community Service (37%), Other Human Services (35%) and Sports and Recreation organisations (30%) reported having more than 20 employees. This is to be expected given that these organisations all provide professional services that require trained employees to work directly with clients. In contrast, only 2% of Philanthropic Organisations and 8% of Religious and Environmental organisations reported having more than 20 employees.

Figure 10 also shows that there is some difference based on whether organisations were public-serving or member-serving (34% vs 22%), and whether the organisation has PBI status or not (44% vs 23%).

**Figure 10: Twenty or more employees, based on principal activity**

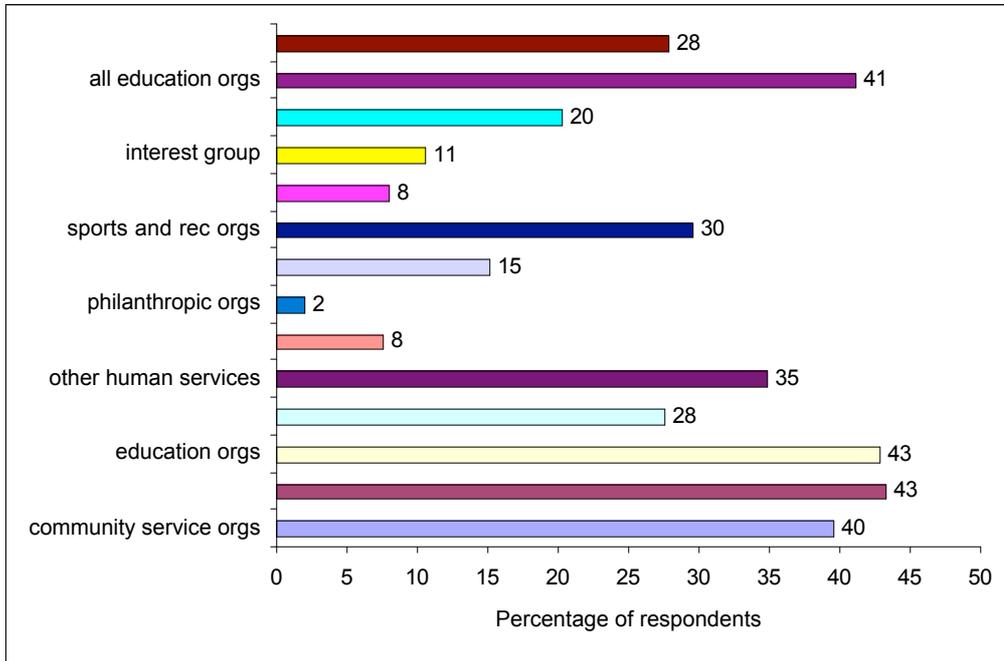


Figure 11 shows that there was a considerable difference between those organisations receiving government funding and those that do not (32% difference). We cannot be certain of the causal logic, that is, whether receiving government funding provides organisations with the capital to employ people, or whether the presence of employees means that those organisations are more likely to attract government funding.

Figure 12 shows that the correlation between the number of employees and the receipt of government funding is quite strong for most activity groups. The main exceptions are Environmental and Sports and Recreation organisations. In the case of Sports and Recreation organisations, this may be because they raise most of their money through membership fees.

**Figure 11: Twenty-plus employees, based on key indicators**

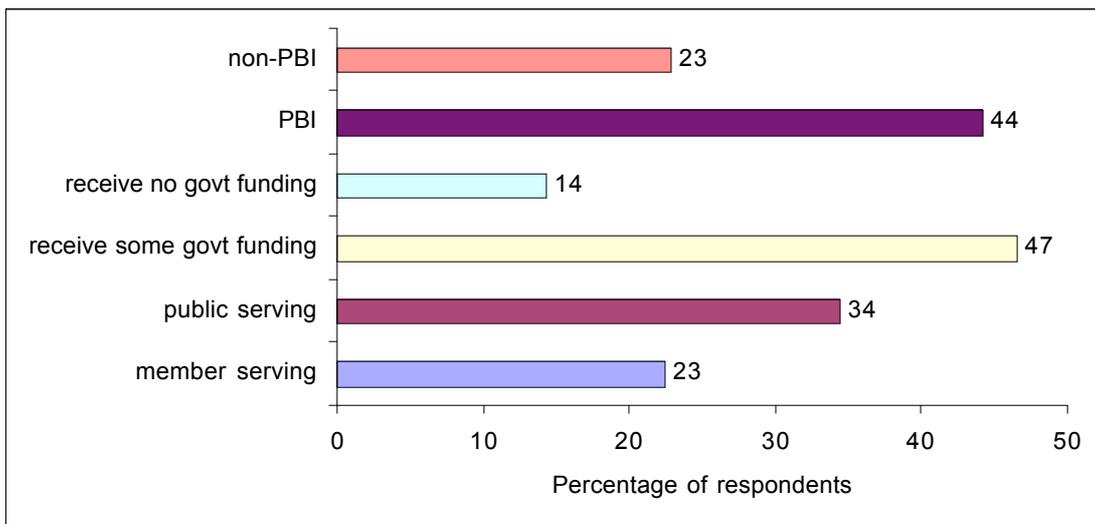
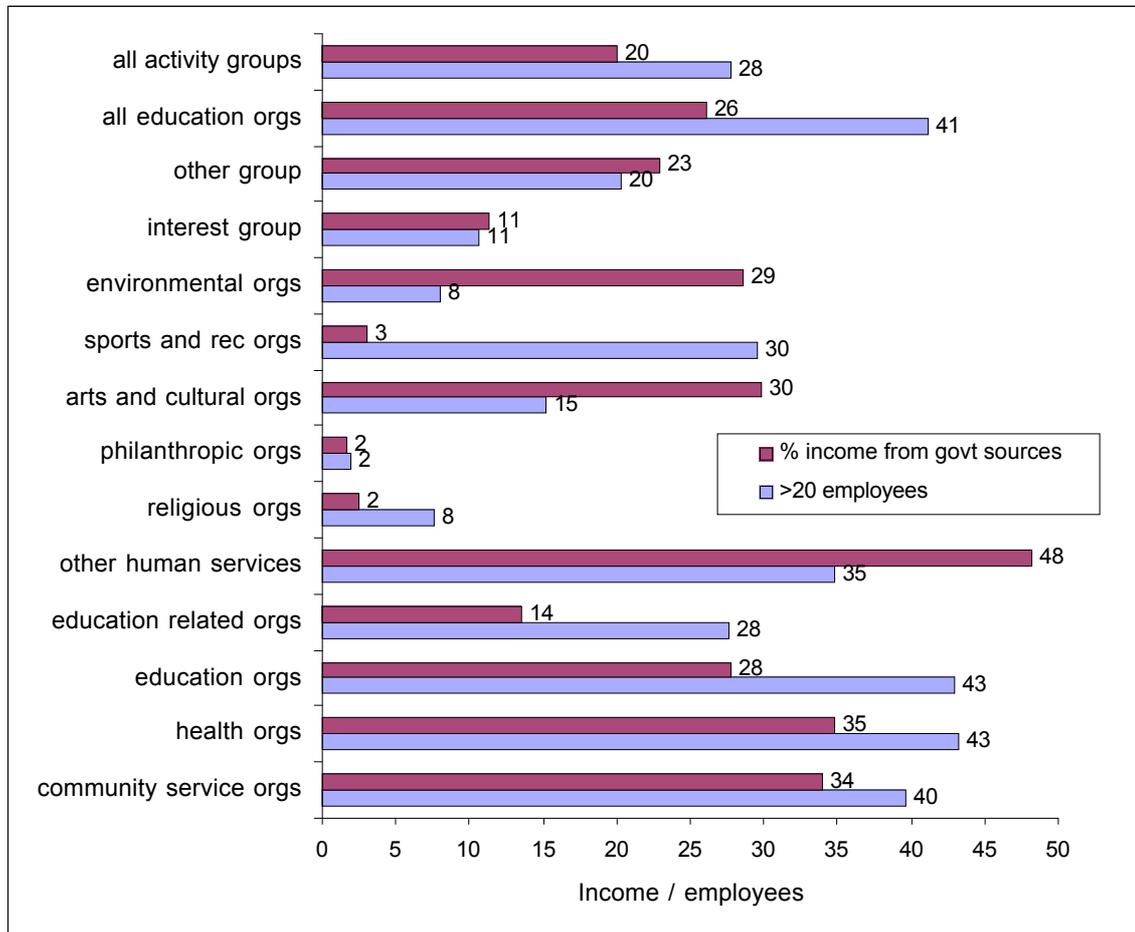


Figure 12: Twenty-plus employees, compared with percentage income deriving from government sources for each activity group



## 7.4. Number of volunteers

### 7.4.1. SURVEY QUESTION

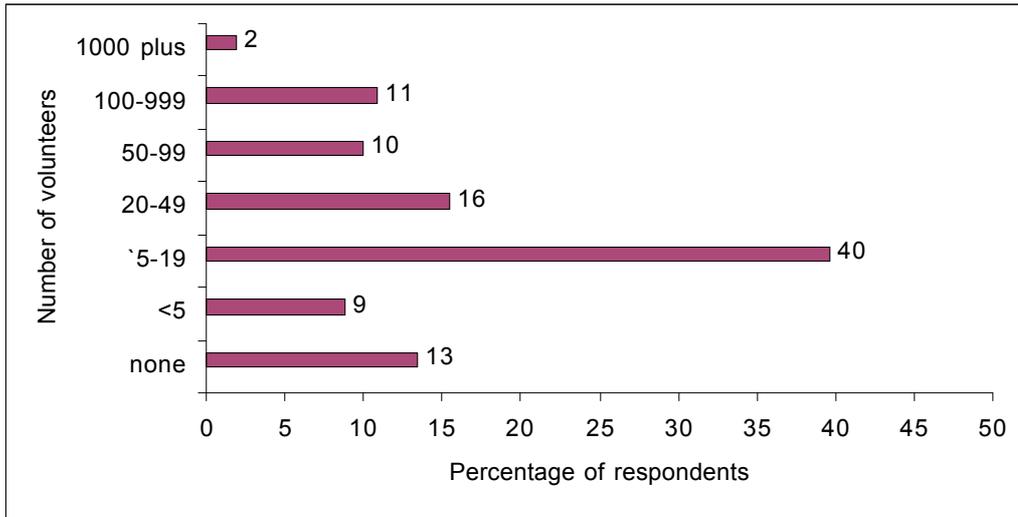
- 2 For 2001, estimate the total number of volunteers (whether full or part-time and including volunteer Board members) that provided assistance to the company.
- none
  - less than 5
  - 5–less than 20
  - 20–less than 50
  - 50–less than 100
  - 100–less than 1,000
  - more than 1,000.

*Number of respondents = 1668*

### 7.4.2. SURVEY RESULTS

The survey results (Figure 13) showed that 86% of respondent companies had at least 1 volunteer and 38% have 20 or more. At the upper end, it is interesting to note that 31 organisations had more than 1,000 volunteers.

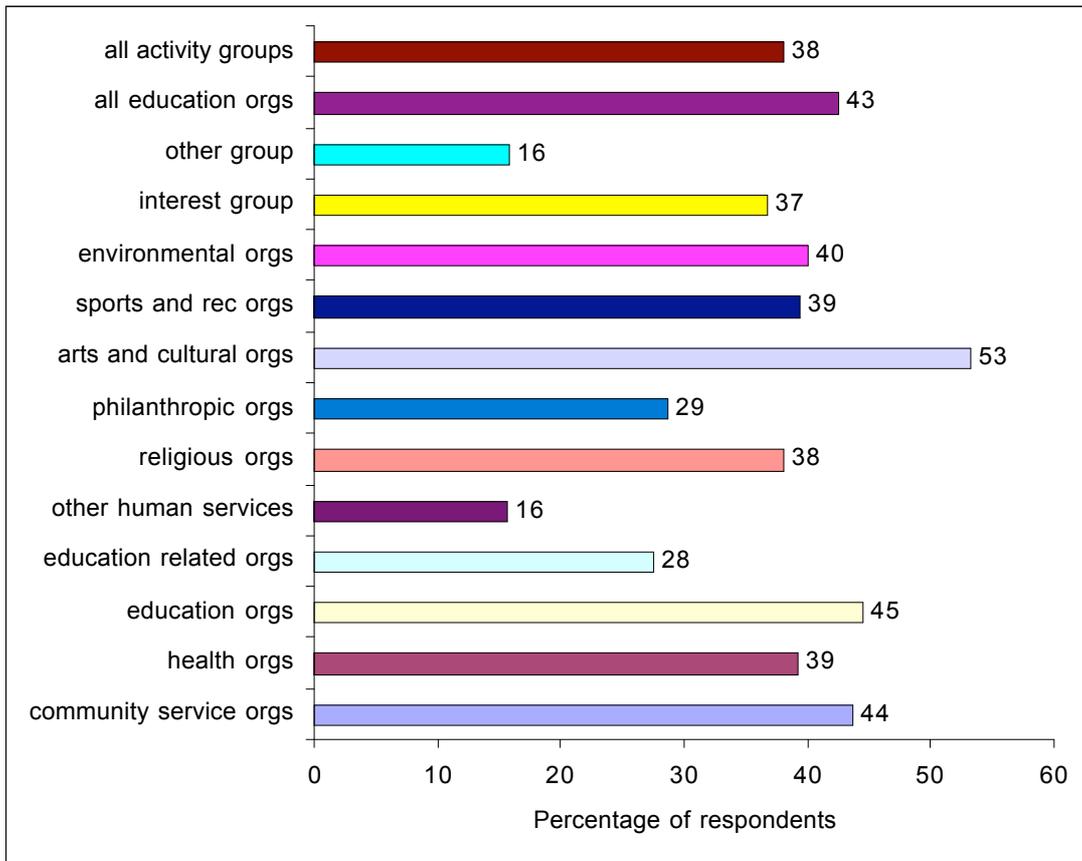
Figure 13: Total number of volunteers providing assistance to the company



7.4.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Figure 14 shows the breakdown of organisations with more than 20 volunteers. The data shows that approximately 53% of Arts and Cultural organisations had more than 20 volunteers, compared with the overall figure of 38%. More than 40% Community Service, Educational and Environmental organisations respectively also have more than 20 volunteers.

Figure 14: 20-plus volunteers, based on principal activity



Cross-tabulations were also done on the basis of size, the receipt of government funding, whether the organisation is public or member-serving and whether the organisation has PBI status. Predictably, large organisations are more likely to have more than 20 volunteers. The other indicators do not have a significant effect on the presence of volunteers.

7.4.4. OBSERVATION

The data shows that volunteers are an important source of labour for many NFP organisations. Their presence appears to constitute a distinctive characteristic of NFP organisations. Their involvement is part of an ideology of inclusiveness and participation and they provide a cost advantage which is unique to NFP organisations.

However, as Leat observes, this advantage is reduced when the cost of managing volunteers is taken into account.<sup>19</sup>

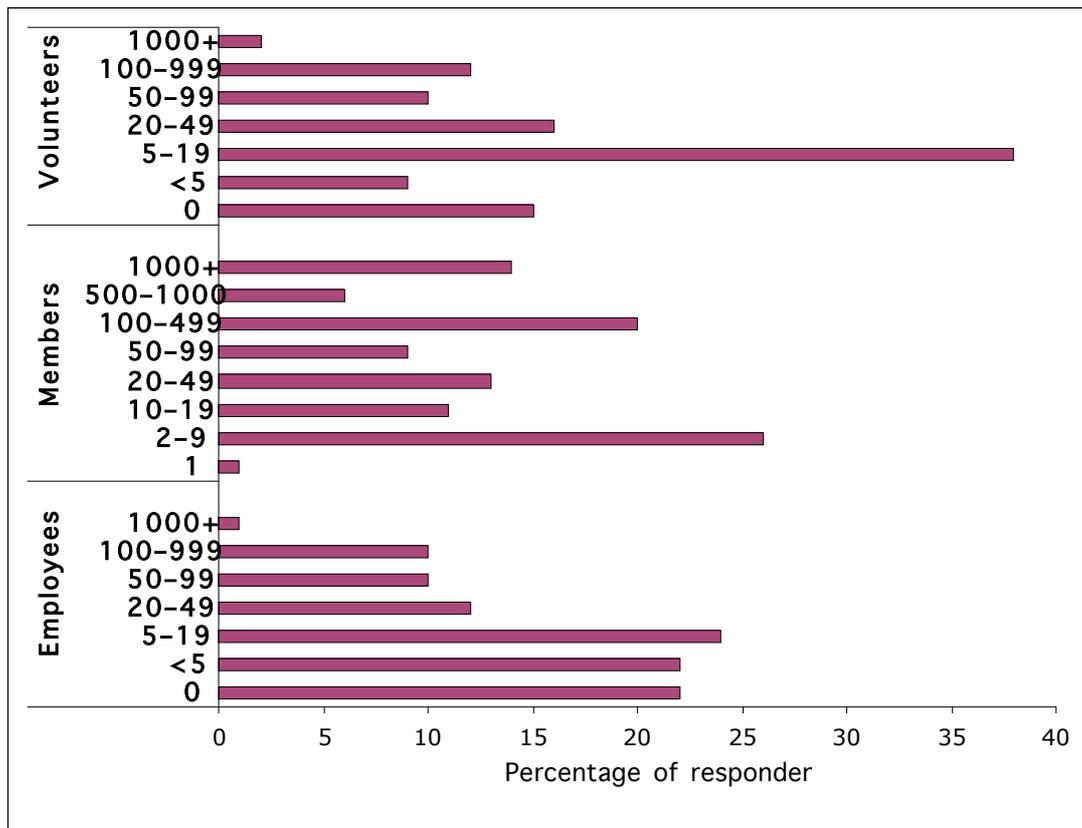
[T]he presence of volunteers and their need for participation and equality, combined with paid professional staff and their need for autonomy, as well as the ‘ambiguous’ relationship between staff and Board, may produce a potent mix from which organisational chaos may all too easily emerge.

The satisfaction of working without pay appears to demand an egalitarian, participative organisational framework. However, this was not necessarily reflected in the findings concerning Board composition or who are regarded as key stakeholders.<sup>20</sup>

7.5. Comparison of employees, volunteers and members

Figure 15 shows the responses to questions about the size of the company in terms of the number of members, employees and volunteers. As seen above, there was a good spread of respondents ranging from very small companies (no employees) through to large NFPs (more than 1000 employees) as well as both small and large membership bases. While the spread was large, the majority of NFP companies limited by guarantee were at the smaller end: 72% of respondents had fewer than 20 employees, 62% had fewer than 20 volunteers and 60% had fewer than 100 members. It is also worth noting that there was no clear relationship<sup>21</sup> between the number of employees and the number of members or volunteers. For example, a large membership base did not necessarily mean a large number of volunteers/employees.

Figure 15: Comparison of employees, volunteers, and members



<sup>19</sup> D. Leat, *Managing Across Sectors: Similarities and Differences Between For-Profit and Voluntary Non-profit Organisations*, City University Business School, 1993, p. 37.

<sup>20</sup> See Chapter 7, Stakeholders, and Chapter 8, Disclosure.

<sup>21</sup> Spearman's range from 0.1 to 0.2.

## 8. SIZE

### 8.1. Income

#### 8.1.1. SURVEY QUESTION

3.1.1 As at the end of the company's last financial year, please indicate gross income from all sources (where relevant, please include fundraising, government funding, fees for service, subscriptions, commercial sales, interest income, bequests, philanthropic grants, corporate sponsorship and any other non-government grants).

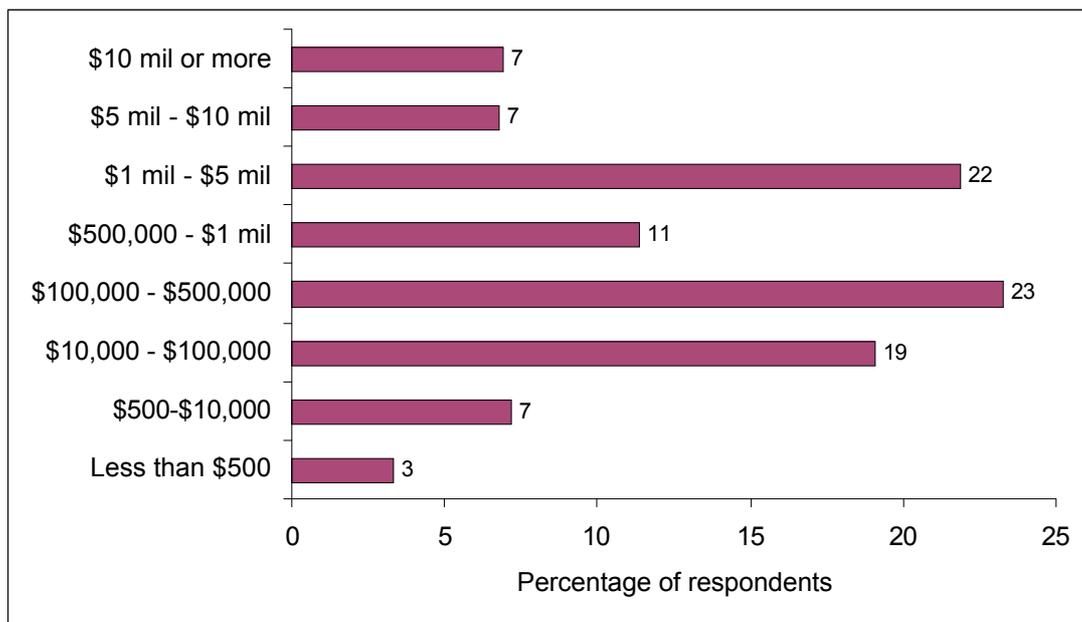
- less than \$500
- \$500–less than \$10,000
- \$10,000–less than \$100,000
- \$100,000–less than \$500,000
- \$500,000–less than \$1mil
- \$1mil–less than \$5mil
- \$5mil–less than \$10mil
- \$10mil or more.

*Number of respondents = 1651*

#### 8.1.2. SURVEY RESULTS

Just under a third of NFP organisations surveyed (30%) had an income of less than \$100,000 in the last financial year, and just over a half (53%) had an income of less than \$500,000. These proportions give an indication of what might be a useful figure when distinguishing between large and small organisations for regulatory purposes. Only 36% of organisations surveyed had \$1 million or more gross income in the last financial year.

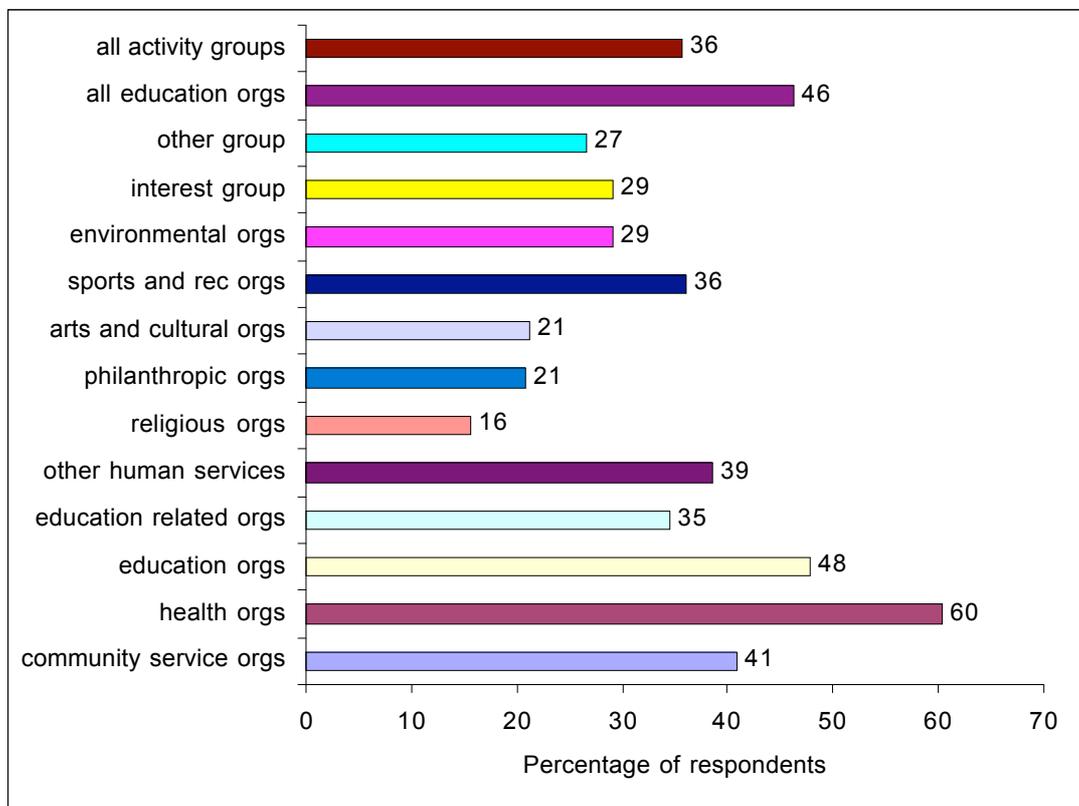
**Figure 16: Gross income**



8.1.3. SIGNIFICANT DIFFERENCES BETWEEN ORGANISATIONS

Figure 17 shows that Health organisations are most likely to have income of more than \$1 million (60%), followed by Education (48%) and Community Service organisations (41%).

Figure 17: \$1 million-plus gross income in the last financial year, based on principal activity



8.2. Income deriving from government sources

8.2.1. SURVEY QUESTION

3.1.2 What percentage of income would you estimate comes from government sources?

..... % (please print a number of zero)

Number of respondents = 1603

8.2.2. SURVEY RESULTS

Fifty-nine per cent of all organisations surveyed received no income from government sources over the financial year prior to the survey being completed. This is a relevant factor to take into account when considering the issue of accountability and disclosure.<sup>22</sup>

8.2.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

As Figure 18 shows, significantly more Religious organisations (89%), Philanthropic organisations (88%) and Sports and Recreation organisations (85%) received no government income compared with the overall figure of 59%.

<sup>22</sup> See Heading 7.

Figure 18: Zero income derived from government, based on principal activity

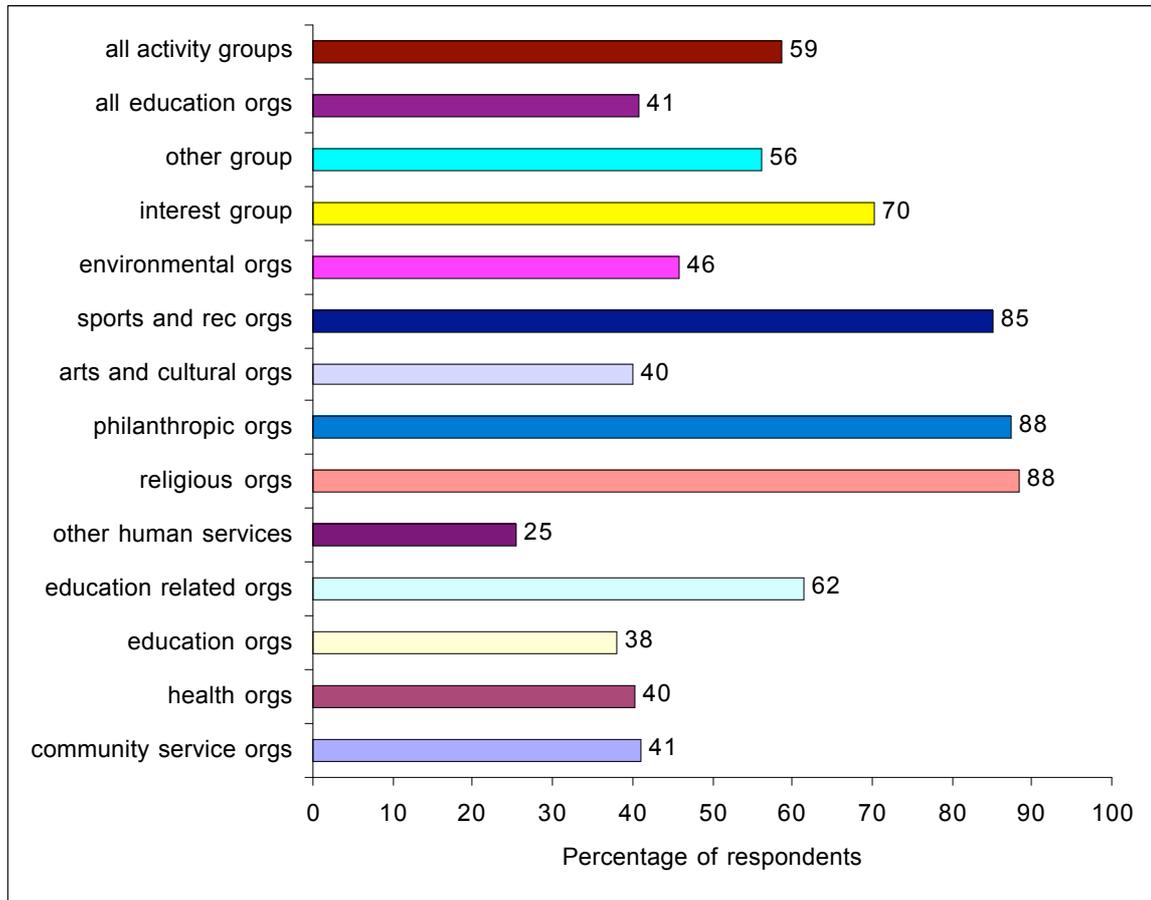
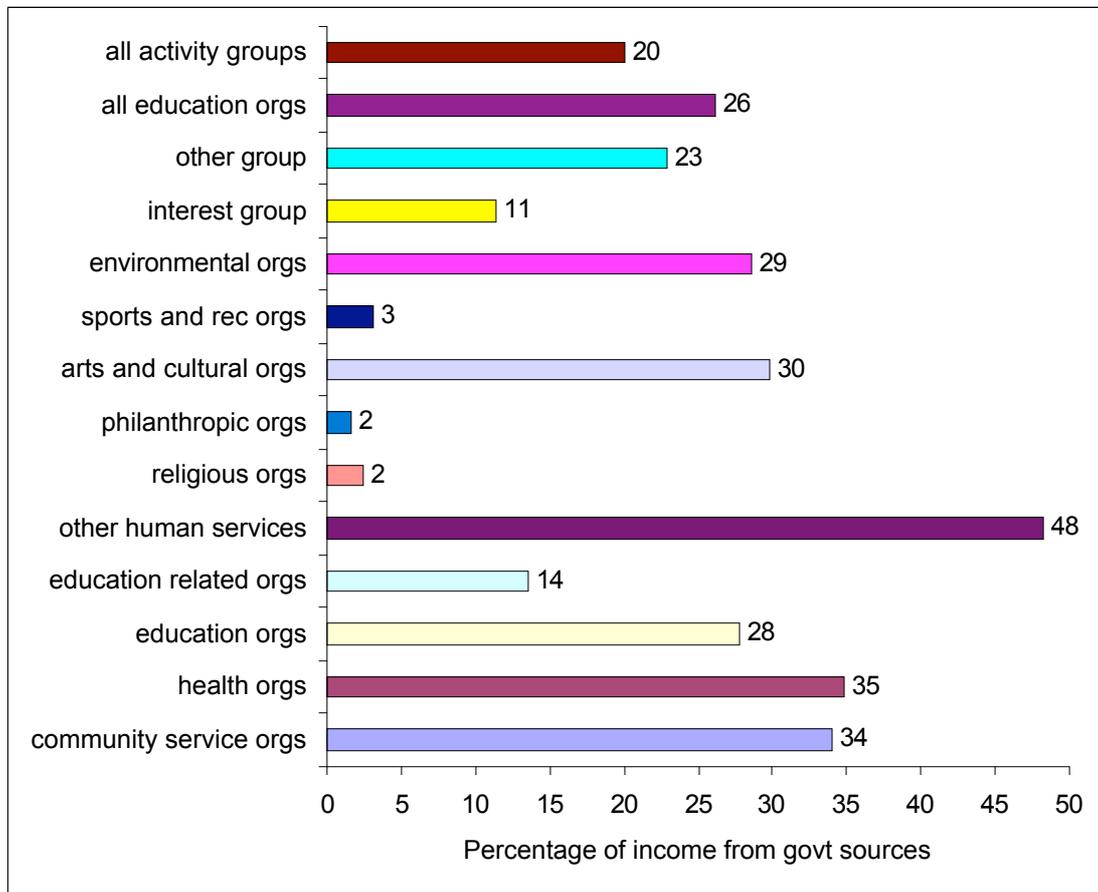


Figure 19 shows the average percentage of *all income* that each organisation estimated came from government sources in the financial year prior to the survey being completed.<sup>23</sup> Other Human Services organisations (48%) receive by far the greatest amount of income as a percentage of their overall income, followed by Health organisations (35%) and Community Service organisations (34%). As expected, the data shown in Figure 18, shows Philanthropic (2%), Religious (2.5%) and Sports and Recreation organisations (7%) receive very little in the way of government funding as a proportion of their overall income.

<sup>23</sup> Around two thirds of the observations shown in Figure 19 fall within (plus or minus) one standard deviation of the mean.

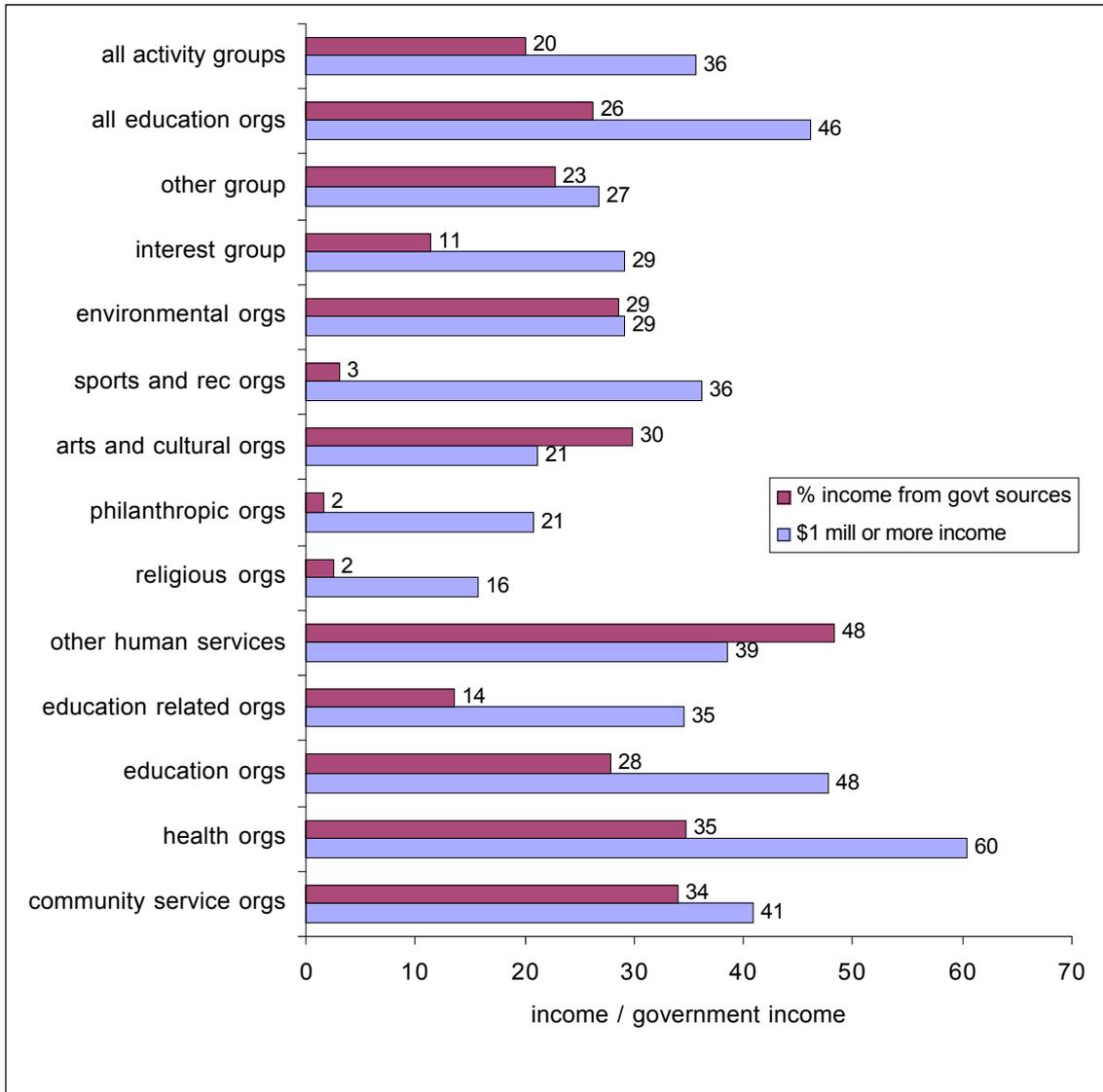
Figure 19: Average percentage of income deriving from government sources, based on principal activity



Using activity groups, Figure 20 indicates the relationship between the total gross income of an organisation and the percentage of income that comes from government sources.<sup>24</sup> For most activity groups relationship between the percentage of government funding and the amount of the organisation's overall income is obvious (for example, Environmental and Community Service organisations). However, for some activity groups further investigation is needed: for example, Health organisations where 60% have a gross income of \$1 million or more, but only 35% of that income comes from government sources.

<sup>24</sup> Around two thirds of the observations shown in Figure 20 fall within (plus or minus) one standard deviation of the mean.

Figure 20: Government income and percentage of organisations receiving gross income of \$1 million-plus



### 8.3. Assets

#### 8.3.1. SURVEY QUESTION

3.2 As at the end of the company's last financial year, please indicate the total value of the company's assets.

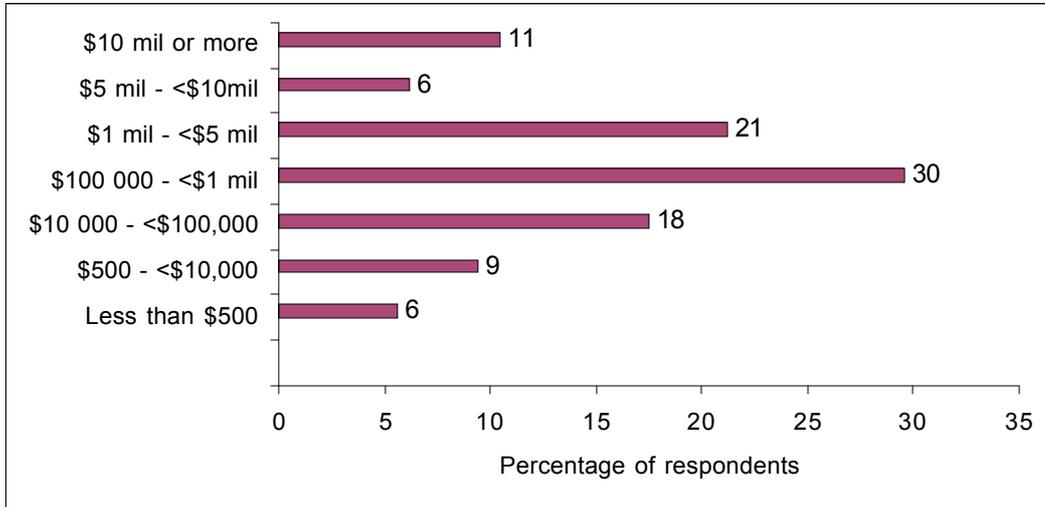
- less than \$500
- \$500–less than \$10,000
- \$10,000–less than \$100,000
- \$100,000–less than \$500,000
- \$500,000–less than \$1 mil
- \$1 mil–less than \$5 mil; \$5 mil–less than \$10 mil
- \$10 mil or more.

Number of respondents = 1637

8.3.2. SURVEY RESULTS

While there was a spread of companies in all categories, the majority (62%) had under \$1million in assets and 83% had under \$5 million in assets (that is, within the s 45A *Corporations Act 2001* (Cth) definition of small proprietary company, see Heading 8.5.1). See Figure 21.

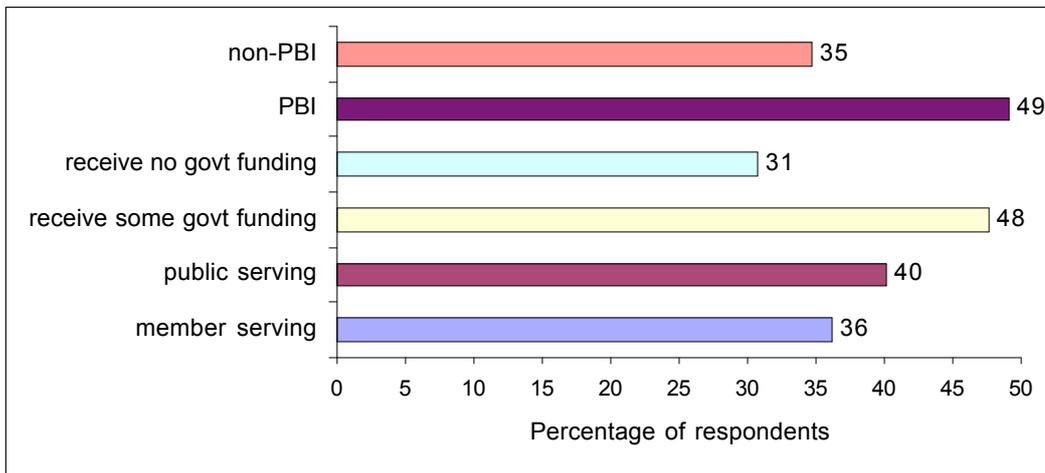
Figure 21: Total value of organisation's assets



8.3.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

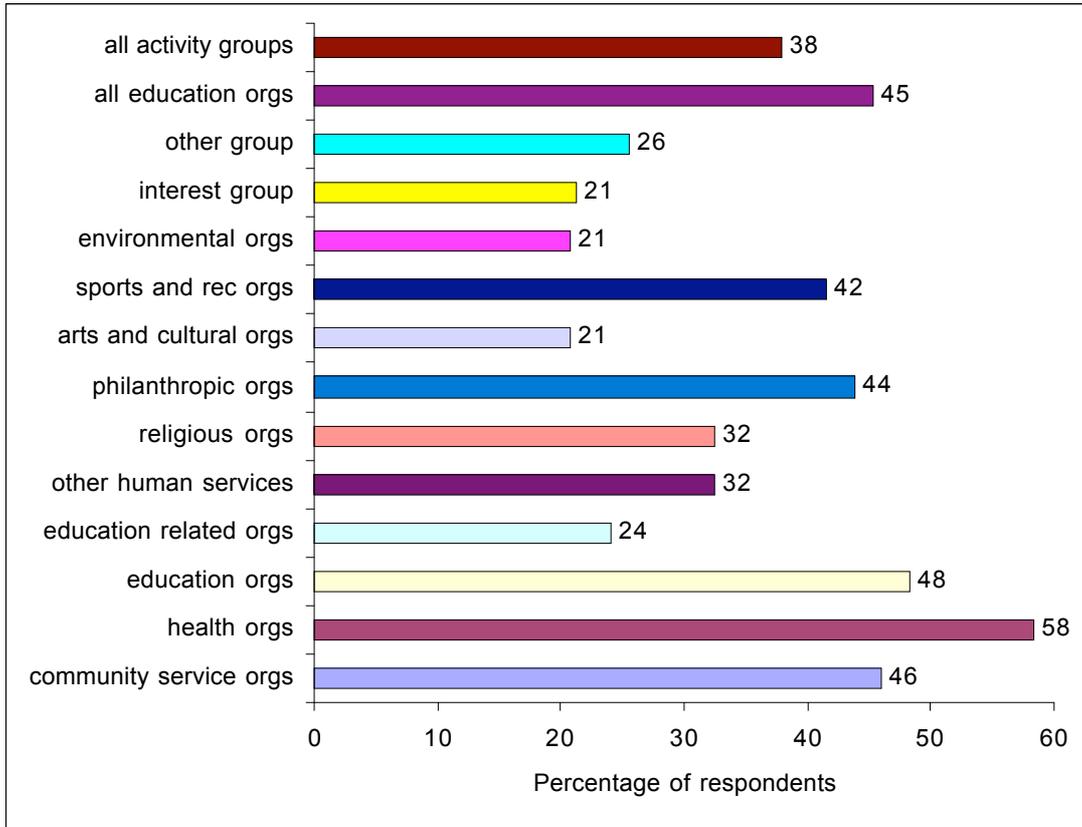
Figure 22 shows the number of organisations in each category with \$1 million or more in assets. There is very little difference between member-serving and public-serving organisations in terms of the size of their assets. Companies with PBI status and those receiving government funding are more likely than those that do not to have larger assets (PBI status/no PBI status = 14% difference, government funding / no government funding = 17%).

Figure 22: Assets of \$1 million-plus, based on three key indicators



There are considerable differences between activity groups in terms of those with \$1 million or more in assets. As might be expected, Health organisations were most likely to have assets valued at \$1 million or more (58% of Health organisations have assets valued at over \$1 million). Health organisations generally require buildings and equipment to carry out their operations. Education organisations (48%), Community Service organisations (46%), Philanthropic organisations (44%) and Sports and Recreation organisations (42%) were the next most likely to have more than \$1 million in assets. As Education organisations include preschools, schools and universities, it is not surprising that their assets might be greater than other types of organisations. Philanthropic organisations often have large investments and endowments that might contribute to the worth of their assets.

Figure 26: Assets of \$1 million-plus, based on principal activity



## 8.4. Liabilities

### 8.4.1. SURVEY QUESTION

3.3 For the company's last financial year, please indicate the company's total liabilities.

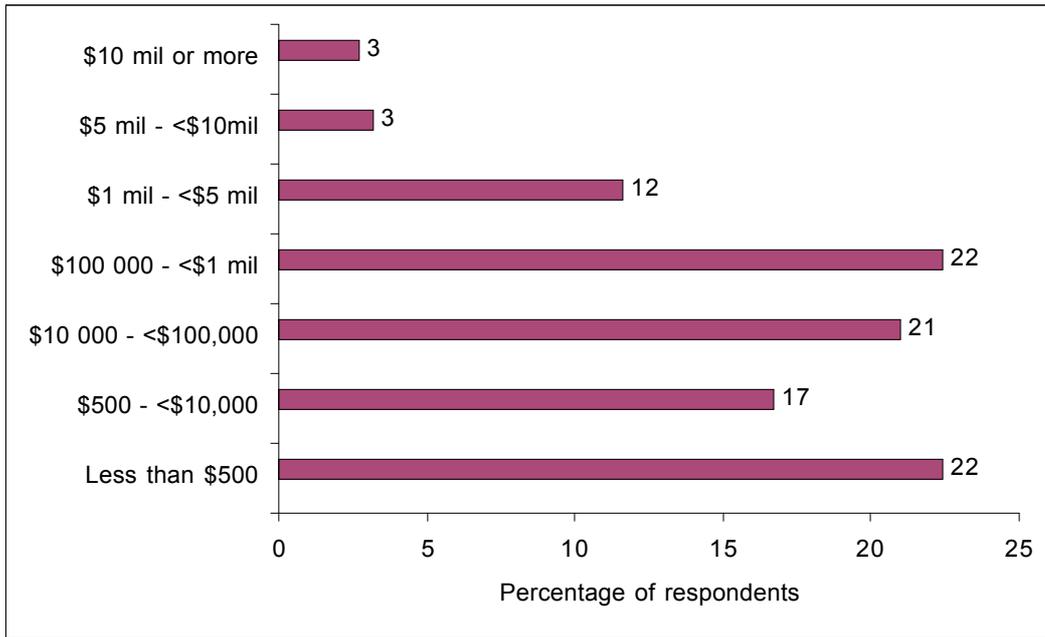
- less than \$500
- \$500–less than \$10,000
- \$10,000–less than \$100,000
- \$100,000–less than \$500,000
- \$500,000–less than \$1mil
- \$1mil–less than \$5mil
- \$5mil–less than \$10mil
- \$10mil or more.

*Number of respondents = 1622*

### 8.4.2. SURVEY RESULTS

There was also a spread in the size of the companies' liabilities in the financial year prior to completing the survey (Figure 24). Eighty-three per cent of all companies had liabilities of less than \$1 million and the majority (60%) had liabilities of less than \$100,000.

Figure 24: Company's total liabilities



8.4.3. SIGNIFICANT DIFFERENCES BETWEEN ORGANISATIONS

Organisations receiving some government funding are 16% more likely than those receiving none to have liabilities valued in excess of \$1 million. Those with PBI status are 11% more likely than those without to have liabilities valued in excess of \$1 million.

Figure 25: Liabilities of \$1 million-plus, based on three key indicators

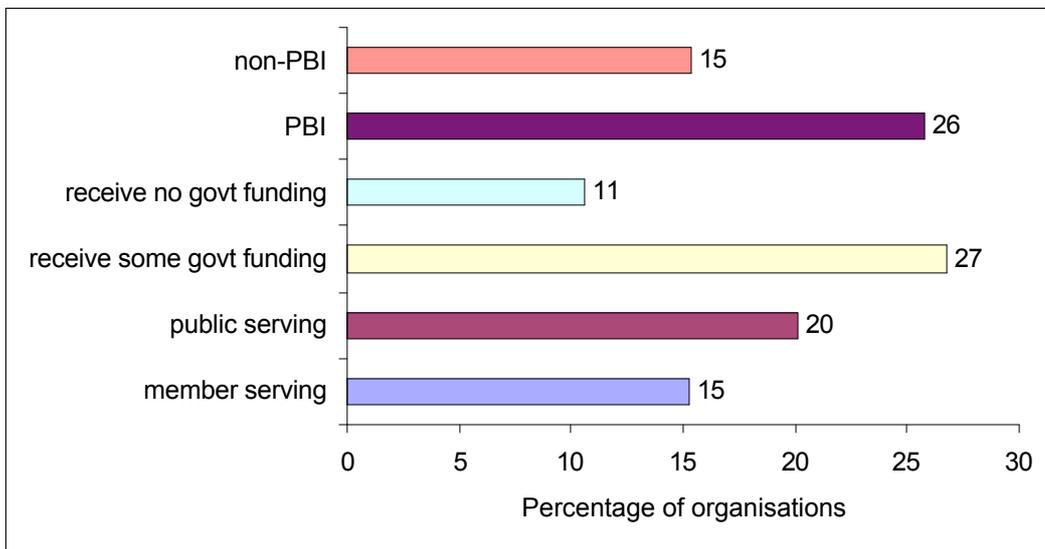
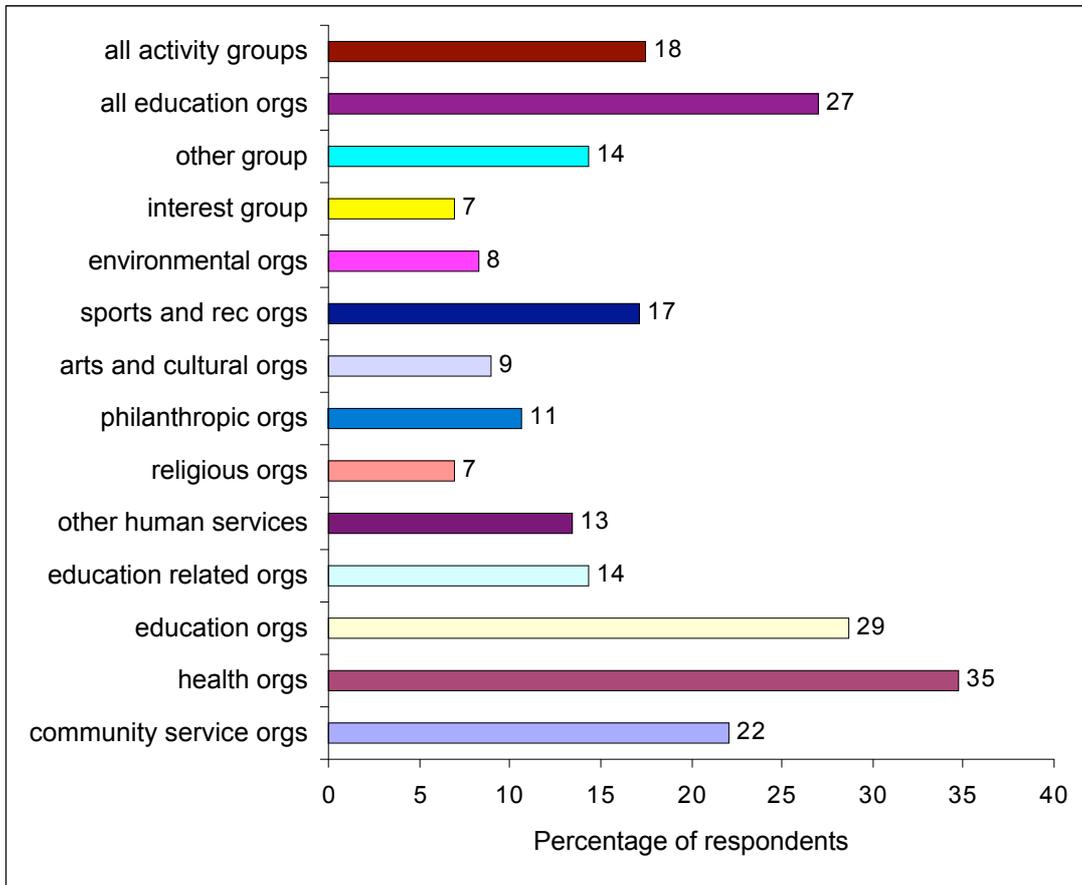


Figure 26 shows that, following the pattern of assets, Health organisations are most likely to have liabilities of more than \$1 million (35%), then Education organisations (29%), and Community Service organisations (22%). Only 7% of Interest Group organisations, 7% of Religious organisations and 8.3% of Environmental organisations had liabilities in excess of \$1 million.

Figure 26: Liabilities of \$1 million-plus, based on principal activity

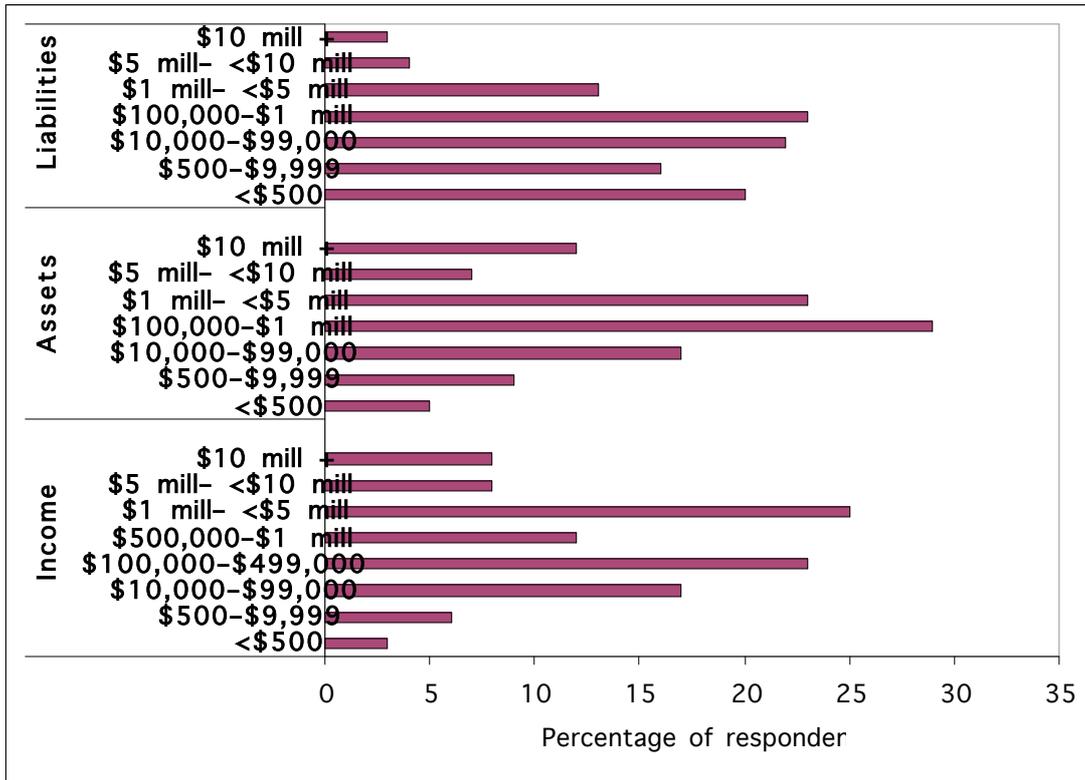


### 8.5. Comparison of income, assets and liabilities

Figure 27 combines the responses to questions about the size of the company in terms of the income, assets and liabilities. Again, there was a good spread of respondents ranging from very small organisations (annual income of less than \$500) through to large NFPs (income of more than \$10 million and assets of more than \$10 million). Unlike the correlation between members, employees and volunteers (see Heading 7.5), there was a strong relationship<sup>25</sup> between the size of the respondent company’s income, assets and liabilities. Namely, a NFP company that had higher income typically also had greater assets and higher liabilities.

<sup>25</sup> Spearman’s correlation ranging from 0.7 to 0.8.

Figure 27: Income, assets and liabilities



8.5.1. OBSERVATION

In order to determine how many of the NFP companies in the sample fell within the *Corporations Act 2001* (Cth) definition of small company, the test for a “small proprietary company” contained in s 45A(2) of the *Corporations Act* was applied to the survey data. Section 45A(2) states:

A proprietary company is a small proprietary company for a financial year if it satisfies at least 2 of the following paragraphs:

- (a) the consolidated gross operating revenue for the financial year of the company and the entities it controls (if any) is less than \$10 million;
- (b) the value of the consolidated gross assets at the end of the financial year of the company and the entities it controls (if any) is less than \$5 million;
- (c) the company and the entities it controls (if any) have fewer than 50 employees at the end of the financial year.

While the wording of the questions relating to size in the questionnaire did not exactly match the wording of s 45A(2), they were considered sufficiently similar for general comparison purposes. In particular, the questionnaire used options that matched in terms of dollar values. For example, in terms of assets, the multiple choice options in the questionnaire could readily be collapsed to show those responses of less than \$5 million, being the amount referred to in s 45A(2)(b). When the s 45A test was applied to the survey data, it showed that 88% of NFP companies in the sample would (for their last financial year) have been classified as ‘small’. This assumed of course, that they were a proprietary company (limited by shares) rather than a company limited by guarantee (for which there is no equivalent ‘small’ and ‘large’ dichotomy).

However, it is important to remember that in the NFP sector there may be a different notion of ‘large’ and ‘small’ than that reflected in the s 45A definition.<sup>26</sup> Many would think that an NFP organisation with say, 45 employees, assets of \$4 million and revenue of \$9 million would be a medium if not large organisation, especially if it had a large volunteer base. Thus, the application of the s 45A definition does not necessarily provide an accurate description of the size of the

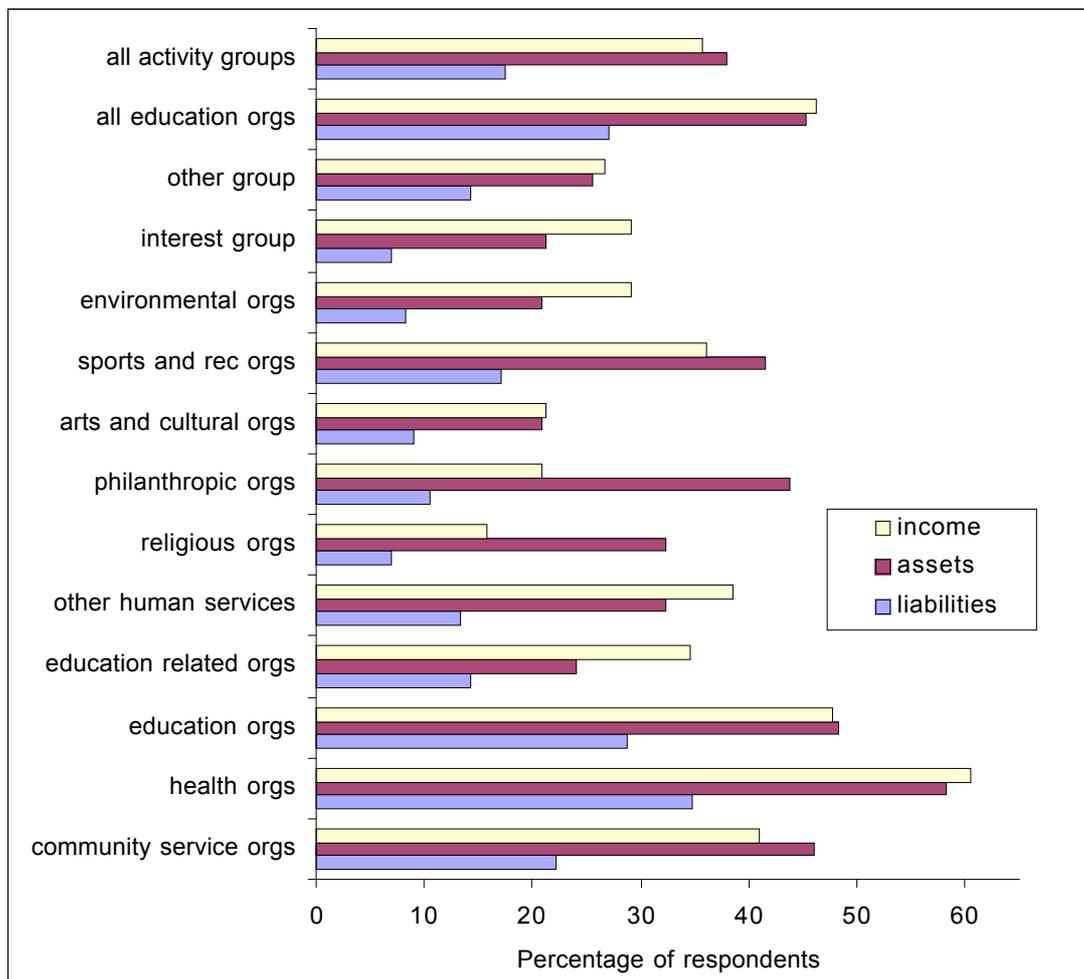
<sup>26</sup> Even among ‘for-profits’ there has been contention about the definition and concern about those companies falling somewhere between those that are clearly ‘small’ or ‘large’. See generally Parliamentary Joint Statutory Committee on Corporations and Securities, *Report on Aspects of the Regulation of Proprietary Companies*, 2000, at <[www.aph.gov.au/senate/committee/corporations\\_ctte/propcom/propcom.pdf](http://www.aph.gov.au/senate/committee/corporations_ctte/propcom/propcom.pdf)>.

respondent companies. Rather, the finding shows that if the vast majority of NFP companies limited by guarantee were proprietary companies, because of their size, they could avoid certain company law disclosure and other requirements. In particular, as 'small' proprietary limited companies (under the s 45A definition), they would not be required by the *Corporations Act* to have their accounts audited or to lodge them with ASIC.<sup>27</sup> This reflects the underlying policy that 'small' proprietary companies, in relative terms, have the most minimal reporting and disclosure obligations compared to public companies, which include companies limited by guarantee. This finding is relevant when considering why a company limited by guarantee is chosen as the legal form, and the disclosure and reporting obligations that are appropriate.<sup>28</sup> See Chapter 3, Legal Structure, Heading 4 for further discussion of these issues in relation to proposed reforms to the incorporated associations regime.

8.5.2. INCOME, ASSETS AND LIABILITIES COMPARED - PRINCIPAL ACTIVITY

Figure 28 shows that there is a very strong correlation between income, assets and liabilities for each group based on principal activity, with the exception perhaps of Philanthropic organisations.

Figure 28: Comparison of income, assets and liabilities of \$1 million-plus, based on principal activity



<sup>27</sup> Unless requested by ASIC ( *Corporations Act 2001* (Cth), s 294) or by the requisite number of members (s 293) or if they are controlled by a foreign owned company (s 292(2)(b)).

<sup>28</sup> See Chapter 8, Disclosure.

### 9. CONCLUSION

This profile data highlights the multiplicity of organisations coming under the umbrella term: not-for-profit. Despite these differences, we can make some generalisations from the data. We can say that the typical respondent to the questionnaire was a CEO (59%) of a NFP company that:

- was member-serving as opposed to public-serving: 56%
- was income tax exempt but did not have tax deductibility status: 91% were income tax exempt; 48% had tax deductibility status
- did not hold a licence to omit the word 'Limited' from its name: only 25% said they held a name licence, 54% did not have such a licence and 21% 'don't know'
- was small-to-medium in size
- received no income from government sources: 59%
- relied on volunteers: 86% had at least one volunteer.

In later Chapters, this profile data has been cross-tabulated with findings concerning stakeholders, disclosure and opinions about a new regulator in an to attempt to discern whether any differences in opinion are based on the profile or the distinctive features of the organisation. However, the profile data has a significance of its own. It can be used to discern whether there are significant differences between NFPs and 'for-profits' which would lead to a need for different regulation.

Some academic commentators have argued that the differences between NFP organisations and 'for-profits' are exaggerated, and, in fact, that there is a convergence between NFP and 'for-profit' companies.<sup>29</sup> The profile data outlined in this Chapter suggests that there are, indeed, significant differences between NFP companies and 'for-profits'. The heavy reliance on volunteers and the general absence of group structures are two such examples. The small size of NFP organisations relative to many of their 'for-profit' cousins is also a significant matter to be taken into account when determining the regulatory burden to be placed on them. Likewise, the taxation benefits that many NFP companies enjoy may mean that the disclosure requirements should be higher than those expected of 'for-profit' companies.

These are all important matters that require detailed consideration. The Chapters that follow are an attempt at beginning that process.

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<sup>29</sup> See for example, Leat, n . 19, 1993. Leat uses the term 'non-profit' rather than 'not-for-profit' and argues that there is a growing convergence between NFPs and 'for-profits'. Leat is interested in this convergence from a managerial perspective, however, and not a regulatory one.

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## CHAPTER 3: LEGAL STRUCTURE

### Do NFP organisations fit the company mould?

#### SUMMARY OF KEY FINDINGS IN THIS CHAPTER

##### Importance of legal structure

- The underlying legal structure must be one suited to the needs of a NFP organisation before accountability can be improved by the application of consistent and appropriate reporting obligations.
- The existing myriad of legal structures hampers nationally consistent accountability.

##### Choice of legal structure

A significant number of NFP companies limited by guarantee were registered prior to the introduction of associations' incorporation legislation. Taking into account this sub-group, the most significant findings as to why a company structure was chosen in preference to, say, an incorporated association were:

- Legal advice and taxation/financial advice received at the time were the two main factors: no doubt this advice would have taken into account a range of reasons, including the other reasons listed in the question.
- More than a third (34%) indicated that being a 'national or multi-state organisation' was an important factor in their choice of a company structure.
- Forty per cent indicated that the 'scale of trading activities' was an important factor, which is an area of debate and variation in the associations' regime.
- Almost a third (31%) identified a preference for Australian Securities and Investments Commission (ASIC) 'rather than State regulator' as an important factor thereby supporting anecdotal evidence that many of the State regulators are under resourced and cannot cope easily with organisations wanting to have variations to the prescribed model rules.
- 'Public perception and status' was important to the majority (52%) which also supports anecdotal evidence that 'serious' or 'more sophisticated' NFP organisations are companies rather than incorporated associations.

##### Success of company structure

- There was no clear evidence of any overall dissatisfaction with the company structure. About three-quarters of the respondents believe that the company structure is well understood by directors and those dealing with the company, and that it has been a flexible structure with manageable reporting obligations.
- However, it is worth noting that:
  - s 'Small' organisations reported more difficulties than 'large' organisations.
  - s Religious organisations reported more difficulties than other companies.
  - s Forty-four per cent of respondents said that the company structure was not readily understood by members.
- There was dissatisfaction about:
  - s Expense: 41% believe that a company structure has 'added expense' and this was higher for "small" and also member-serving organisations.
  - s Paperwork: the majority (51%) thought a company structure had 'added a lot of paperwork'.
- Written comments highlighted that the difficulties experienced often stem from:
  - s A company limited by guarantee (which is a public company) not being specifically designed to meet the needs of NFP organisations.
  - s Difficulties and expense in migrating to the incorporated associations regime.
  - s The significant cost of audit fees.

##### Group structures

- Group structures were not common. Only 14% of respondents were part of a group structure.
- Of this 14%, the majority were Philanthropic organisations with only one or two related entities.

### Need for unified regulation

- While the survey did not cover incorporated associations, there were several findings (and other feedback) that indicate problems caused by the inconsistencies between the States and Territories.
- The data in this Chapter supports the data in Chapter 4, Regulation, and our recommendation for a single, Commonwealth regime for all corporate bodies, but with a specialised corporate form for NFP organisations.
- The data reported in this Chapter also supports the introduction of different reporting obligations dependent on an organisation's size (see Chapter 8, Disclosure).

## RECOMMENDATIONS

### Modify existing Corporations Act requirements

While the existing company limited by guarantee structure has proved satisfactory in the main, some aspects need reform. These includes:

- the fee structure should be revised to provide a sliding scale based on size.
- information required for disclosure should be tailored to the needs of NFP stakeholders rather than to 'shareholders', and this needs to be supported by an NFP specific accounting standard.
- the requirement to lodge audited accounts needs to be reconsidered for small NFP organisations.
- a plain-language guide summarising the provisions/obligations relevant to NFP companies (along the lines of the Small Business Guide contained as Part 1.5 of the *Corporations Act 2001* (Cth) should be available.
- all NFP companies should be required to have an objects clause and the directors should have a duty to pursue those objects.
- all NFP companies should be required to have a 'non-distribution' clause.
- the remedies available for a breach of the objects clause need to be clarified and strengthened.

### Future NFP legal structures

It is our recommendation that a national regulatory regime be implemented (see Chapter 4, Regulatory Framework). It would be appropriate at that time to reconsider the range of existing legal structures used by NFP organisations. This would be with a view to introducing a single specialist NFP legal structure. Whilst maintaining some level of choice is desirable, the current myriad of legal structures leads to confusion and inefficiencies in regulation. Consideration should be given to combining the best aspects of corporations law and the incorporated associations regimes. The work being done by the UK government would be useful to explore. Any new structure should meet the needs of both small and large NFP organisations, and the issue of converting from existing forms should be addressed in a simple and no-cost way.

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## 1. INTRODUCTION

This project considers the concepts of ‘accountability and corporate governance’ in the NFP context. It is our opinion that the related goals of improved accountability and good corporate governance must be supported by the underlying legal structure(s) adopted by NFP organisations. If the legal structure meets the needs of the organisation then it will be easier to build consistent and appropriate reporting obligations. In turn, these are the cornerstone of accountability. The current myriad of legal structures under which NFP organisations operate (incorporated association, company limited by guarantee, proprietary company, trust, cooperatives, Royal Charter, special Act of Parliament, aboriginal corporations) are confusing and hamper accountability.

A key research question has been ‘Is a company structure under the *Corporations Law* (in particular, a company limited by guarantee), a structure that meets the needs of NFP organisations and their stakeholders?’ This issue was considered to some extent by the 1995 Australian Industry Commission Report into Charitable Organisations. It recommended that a special form of incorporation under corporations’ legislation should be introduced for ‘community social welfare organisations’. The UK Strategy Report (2003) also recommended the establishment of two new types of company: the ‘Community Interest Company’ and the ‘Charitable Incorporated Organisation’ as discussed under Heading 5.2.<sup>1</sup> On 4 December 2003 the UK government released draft legislation, the *Companies (Audit, Investigations And Community Enterprise) Bill*,<sup>2</sup> which if enacted, would make the Community Interest Company proposal part of company law.

## 2. SURVEY QUESTIONS - CHOICE OF STRUCTURE

Part B of the survey form was headed ‘Legal Structure’. The questions under this Heading related to the choice of structure and whether or not the respondent was part of a group structure.

### 2.1. Factors behind choice of company structure

#### 2.1.1. SURVEY QUESTION

4.1 Please indicate how important the following reasons were for choosing a company as the form of incorporated legal structure rather than, for example, an incorporated association or cooperative?

(indicate your response by circling one number - numbers ‘1’ and ‘4’ both represent very definite positions, the numbers in between represent intermediate positions.)

**(1) not at all important, (4) very important, (0) don’t know**

- requirement of grant maker	1	2	3	4	0
- organisation’s size	1	2	3	4	0
- national or multi-state organisation	1	2	3	4	0
- public perception and status	1	2	3	4	0
- taxation / financial advice received at the time	1	2	3	4	0
- legal advice received at the time	1	2	3	4	0

Note: All references in this Report to small and large organisations or companies are based on the definition of “small” and “large” (proprietary companies) as contained in s 45A of the *Corporations Act 2001* (Cth), unless detailed otherwise.

<sup>1</sup> Charities and Not-for-Profits: A Modern Legal Framework. The Government’s response to ‘Private Action, Public Benefit’, Home Office, July 2003, p. 15. The ‘Private Action, Public Benefit’ report also recommended an additional legal form called the Charitable Incorporated Organisation, which would be available only to charitable organisations. This recommendation was accepted by the government, although it will not become the compulsory form for charities wishing to establish themselves in a corporate form (p.17).

<sup>2</sup> See [http://www.dti.gov.uk/cld/companies\\_audit\\_etc\\_bill/](http://www.dti.gov.uk/cld/companies_audit_etc_bill/)

## Chapter 3 - Legal Structure

- scale of trading activities	1	2	3	4	0
- preferred to deal with Australian Securities and Investment Commission rather than State regulator	1	2	3	4	0
other important reasons ( <i>please specify</i> ) .....					
.....					
.....					

*Number of respondents = varied between 1433 – 1464 for each option*

### 2.1.2. BACKGROUND

There is an important historical context to bear in mind when considering the results for this survey question. Respondents in the sample include organisations established prior to the introduction of the incorporated associations' legislation (in Victoria, 1981). Ideally, we should have asked respondents to indicate if they were registered prior to 1980 in order to explore the extent to which the lack of an incorporated association option was relevant to their choice of structure.<sup>3</sup> Subsequent to the survey we requested information from ASIC about the number of companies limited by guarantee with a pre-1980 registration date. ASIC has informed us that 3413 (35%) of the 9817 registered companies limited by guarantee registered with ASIC as at 1 March 2002<sup>4</sup> were companies whose date of registration was 1 January 1980. This is a significant number.

The importance of this historical factor is also borne out by qualitative data collected in the survey. In the space for 'other important reasons', 87 respondents mentioned the lack of other options at the time of registration, see Heading 2.3.1. It is worth noting, therefore, that cost and organisational difficulties are factors likely to have prevented existing NFP companies from changing to the incorporated associations' regime.

In addition to not having the association option, there were three other historical reasons for choosing a company limited by guarantee as the legal structure. First, until 1982, a company limited by guarantee received preferential treatment. For example, they enjoyed exemptions from lodging changes to directors and annual reports. However, since 1982 these exemptions have been removed, though this may not have prompted existing companies limited by guarantee to change their legal structure.

Second, in some instances there has been legislation passed requiring organisations to transfer to the companies' regime. For example, in the 1980's the NSW government required all registered clubs to incorporate as companies limited by guarantee and no longer as cooperatives or associations. More recently, the Commonwealth has required all credit unions to transfer from the cooperatives regime.<sup>5</sup>

Third, it was fairly easy for a company limited by guarantee to obtain a name licence which was thought to give the company a 'halo' of respectability.<sup>6</sup> However, since 1991<sup>7</sup> all companies (even those holding a name licence) have been required to include their ACN on public documents.<sup>8</sup> This requirement has significantly eroded one of the main reasons for applying for a name licence,<sup>9</sup> namely that without such a licence potential donors may be discouraged because of an (incorrect) assumption that a company necessarily implies 'for-profit' motives.<sup>10</sup> If it can be said, therefore, that holding a name licence is not the incentive it was, why would an organisation choose (or continue) to be a company limited by guarantee?

<sup>3</sup> For the purpose of exploring this issue further, the author has requested information from ASIC on the percentage of companies limited by guarantee with pre-1980 registration dates. As at the date of writing, this information has not been provided.

<sup>4</sup> 1 March 2002 was the date used for the purposes of our survey.

<sup>5</sup> M. Lyons, *The Legal and Regulatory Environment of the Third Sector*, *Asian Journal of Public Management* forthcoming 2004 at p. 9.

<sup>6</sup> See M. McGregor-Lowndes & K. Levy, 'Name Licences: the Company Name You Have When You are Not Having a Commercial Company Name', 1996, 4 *Current Commercial Law* 12 and S. Woodward, 'Not-For-Profit Companies – Some Implications of Recent Corporate Law Reforms', 1999, 17 *C&SLJ* 390 at 393.

<sup>7</sup> Amendment to s 219(3) contained in Sch. 2 of the *Corporations Legislation Amendment Act 1991* (Cth).

<sup>8</sup> Australian company number: see *Corporations Act 2001* (Cth), s 153.

<sup>9</sup> See para. PS 50.4 of ASC (now ASIC) Policy Statement 50, Omission of 'Limited' from Company's Name, issued 29 March 1993.

<sup>10</sup> See Mc Gregor-Lowndes and Levy n. 6.

## 2.2. Quantitative survey results - reasons for choosing company limited by guarantee

Survey question 4.1 asked respondents to rank the importance of the various reasons a company structure was chosen as the legal structure, rather than, for example, an incorporated association or a cooperative. The factors stated in the question for selection were based on those that we believed (from experience and from consultations with others)<sup>11</sup> to be relevant considerations. Table 1 shows the reasons listed in the questionnaire and the percentage (in descending order of prevalence) of respondents who indicated that the reason was important. In order to see the significance of these results more easily, the 'don't know' group was removed and the results were collapsed to 'important' (3 and 4 on the scale) and 'not important' (1 and 2 on the scale).<sup>12</sup>

Table 1: Respondents' reasons for choosing company structure

<i>Reason why company structure chosen</i>	<i>Per cent of respondents who agreed was an important factor (in descending order of prevalence)</i>
legal advice received at the time	87
taxation/financial advice received at the time	71
public perception and status	52
scale of trading activities	40
organisation's size	39
national or multi-State organisation	34
requirement of grant maker	33
preferred to deal with ASIC rather than State regulator	31

For each of these factors, at least a third of the respondents thought they were 'important'. Perhaps not surprisingly, 87% of respondents indicated that 'legal advice received at the time' was an important factor and 71% indicated that 'taxation/financial advice received at the time' was important. We suggest that the other factors were probably factors taken into account by the legal and financial advisors. It is also interesting to note that more than half (52%) of respondents indicated 'public perception and status' was an important factor in the decision to use a company structure rather than an incorporated association. This supported anecdotal evidence that 'serious' or 'more sophisticated' NFP organisations use the *Corporations Act 2001* (Cth) rather than incorporated associations' legislation.

<sup>11</sup> The author sought the views of a range of advisors to NFP organisations, see Appendix 1, Methodology.

<sup>12</sup> The collapsed chart did not result in any distortion of the refined patterns. The 'don't know' option was given for this question because it was recognised that, unless the company was formed in fairly recent times and/or the CEO had been with the company for a long period, it would be too difficult/time consuming for a view to be expressed. As expected there was a significant 'don't know group' — it varied between the options, but was an average of 16%.

2.2.1. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Chose structure because 'required by grant maker'

Whilst Table 1 shows the overall ranking of reasons for choosing to become incorporated as a company limited by guarantee, this ranking was not true for all respondents.

Being 'required by a grant maker' to choose a company structure was a significantly more important factor for several types of organisation. Forty-five per cent of those receiving any government income said that 'requirement of grant maker' was 'important' or 'very important' compared with only 22% of those receiving no government income. Whilst we are unaware of any government funding agreements that require the company limited by guarantee structure, many funding agreements specify that an organisation must be 'incorporated' before receiving funds. This general requirement, combined with the results for 'public perception and status', may mean that government funding agreements are being *interpreted* as requiring a company limited by guarantee structure.

Other interesting results concerning the relative importance of the 'requirement of grant maker' in determining the choice of legal structure include:

- Community Services (41%), Education and Education Related organisations (45%) said 'requirement of grant maker' was important compared with the overall frequency for respondents of 33%. Other activity groups cited 'requirement of grant maker' as an important factor significantly less often - 15% of Religious organisations, 13% of Interest groups and 21% of Sport and Recreation groups. See Figure 1.
- Public-serving organisations were more likely to cite this as an important reason (43%) than member serving (25%). See Figure 2.
- Organisations with PBI status (42%) were more likely to cite this as an important reason than those without PBI status (30%). See Figure 2.

One respondent wrote that the reason was a combination of factors:

Substantial assets and construction contracts - corporate reporting requirements give comfort to government and grant makers.

Figure 1: 'Requirement of grant maker', based on principal activity

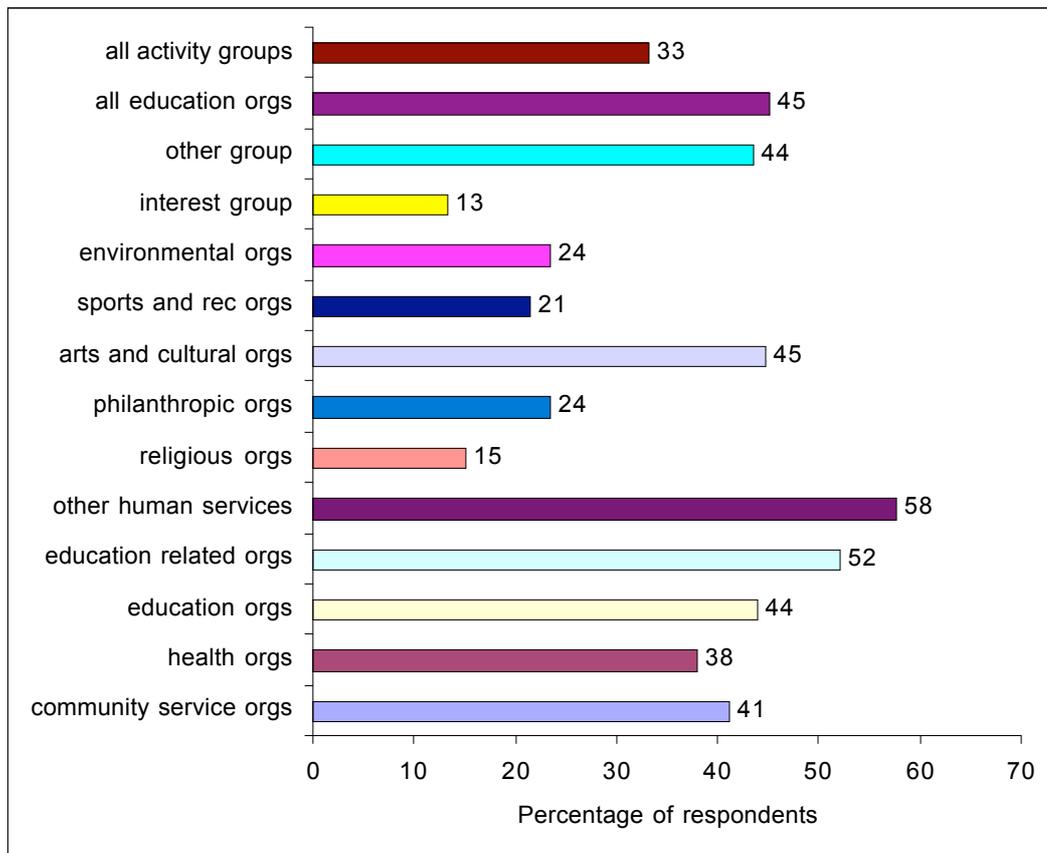
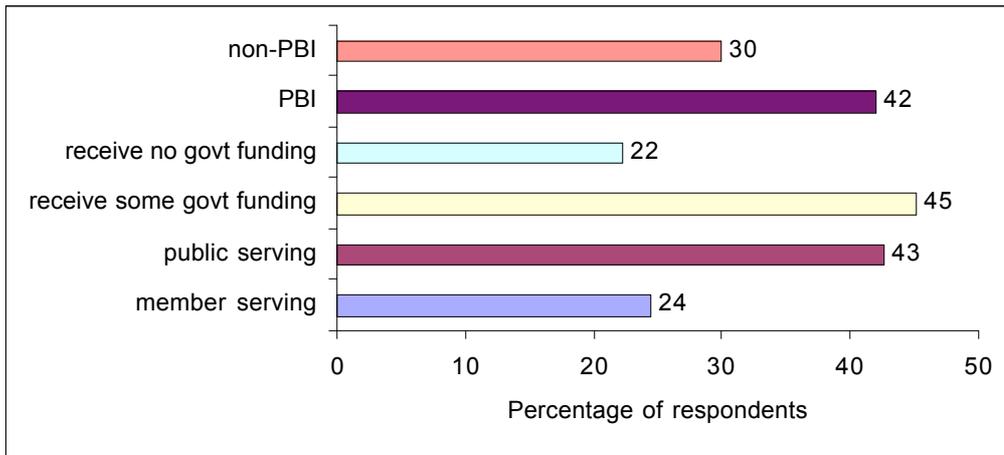


Figure 2: 'Requirement of grant maker', based on key indicators

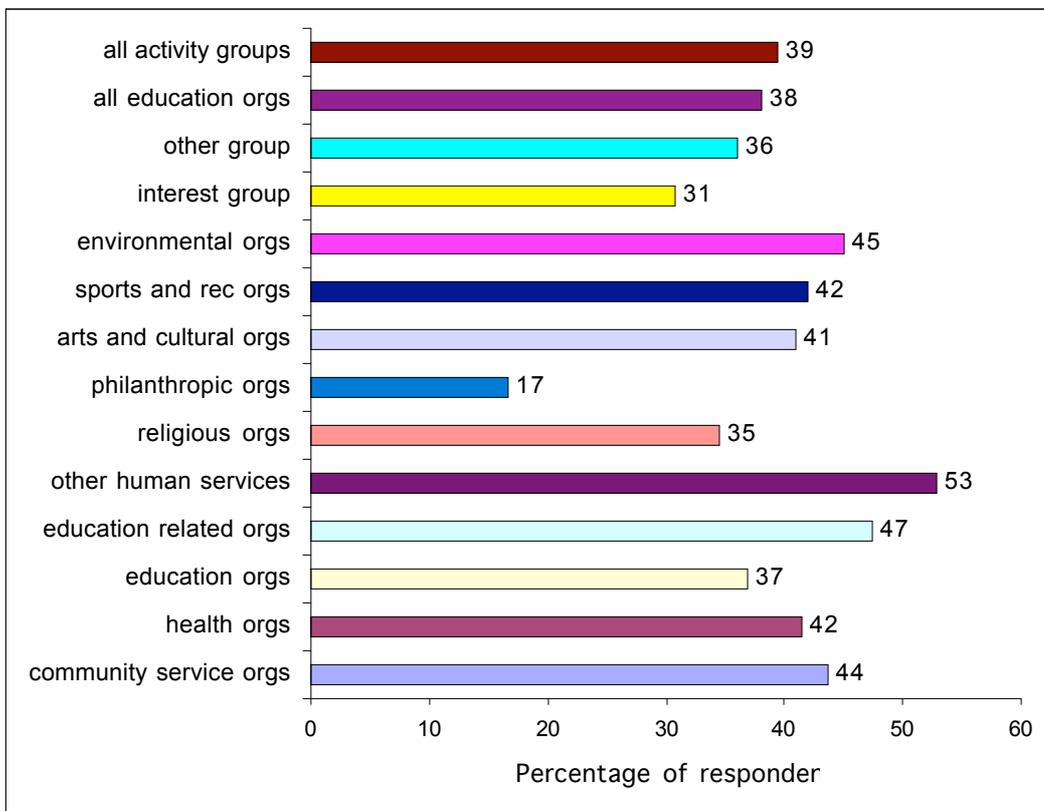


Chose structure because of 'organisation's size'

Respondents from Other Human Services organisations were more likely than other activity groups to mention organisational size as an important factor in their choice of legal structure (53% vs 39%). This is an interesting result, as Other Human Services are not, on average, the largest NFP companies.<sup>13</sup> In contrast, it was not a commonly mentioned factor for Philanthropic respondents (17% vs 39% for all activity groups).

As might be expected, large organisations are significantly more likely to cite organisational size as a reason for choosing the company structure than small organisations (58% vs 37%).

Figure 3: 'Organisation's size', based on principal activity



<sup>13</sup> Health organisations, Community Service organisations and Education organisations have, on average, greater income and assets compared with Other Human Services (see Profile Data chapter).

Chose structure because 'national or multi-state organisation'

Almost 69% of Interest Groups said that being a 'national or multi-state organisations' was an important reason for incorporating as a company limited by guarantee. This was more than for any other activity group. Many organisations with this profile are peak bodies - labour bodies, professional bodies and representative organisations that operate on a national/multi-State basis.

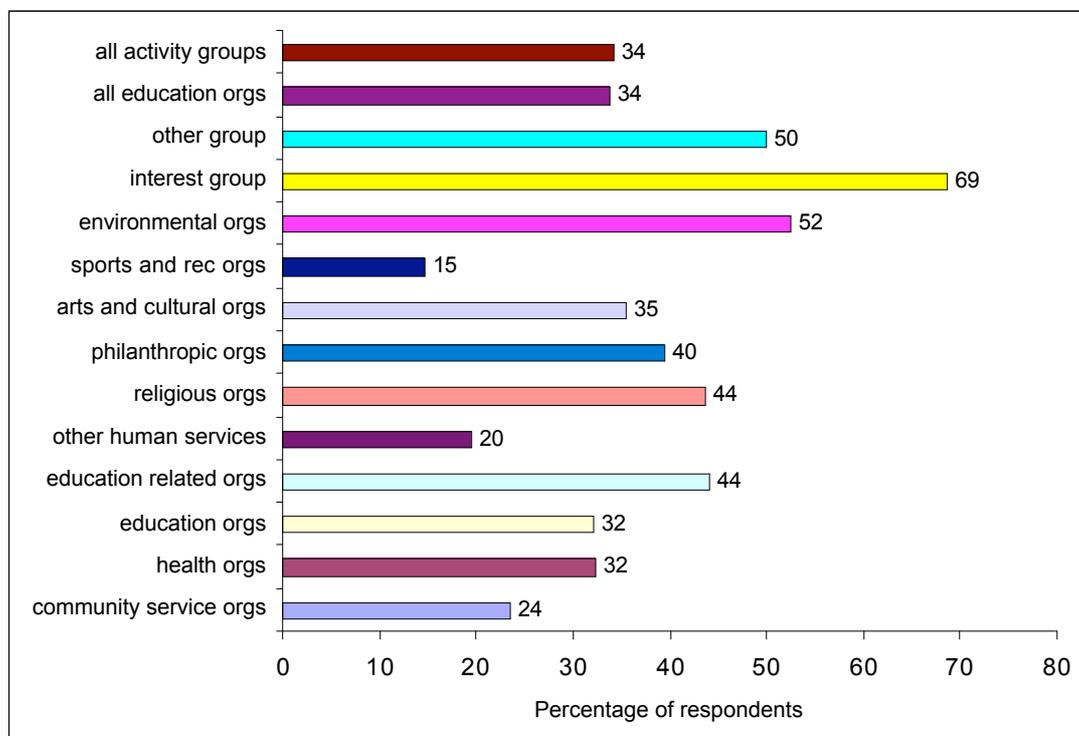
NFP organisations that carry on, or hope in time to carry on, operations in more than one jurisdiction, face a difficult dilemma. To take advantage of the associations incorporations legislation, (which is said to be specifically designed to meet the goals of simplicity and inexpensiveness), it will have to register a separate association in each State and/or Territory it wants to operate in. This will involve duplicating fees, ongoing paperwork and complexity because of a need to appreciate and keep abreast of the variations (even if only in minor detail) between legislation in the respective States and Territories. (The time and difficulty it took to prepare the comparative table in Appendix 5, even by an academic highly experienced in the area, has been practical testament to us of this fact.)

Aside from registration as a company under the *Corporations Act 2001* (Cth), the only other option for such an organisation is to register as an association in one State and then, if it 'carries on business' in another State or Territory, also register in that jurisdiction as a Registrable Australian Body under Part 5B.2 of the *Corporations Act*. Again, this involves extra time, expense and paperwork. This course also involves many uncertainties, especially about the scope of the concept of 'carrying on business' and how this concept applies to a NFP organisation. A breach for failing to register as such a body under the *Corporations Act* may occur quite inadvertently if, for example, a committee member moves to a different jurisdiction and takes part of the association's administrative structure with them.<sup>14</sup>

Several activity groups, including Interest Groups, Environmental organisations (53%) and Other Groups (50%), cite this as an important factor. In contrast, only 15% of Sports and Recreation organisations selected this as an important reason. We suggest that this is because they are more often only based in one State.

Interestingly, small organisations (36%) and those not receiving government funding (37%) were likely to cite this as a reason for choosing to be a company limited by guarantee rather than large organisations (22%) and organisations receiving government funding (31%). This is possibly because the larger organisations (Health, Education and Community Services) are often only located in one State and less often have related bodies.

Figure 4: 'National or multi-State organisation', based principal activity



<sup>14</sup> S. Sievers, 'Incorporation of Non-Profit Associations: The Way Ahead?' 18 *C&SLJ* 311-25 at p. 319.

**Chose structure because of 'public perception and status'**

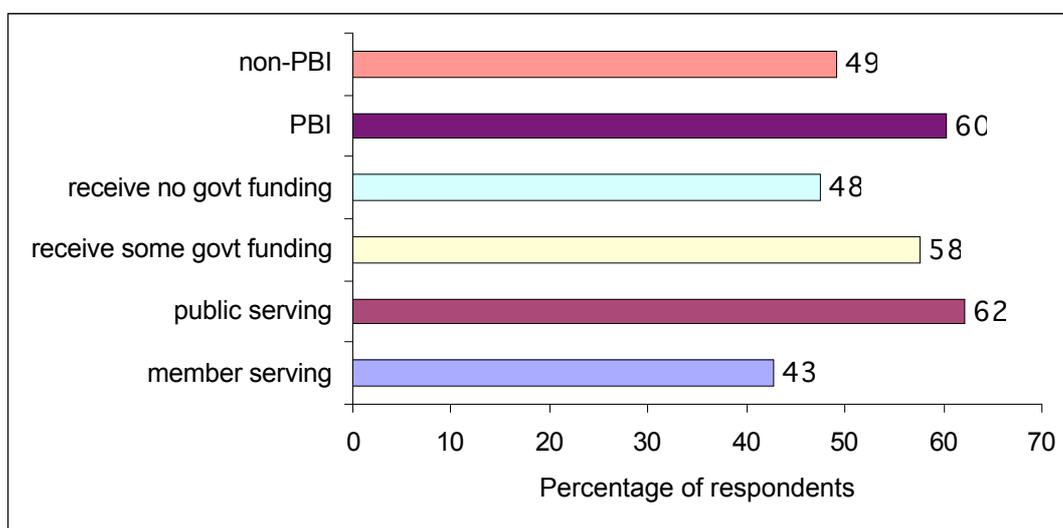
There was little difference between small and large organisations in this respect. However, those organisations receiving government funding were more likely than those that do not to cite public perception and status as an important reason (58% vs 48%). This is interesting given that there is a correlation between size and receipt of government funding

There was also a large difference between member-serving organisations and public-serving organisations. Twenty per cent more public-serving organisations than member-serving organisations thought this was an important reason for choosing this legal structure. As there is a strong correlation between public-serving organisations and PBI status, it is not surprising that there is also a difference between those respondents with PBI status and those without (a difference of 11%).

Sixty per cent of Community Services organisations and 67% of Arts and Cultural organisations also said this was an important reason for choosing the structure - considerably more than overall (52%).

We cross-tabulated the holding of a name licence<sup>15</sup> with this factor to see if those that held a name licence were more likely to cite 'public perception and status' as an important factor. There was a weak yet discernible relationship between the two variables (57% of respondents who *do* hold a name licence chose to incorporate because public perception and status is important vs 50% of respondents who *do not* hold a name licence and who chose to incorporate because public perception and status is important).<sup>16</sup> This was not as significant as we had predicted.

**Figure 5: 'Public perception and status', based on key indicators**



**Chose structure because of 'legal/taxation/financial advice received at the time'**

There was only one significant difference between respondents in relation to either 'legal advice received at the time or 'taxation/financial advice' received at the time as an important reason for choosing the legal structure. Philanthropic organisations were the only noticeable exception. Ninety-one per cent of Philanthropic organisations said that taxation/financial advice was an important reason, much higher than the overall figure of 70%. Again 96% of Philanthropic bodies said that legal advice was an important reason, again, higher than the overall figure of 87%. Advice sought from Philanthropy Australia suggests these results may be because this group is accustomed to approaching specialists for advice. Many philanthropic organisations are created by people/companies in high income brackets who (1) are more likely to have access to legal and financial advice, and (2) will be motivated at least in part, by a desire to maximise income tax benefits.

<sup>15</sup> See Chapter 2, Profile Data. Twenty-five per cent said that they held a name licence.

<sup>16</sup> The significant 'don't know' group to the name licence question were excluded from this cross-tabulation. Assuming that at least some of this group do, in fact, hold a name licence the relationship between the two variables could be stronger.

### Chose structure because of scale of trading activities

Sports and Recreation organisations (51%) were much more likely than other organisations to cite this as a reason (51% vs 40% overall), as were 'large' organisations (54% vs 40%). Presumably, this is because both of these groups have (or hope to have) more extensive trading activities than other organisations. In contrast, Philanthropic organisations and Religious organisations were far less likely to cite the scale of trading activities as a reason for choosing to incorporate as a company limited by guarantee (23% and 24% respectively vs 40% overall).

### 2.3. Qualitative survey results - reasons for choosing company limited by guarantee

Two hundred and twenty-two respondents commented in the space provided at the end of question 4.2. These were analysed and coded and Figure 6 summarises the results. Each category is discussed in the subsequent sections.

#### 2.3.1. INCORPORATED ASSOCIATION NOT AN OPTION AT THE TIME OF INCORPORATION

Of these 222 responses, 87 wrote that it was because there was no other option for NFP organisations that wanted to incorporate at the time. This sentiment is summarised by the following comment:

At the time of incorporation, Incorporated Associations Acts did not exist, and no-profit-sharing company limited by guarantee was the only known structure.

#### 2.3.2. LEGISLATIVE OR GOVERNMENT REQUIREMENT

Sixty-one respondents commented that they had chosen the legal structure due to legislative or government requirements. Specific legislative requirements mentioned included the *Registered Clubs Act 1976* (NSW) and the *Aged Care Act 1997* (Cth). Some legislation requires the organisation to incorporate/register as 'a company'. But other provisions only require the organisation to be a 'body corporate', which leaves open the incorporated association option. We are unaware of any legislation that specifically requires registration as a company limited by guarantee.

#### 2.3.3. PREFERABLE REGIME/GREATER FLEXIBILITY

Thirty-five respondents reported that the company limited by guarantee structure provided them with greater flexibility and that the corporations law regime was preferable to other options. This supports anecdotal evidence that some organisations have had difficulty incorporating as an association if their structures or constitution differs significantly from the model rules contained in the incorporated associations legislation.

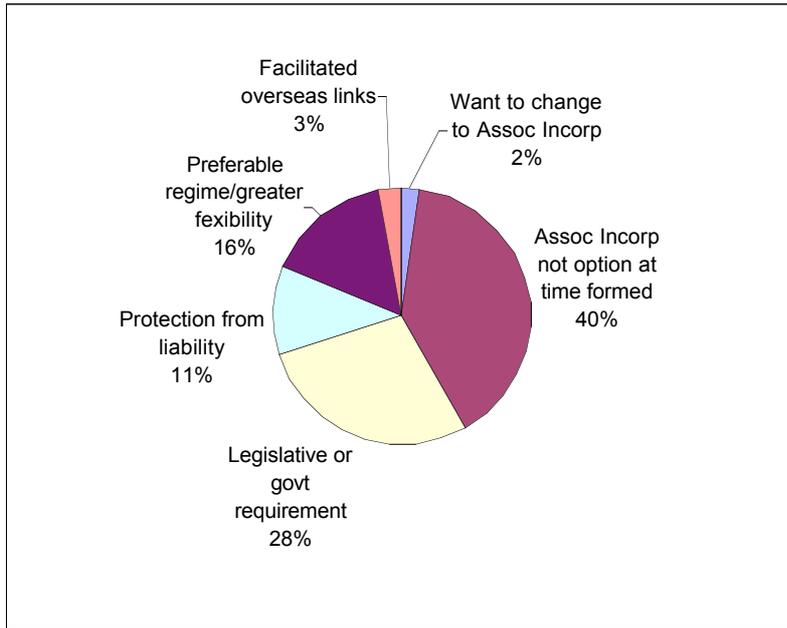
Respondents receiving government funding were much more likely to have this view.

#### 2.3.4. OVERSEAS LINKS

Six respondents commented that the company structure facilitated overseas links.

As organisations follow the general trend towards globalisation and expand across international borders, or form relationships with like organisations overseas, this may become an increasingly important reason for choosing the company limited by guarantee structure. The familiarity of the structure for overseas organisations - compared with the more unusual incorporated associations structure - may make it attractive for international organisations. A comparative study of NFP structures in different countries is an area for further research.

Figure 6: Additional comments made concerning choice of structure (n = 222)



## 2.4. Success of company structure?

### 2.4.1. SURVEY QUESTION

4.2 From your experience with this company, would you say that the choice of this form of legal structure (that is, a company):

(1) strongly disagree, (4) strongly agree, (0) can't say

- has caused difficulties 1 2 3 4 0
- is readily understood by the company's directors 1 2 3 4 0
- is readily understood by the company's members 1 2 3 4 0
- is readily understood by those dealing with the company (such as funding bodies) 1 2 3 4 0
- has added significant expense 1 2 3 4 0
- involves manageable reporting obligations to members and the Australian Securities and Investments Commission 1 2 3 4 0
- has been sufficiently flexible to meet the organisation's needs over time (for example, if a merger has been necessary) 1 2 3 4 0
- has added a lot of paperwork. 1 2 3 4 0

Other comments.....  
 .....  
 .....  
 .....

Number of respondents = varied between 1571–1609 for each option

## 2.5. Quantitative survey results - success of legal structure

Table 2 shows the results to survey question 4.2. Again the 'can't say' responses were excluded and the results were collapsed to 'agree' and 'disagree'.<sup>17</sup>

Table 2: Success of company structure

<i>Positive questions about company structure</i>	<i>Negative questions about company structure</i>
<ul style="list-style-type: none"> <li>is readily understood by the company's directors <i>majority (73%) agreed</i></li> </ul>	<ul style="list-style-type: none"> <li>has caused difficulties <i>majority (76%) disagreed</i></li> </ul>
<ul style="list-style-type: none"> <li>is readily understood by the company's members <i>majority (57%) agreed</i></li> </ul>	<ul style="list-style-type: none"> <li>has added significant expense <i>majority (59%) disagreed</i></li> </ul>
<ul style="list-style-type: none"> <li>is readily understood by those dealing with the company (such as funding bodies) <i>majority (73%) agreed</i></li> </ul>	<ul style="list-style-type: none"> <li>has added a lot of paperwork <i>majority (51%) agreed</i></li> </ul>
<ul style="list-style-type: none"> <li>involves manageable reporting obligations to members and ASIC <i>majority (76%) agreed</i></li> </ul>	
<ul style="list-style-type: none"> <li>has been sufficiently flexible to meet the organisation's needs over time (for example, if a merger has been necessary) <i>majority (72%) agreed</i></li> </ul>	

There was no clear evidence of any overall dissatisfaction with the structure. The dissatisfaction expressed was about the expense<sup>18</sup> (41% believe that a company structure had 'added significant expense') and the paperwork (51% believe it had 'added a lot of paperwork'). About three-quarters (73%) of the respondents believe that the company structure is well understood by directors and those dealing with the company and that it has been a flexible structure with manageable reporting obligations. However, only just over half (57%) thought that it was 'well understood by members'.

### 2.5.1. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

#### Has caused difficulties

Overall, only 24% of respondents said that the company limited by guarantee structure had caused difficulties. However, there were quite significant differences between large organisations and small organisations (11% difference) and a related difference between those organisations receiving government funding and those receiving none (7% difference). Whilst the proportion of small organisations that thought the structure had caused difficulties was still quite low (only 26%), the difference between small and large organisations suggests that the structure is considered to be more suitable for large organisations, despite the fact that most NFP organisations are not particularly large by 'top 100' business standards.

<sup>17</sup> The collapsed chart did not result in any distortion of the refined patterns. The 'can't say' group were 7% or less, except for 'is readily understood by those dealing with the company' (18% 'can't say') and 'has been sufficiently flexible to meet the organisation's needs over time' (25%).

<sup>18</sup> For a comparison between modes of incorporation and costs see K. Fletcher, 'Developing Appropriate Organisational Structures for Non-profit Associations' in M. McGregor-Lowndes, K. Fletcher, A.S. Sievers (eds), *Legal Issues for Non-Profit Associations*, LBC Information Services, 1996, p. 1, especially pp. 9–10.

A significantly higher number of Religious organisations said that the structure had caused difficulties (36% vs 24% overall). This is reflected in the high proportion of written comments concerning problems with the structure that were made by Religious organisations. We did get some anecdotal feedback that the company law model creates problems for Religious organisations when it comes to classifying stipends.

### Is readily understood by the company directors

Overall, 73% of respondents said that the legal structure was readily understood by the directors. Large organisations were more likely to say that it was understood by the directors - 81%. This may be because large organisations are more able to attract people with experience on corporate Boards, who understand corporations law requirements of directors.

### Is readily understood by the company's members

Only just over half (57%) of all respondents, said that the company's members readily understand the company structure. This raises a significant query over the effectiveness of members' remedies as a mechanism for ensuring accountability, particularly by directors.<sup>19</sup> In the NFP context other accountability mechanisms such as stock exchange regulation, dividends/returns to members and the influence of institutional investors do not apply. Falling back on members to take action must be a concern in view of the data showing that respondents believe that almost half do not readily understand the organisation's legal structure. This data also supports the discussion in Chapter 7, Stakeholders, that the remedies open to members of NFP companies need to be clarified and in some respects, to be strengthened.

Within the overall response of 56%, there was, once again, a significant difference between small organisations and large organisations. Significantly more respondents from large organisations said that the members readily understood the structure (70% vs 57% overall and 55% for small organisations).

### Is readily understood by funding bodies

Overall, there were high levels of confidence in the understanding by funding bodies of the company legal structure. This confidence was higher for those organisations receiving government funding (78%) than those that do not (68%).

Eighty-five per cent of Arts and Cultural respondents also said that funding bodies readily understood the legal structure. This may be due to the nature of the funding bodies that donate to Arts and Cultural organisations.

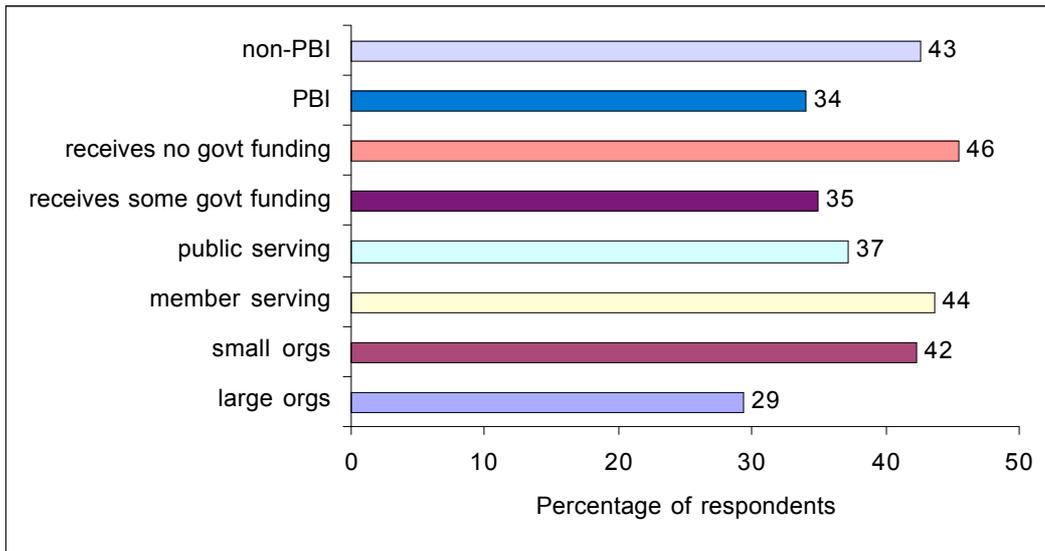
### Has added significant expense

Overall 41% of respondents thought the legal structure had added significant expense to their organisation. This figure was slightly higher for small organisations (42%) and, predictably, much lower (29%) for large' organisations. Public-serving organisations were also less likely to think that the legal structure had added significant expense. This may be because public-serving organisations believe that, on balance, the cost of more rigorous regulation is worthwhile. More than half of Religious organisations (55%), which are generally member-serving organisations, said that the legal structure had added significant expense.

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<sup>19</sup> Alternatively, it may simply mean that CEOs (who made up the bulk of the respondents) do not have confidence in their membership in this respect.

Figure 7: Legal structure has added significant expense, based on key indicators

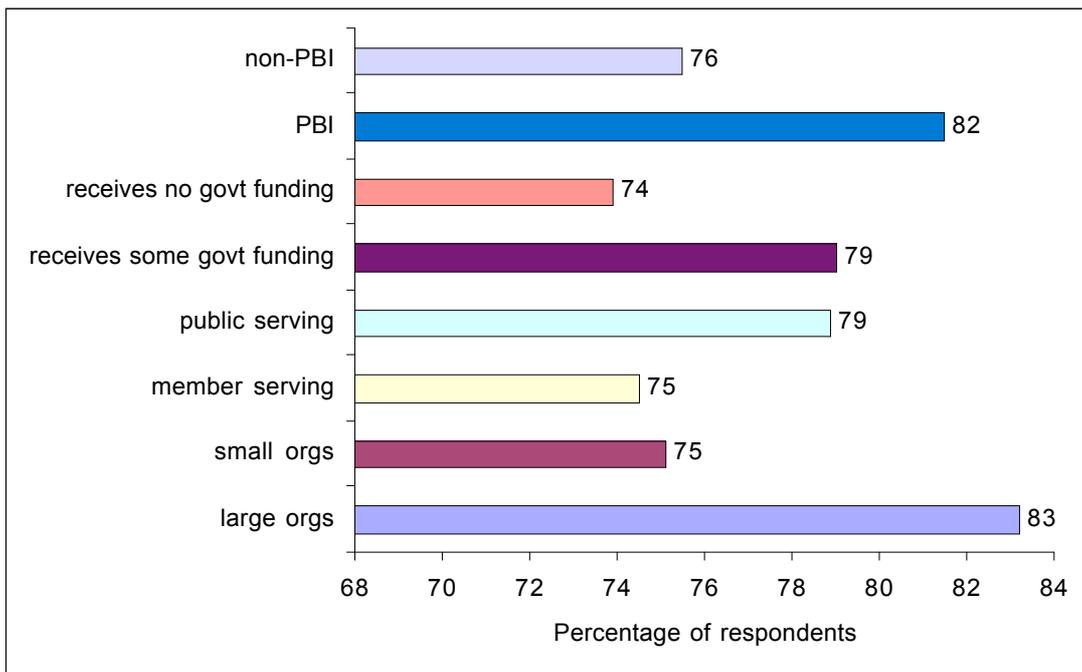


**Involves manageable reporting obligations to members and ASIC**

Overall, the great majority of respondents (76%) said that the legal structure involved manageable reporting obligations to members and to ASIC. This is an interesting result given that the results for other survey questions concerning what should be reported, indicated that very often respondents did not think that what is currently required should be included in any revised regime (see in Chapter 8, Disclosure).

Once again, there were divisions between small and large organisations (8% difference), those receiving government funding and those that do not (5% difference), public-serving vs member-serving (4% difference) and those with PBI status and those without (6% difference). It is clear that larger organisations receiving government funding and benefit from current taxation regimes, find navigating ASIC and meeting the disclosure obligations easier than smaller organisations.

Figure 8: Involves manageable reporting obligations to members and ASIC, based on key indicators



**Legal structure has been sufficiently flexible to meet the organisation’s needs**

There was very high approval of the flexibility that the legal structure gives to NFP organisations —overall 72% of all respondents thought the legal structure had been sufficiently flexible to meet the organisation’s needs. Some groups of respondents did not feel quite as positive about the flexibility: 69% of member-serving organisations said that it was sufficiently flexible, and 65% of Sports and Recreation organisations said that it was sufficiently flexible. Although these figures are slightly lower than the overall figure, they still demonstrate relatively high levels of approval.

This data complements anecdotal evidence that many NFP organisations find the application of incorporated associations legislation inflexible, and for this reason, chose to register as companies.

**Has added a lot of paperwork**

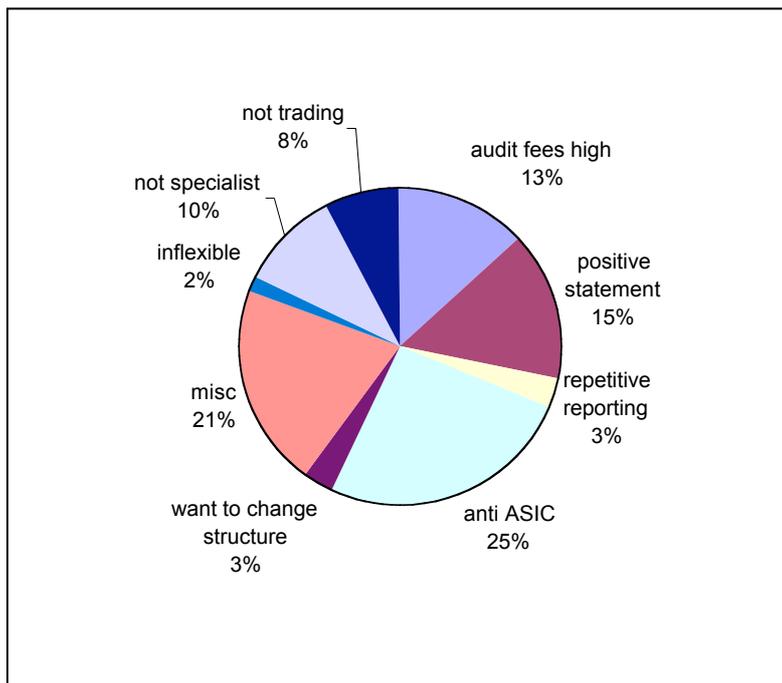
Overall, just over half (51%) of respondents said that the structure had added a lot of paperwork. Reflecting the fact that member-serving organisations were more likely than public-serving organisations to hold this opinion (54% vs 47%), 57% of Sports and Recreation groups and 68% of Religious organisations said that the structure had added a lot of paperwork.

Only 35% of Human Services organisations said that the structure had added paperwork. This reflects, perhaps, their acceptance of high levels of accountability and the fact that, in comparison with the level of accountability required of them by funding bodies and other statutory regimes, the disclosure required to ASIC is minimal.

**2.6. Qualitative survey results - success of company legal structure**

One hundred and thirty four respondents wrote a comment in the space provided at the end of question 4.2. These comments were analysed and coded and Figure 9 summarises the results. Each category is discussed in the subsequent sections.

**Figure 9: Comments re success of structure (n = 134)**



**2.6.1. ANTI-ASIC: DEADLINES AND FINES**

Around 25% (n=34) of those respondents commenting on the success of the legal structure complained about problems with ASIC, not with the structure itself.

Some companies objected to having to provide the same disclosure as large, ‘for-profit’ companies. For example, one Religious organisation objected that:

ASIC requirement are better for large companies but are inappropriate and wasteful and cumbersome for us.

## Chapter 3 - Legal Structure

Likewise, a Business or Professional Interest Group organisation said:

The reporting requirements to ASIC seem quite unnecessary for a Not-for-Profit. ASIC does not give much consideration to volunteer run organisations, where we often cannot meet their deadlines.

Another Business or Professional Interest Group organisation said:

ASIC are inhuman!

### 2.6.2. NON SPECIALIST NFP STRUCTURE

Fourteen respondents said that the problem with the legal structure stems from the fact that it is not specially designed for NFP organisations.

A medium-to-large Religious organisation with an income of between \$1mil and \$5mil strongly agreed that the company structure 'had added a lot of paperwork'. The comment suggests, though, that they might find this amount of 'paperwork' acceptable if the reporting requirements were more relevant to the needs of the organisation:

The requirements of the Act and the applicable (and ever changing) Accounting Standards are largely irrelevant to meaningful reporting by the company to its members and the board.

A very large organisation (income of \$10mil or more), which provides a range of community, health and education services complained, not so much about the extra costs of compliance, but more about their lack of relevance:

Compliance with Accounting Standards developed for Corporations Law written to protect owners does not allow true provision of important information to major stakeholders.

### 2.6.3. WANT TO CHANGE BUT TOO EXPENSIVE

Four organisations reported wanting to change from being a company limited by guarantee, but could not due to the legal costs involved or because of perceptions about their legal status.

The comments of one Religious organisation demonstrate that there can be difficulties in migrating from the *Corporations Act 2001* (Cth) regime to an incorporated associations Acts:

We want to cease being a company but (apparently) can only do this by ceasing to trade or having less than \$1000 in assets.

Other organisations, like this Pre-school, simply find the cost of changing legal structures too high:

Would change legal status from company limited by guarantee to incorporated association but legal quote is in the 1000s of dollars.

### 2.6.4. REPETITIVE REPORTING

Four organisations complained about the duplication of reporting to various agencies and reporting bodies. For example, one medium-sized Disability Services organisation wrote:

Difficulties arise with repetitive explanations of status, eg Funders, Suppliers, Government Agencies, etc.

### 2.6.5. POSITIVE STATEMENTS

Not all organisations wrote negative comments. Twenty organisations wrote positive statements about the legal structure itself, the reporting requirements and their dealings with ASIC.

A small Industry Association commented that:

Filing and paperwork of no real problem as ASIC are contactable (by phone) and very helpful with advice and assistance.

An Education Related organisation said:

It has been a good arrangement, with minimal paperwork.

A small Community Services organisation responded:

I like the fact that we are accountable and though the yearly audit is expensive, it is a good thing to do because if mistakes are made they are found quickly.

This comment came from a respondent who disagreed that the legal structure 'has added a lot of paperwork':

Our annual audit involves assembling and compiling data from over 50 bank accounts of projects and offices around the country. Experience and in-house training has helped a lot.

A Religious organisation providing community and health services, with between 20–50 employees and between \$500,000–\$1mil in income said:

'We believe the reporting obligations to the ASIC are extremely important. There can be no credibility without accountability.'

**2.6.6. AUDIT FEES EXPENSIVE/COMPLIANCE COSTS HIGH**

Eighteen organisations complained about the costs of audits and compliance with the *Corporations Act 2001* (Cth) in their comments. The following comments concerning the costs of audits demonstrate that the cost of auditing can be over 10% of an organisation's annual income.

A Sports and Recreation organisation with income of less than \$100,000 said:

For a small organisation the audit requirement is expensive and onerous. Cost \$9300 last year. The fines are also an important fee for a voluntary organisation when non-compliance occurs, as it often does.

A museum with income of less than \$10,000 said:

Audit fees are over \$1200 due to the necessity of a legal 'registered company auditor' not your 'friendly accountant' who will audit for free!!!!

Another respondent, a Community Services organisation with an income under \$10,000 agreed that Audit costs are too high:

Cost of audited returns each year is ridiculous, eg \$1200.

Most would agree that spending over 10% of income on auditors' fees is excessive, and would be difficult to justify to both members and donors. It often is recommended that donors look for organisations that keep their administration fees below 10%. Yet organisations of this size have already spent over 10% on administration fees before they have even begun to administer their core activities.

Along these lines, a Sport organisation with an income between \$100,000–\$500,000, who strongly agreed that the choice of legal structure had 'added significant expense', suggested that the disclosure requirements were a distraction from the core activities of the organisation:

In an organisation (sporting) where members primarily want to play their sport some administrative duties are quite onerous.

A Professional Interest Group with an income between \$500–\$10,000 said that becoming a company limited by guarantee had certain pitfalls:

It added a compulsory audit which is unnecessary for the company's need and the members need.

A Primary School observed that as long as accountants were willing to provide their time as a volunteer, compliance costs could be kept down:

Relatively cheap to administer if you have volunteer accountant - much more costly if you need to hire advice - accountant/auditor \$150–\$500 per hour.

All of these comments highlight the need to balance the goals of accountability and transparency from organisations that are dealing with public money, against the negative effects of high administrative and time costs.

## 3. GROUP STRUCTURES

### 3.1. Survey question

5.1 Does the company have any subsidiary companies or related entities? (Note: for the purposes of this question, a division within the company is not a related entity).

- yes
- no

*Number of respondents = 1667*

If 'yes', please indicate the number of each type:

1. ....proprietary limited company (Pty Ltd)

Number of respondents = 59

2. ....public company (Ltd)

Number of respondents = 59

3. ....trust/foundation

Number of respondents = 83

4. ....parent company

Number of respondents = 12

5. ....other (please specify) .....

### 3.2. Survey results

While group structures are par for the course in listed public companies and even in medium-size businesses, they were uncommon among NFP companies. The data showed that only 14% were part of a group structure and, even within that 14%, the majority only had one or two related entities (for example, one proprietary company or one foundation). Further, 74% of respondents only had individuals as members and not all peak bodies had organisations as members.

### 3.3. Significant differences between respondents

Cross-tabulation of the results revealed the following differences between organisations:

- Large organisations were significantly more likely than small organisations to have a subsidiary or related entity (28% vs 12%).
- Philanthropic bodies were most likely to be part of a group structure (29%). Eighty-six per cent of those were trusts or foundations. This is not a surprising result as it is prudent to have a company as the trustee to protect individuals from liability and to have a separate legal entity in whose name the trust assets can be placed.
- Sports and Recreation organisations were least likely (5%) to be part of group structures.

## 4. IMPLICATIONS FOR INCORPORATED ASSOCIATIONS' REGIME

While the survey did not cover incorporated associations, there are certain findings that are relevant to reflect on after more than a decade of this regime.

### 4.1. National and multi-state organisations

Thirty-five per cent of respondents indicated that being a 'national or multi-State organisation' was an important factor in their choice of a company structure. This was particularly so for small organisations, that is, organisations that can be assumed might otherwise have been better suited to the cheaper incorporated associations' regime. In addition, it is likely that this factor was very relevant to the advice given by legal and other advisors, even if not specifically identified by the respondent.<sup>20</sup>

This data confirms that the needs of small, but national or multi-state, NFP organisations are not being adequately met by the current incorporated associations' regime. It is also a particular problem for a federated body. We are aware of several organisations with a small national secretariat incorporated as a company limited by guarantee, but all their member State and Territory bodies are incorporated associations. This model increases administrative costs for those organisations. It also makes it difficult to produce educational NFP management material that caters for both the State/Federal regimes and for the variations between the States/Territories in

<sup>20</sup> See Heading 6.3.

their associations' legislation.<sup>21</sup> With increased use of technology such as email and internet, many organisations are better able to operate on a national basis. Therefore, this is an increasingly important issue for the States and Territories to consider.

## 4.2. Trading activities

Forty per cent of respondents indicated that the 'scale of trading activities' was an important factor, an area of debate and variation in the associations' regime.<sup>22</sup> This factor is likely to have been relevant to the advice given by legal and other advisors, even if not specifically identified by the respondent. Several respondents indicated in written comments that they would prefer to be an association but, because of the actual or likely scale of their trading activities, said they had decided, or had been directed by the relevant registrar, to incorporate as a company.<sup>23</sup>

## 4.3. Size

The *Review of the Associations Incorporated Act 1984 NSW Consultation Paper*<sup>24</sup> refers to larger associations as those with 'an annual turnover of \$250,000 or more'. In the consultation paper there is the suggestion that those NSW associations 'with turnover in excess of \$500,000' are required to incorporate as a company.<sup>25</sup> Under the s 45 of the *Corporations Act 2001* (Cth) definition, such an organisation would be regarded as small.<sup>26</sup> However, we would argue that most people participating in the NFP sector would think that an NFP organisation with, say, 45 employees, assets of \$4 million and revenue of \$9 million would be a large (or at least not a small) organisation, especially if it had a large volunteer base.

It is important to consider the implications of this definitional mismatch. If the NSW Department's Review results in associations that it regards as large being required to be registered under the *Corporations Act* rather than under the *Associations Incorporations Act* then it is worth noting that it will be possible for these organisations (those whose annual turnover is, say, in excess of \$500,000) to fall within the *Corporations Act* definition of small (which refers to revenue of \$10 million) if they registered as a small proprietary limited company.<sup>27</sup> In this event, certain company law disclosure and other requirements could be avoided. In particular, they would not be required by the *Corporations Act* to have their accounts audited or to lodge them with ASIC.<sup>28</sup>

A national regulatory regime for all incorporated NFP organisations within the auspices of the *Corporations Act* would enable the issue of graded reporting obligations (dependent for example on size) to be addressed. This would eliminate the ability of an organisation to avoid their reporting obligations merely on the basis of its legal structure and/or its place of incorporation/registration.

## 4.4. Regulator

Almost a third (31%) of respondents identified a preference for ASIC 'rather than State regulator' as an important factor, supporting anecdotal evidence that many of the State regulators are under resourced and cannot cope easily with organisations that want to have variations to the prescribed model rules.

<sup>21</sup> See this argument made by other academics: M. McGregor-Lowndes, 'Reforming Queensland's Incorporated Associations Legislation', 22 *The Queensland Lawyer*, pp. 9–19 and K. Fletcher, 'Incorporated Associations: Cheap Incorporation — Limited Choices' 22 *The Queensland Lawyer*, pp. 20–4.

<sup>22</sup> See A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand*, The Federation Press, 1996, para. 4.1.4.

<sup>23</sup> See Heading 1.2.1, Chose structure because of scale of trading activities.

<sup>24</sup> See *Review of the Associations Incorporations Act 1984 Consultation Paper*, April 2003, Office of Fair Trading, Department of Commerce, NSW, see p. 5.

<sup>25</sup> *Review of the Associations Incorporations Act 1984 Consultation Paper*, p. 10.

<sup>26</sup> The *Corporations Act 2001* (Cth) s 45A(2) states: 'A proprietary company is a small proprietary company for a financial year if it satisfies at least 2 of the following paragraphs: (a) the consolidated gross operating revenue for the financial year of the company and the entities it controls (if any) is less than \$10 million; (b) the value of the consolidated gross assets at the end of the financial year of the company and the entities it controls (if any) is less than \$5 million; (c) the company and the entities it controls (if any) have fewer than 50 employees at the end of the financial year.'

<sup>27</sup> There is no taxation or company law requirement that they register as a company limited by guarantee rather than a company limited by shares. In fact, we are aware of several NFP organisations that are registered as proprietary limited companies.

<sup>28</sup> They would not be required to lodge such accounts unless requested by ASIC (s 294 *Corporations Act 2001* (Cth)) or by the requisite number of members (s 293) or if they are controlled by a foreign owned company (s 292(2)(b)).

### 4.5. Public perception and status

'Public perception and status' was important to the majority of respondents (52%) and, as stated previously, supports anecdotal evidence that 'serious' or 'more sophisticated' NFP organisations are companies rather than incorporated associations.

## 5. SPECIALIST NFP STRUCTURE

### 5.1. Feedback received

Further data was obtained in May 2003 from participants at a conference of Chief Executive Officers of disability organisations who are members of the peak body ACROD (National Industry Association for Disability Services), where Ms Woodward was invited to deliver a presentation on the Project. Participants were asked to complete a brief feedback form for ACROD. From the 125 responses (out of about 140 who attended the session), the majority (68) were incorporated associations and 46 were companies limited by guarantee. Eighty-four per cent indicated that they were in favour of a new specialist NFP legal structure.

A very important point on this issue was made in email feedback we received from the President of a ski club who is also a lawyer:

I found your preliminary findings very interesting. The problem with most clubs is dealing with members who come and go. Small proprietary companies must still have less than 50 members. If the Club was to issue a new share each time a new member joined, the Club would rapidly exceed 50 members. The only other alternative is to have an existing [member] transfer his/her share. This may be difficult to organise at the time. Also the Club may not want shares traded. Frequently members just cease to respond to any correspondence and drop out. It is necessary to delete these members from the companies books to save money.

The *Associations Incorporation Act* is more practical when dealing with members but did not exist when many clubs were incorporated. A special company based on the *Associations Incorporation Act* with an easy transfer from the Clubs present structure would in my view be the way to go.

### 5.2. UK reforms

In September 2002 the Strategy Unit in the UK Government Cabinet Office produced a Report titled *Private Action, Public Benefit - A Review of Charities and the Wider Not-For-Profit Sector*. The Report recommends a new form of company structure called a Community Interest Company (the CIC Proposal). To quote from this interesting Report:

5.19 The company form is attractive to many social enterprises. Company law is well developed and companies are well understood by professionals such as bankers and lawyers. The company limited by guarantee form in particular is popular, and is used by some very large not-for-profit organisations such as BUPA, the private health provider.

5.20 Against the popularity and strong image of companies, however, must be balanced the fact that the companies legislation was not designed with the needs of smaller scale community-based social enterprises in mind. Problems include the fact that there is no entrenchment of the non-profit-distributing nature of the organisation, nor the devotion of assets to a public purpose; that the Company Limited by Guarantee does not allow access to equity; and that the company 'brand' is almost exclusively associated with profit-making.

5.21 This report therefore recommends the establishment of a Community Interest Company ('CIC'), drawing as appropriate on company law, but with certain additional constraints and features which make it suitable for use by small scale community-based not-for-profit social enterprises familiar with the company form.

The UK Report then outlines the key characteristics of the new form of company, the CIC:

- Protection of assets against distribution to members or shareholders.
- Ability to choose the limited by guarantee or by shares format, with full adherence to UK and European company law and guidelines, including rules on insolvency, accountancy, and governance.
- Ability to issue preference shares with a fixed rate of return (this applies to both the limited by guarantee and limited by shares models).

- Increased requirements in terms of transparency and accountability.
- A requirement to have a clause in the constitution setting out the objects of the company.
- A check at the point of registration that the objects of the organisation are in the public and community interest, with subsequent changes being subject to regulatory approval.

There was wide public consultation on the recommendations contained in this Report between September and 31 December 2002. In July 2003, the Home Office published a Report titled *Charities and Not-For-Profits: A Modern Legal Framework* as the Government's response to the Strategy Unit Report.<sup>29</sup> The Department of Trade has published (with the Treasury and Home Office) a series of documents about the CIC proposal. One of those documents summarises the responses received during the consultation period and of 114 responses received about the CIC proposal, 97 endorsed the recommendation.<sup>30</sup> On 4 December 2003 the UK government released draft legislation, the *Companies (Audit, Investigations And Community Enterprise) Bill*,<sup>31</sup> which if enacted, would make the Community Interest Company proposal part of company law.

### 5.3. Australian context

We believe that the UK Strategy Unit Proposals warrant serious consideration in the Australian context. The finance option of preference shares is novel and is designed to give NFPs the advantages of having some form of share capital as part of their overall financing mix. We agree with the requirement of having non-distribution and objects clauses. We argue that these should be required as a matter of company law rather than just as ATO practise for those with DGR status. However, not all aspects of the Report's recommendations about CICs are relevant to the Australian context. The Report also recommends a new form of legal structure called a Charitable Incorporated Organisation specifically for those organisations registered with the UK Charity Commission. This is intended as a legal structure to better meet the needs of charities, some of whom are not separately incorporated or who currently opt for incorporation as a company limited by guarantee or an industrial society. This distinction between registered charities and other NFPs does not operate in the same way in the Australian context.

Within the constraints of this Project we have not been able to analyse the UK reform proposals in any depth, or to look at other overseas models for NFP legal structures. However, while we continue to have a dual regulatory system of State/territory based incorporated associations and a national companies regime, it does not seem of any real benefit to consider seriously the introduction of yet another type of legal structure. The existing company limited by guarantee model could be reformed to take in some of the UK reforms, but where would this leave the vast majority of existing incorporated associations? In our view, the better approach is to pursue a single regulatory regime and, then (or at the same time) consider a revised structure that might take in some of the UK proposals. Options for a national regulatory framework are canvassed in Chapter 4, Regulatory Framework.

## 6. SMALL AND LARGE DICHOTOMY FOR NFPs

The regime of small and large proprietary companies was introduced primarily as a result of pressure from the business community to reduce and streamline the regulatory burden on small business. Consideration needs to be given to the position of small NFP organisations. The public policy argument for requiring disclosure from small NFPs is arguably greater than for small 'for-profit' companies because the majority of them enjoy (as a minimum) income tax exemption. However, there is a strong argument for tailoring the nature of what is disclosed and the fees payable to meet their different needs. It is not so much the extent of the disclosure, as its relevance and accessibility to the different stakeholders that NFP organisations serve, for example, the donating public, members and clients rather than shareholders. But to be effective as a mechanism for good corporate governance, disclosure needs to depend on considerations such as size, purpose and taxation status, NOT on jurisdiction and choice of legal structure.

<sup>29</sup> The Government's response to the Strategy Unit Report is available at <<http://www.homeoffice.gov.uk/>>.

<sup>30</sup> See *Views on Community Interest Companies* available at <<http://www.dti.gov.uk/cics/views.htm>>.

<sup>31</sup> See <[http://www.dti.gov.uk/cld/companies\\_audit\\_etc\\_bill/](http://www.dti.gov.uk/cld/companies_audit_etc_bill/)>

While there are many overarching provisions in the *Corporations Act 2001* (Cth) that should apply to all companies (particularly, directors' duties), the unique issues faced by NFP companies (some of which are described in this Report),<sup>32</sup> could be addressed in specialist provisions. A plain-language guide along the lines of the Small Business Guide could make an enormous difference. Capital reductions and share buy-back provisions have no relevance for NFP organisations, so why not make this clear? At the time that the incorporated associations' legislation was introduced, the simplification of requirements and filings for small business had not been introduced into the corporations' regime. The concept of replaceable rules under the *Corporations Act* is not dissimilar to that of model rules under the various State and Territory incorporated associations Acts. If there can be some replaceable rules that apply only to public companies, why could there not be some designed specifically for NFP bodies?

There is a strong argument for tailoring the nature of what is disclosed and the fees payable to meet their different needs.<sup>33</sup> It is not so much the extent of the disclosure, as its relevance and accessibility to the different stakeholders that NFP organisations serve, for example, the donating public, members and clients rather than shareholders.

### **Recommendation: Modify existing Corporations Act requirements**

While the existing company limited by guarantee structure has proved satisfactory in the main, some aspects need reform. These include:

- the fee structure should be revised to provide a sliding scale based on size
- information required for disclosure should be tailored to the needs of NFP stakeholders rather than to 'shareholders', and this needs to be supported by an NFP specific accounting standard
- the requirement to lodge audited accounts needs to be reconsidered for small NFP organisations
- a plain-language guide summarising the provisions/obligations relevant to NFP companies (along the lines of the Small Business Guide contained as Part 1.5 of the *Corporations Act 2001*(Cth)) should be available
- all NFP companies should be required to have an objects clause and the directors should have a duty to pursue those objects
- all NFP companies should be required to have a 'non-distribution' clause
- the remedies available for a breach of the objects clause need to be clarified and strengthened.

The latter three points (objects clauses, non-distribution clauses and remedies) are discussed in detail in Chapter 7, Stakeholders. It is worth noting that at Ms Woodward and Ms Marshall's presentation for Freehills<sup>34</sup> there was clear agreement from participants about:

- a compulsory non-distribution clause to prevent distributions of money or assets to members or related parties
- support for a plain-language guide for NFP companies
- support for a sliding scale of fees based on the size of the organisation.

### **Recommendation: Future NFP legal structures**

A national regulatory regime should be implemented. It would be appropriate at that time to reconsider the range of existing legal structures used by NFP organisations. This would be with a view to introducing a single, specialist NFP legal structure. Whilst maintaining some level of choice is desirable, the current myriad of legal structures leads to confusion and inefficiencies in regulation. Consideration should be given to combining the best aspects of the corporations law and the incorporated associations regimes. The work being done by the UK government would be useful to explore. Any new structure should meet the needs of both small and large NFP organisations, and the issue of converting from existing forms should be addressed in a simple and no-cost way.

<sup>32</sup> See Heading 2.3.

<sup>33</sup> See UK Report, n. 23.

<sup>34</sup> See Heading 6.1 Chapter 4, Regulatory Framework

## 7. CONCLUSION

There were several interesting findings about why a company limited by guarantee had been chosen as the legal structure. While a significant number were formed at a time when there was effectively no other option (and they have not subsequently chosen to transfer to the incorporated associations' regime), others have chosen the structure because of factors such as public perception and status, the scale of their trading activities and because they are a national or multi-State organisation. While the existing company limited by guarantee legal structure seems to be meeting the overall needs of many NFP organisations, there are many simple ways the structure could be improved within the current regulatory framework. For example, a plain-language guide for NFP users, a sliding fee scale based on size, and more relevant disclosure requirements. The desirability of requiring objects clauses and non-distribution clauses in the constitutions of all NFP companies has also been raised in this Chapter and, together with a discussion of remedies for members, is developed more fully in Chapter 7, Stakeholders.

On a more fundamental level, there are findings in this Chapter that support the need for a single, Commonwealth statutory regime in order to overcome the problems faced by the increasing number of NFP organisations that wish to operate on a national or multi-State basis (this recommendation is made in the following Chapter, Regulatory Framework). Our data (both from this Chapter and Chapter 1, Profile Data) also shows that it is not simply a matter of thinking that small NFPs should be incorporated as associations and large ones should be required to register as companies. If a national regulatory scheme were introduced for all NFP organisations, then it would be possible to bring together the best aspects of the company structure with those of the associations' regime (and possibly some new features) to introduce a single, specialist NFP legal structure.

## CHAPTER 4: REGULATORY FRAMEWORK

### *Who understands? Who can help?*

#### SUMMARY OF KEY FINDINGS IN THIS CHAPTER

##### ASIC's performance

- Overall there was dissatisfaction with ASIC's performance as a regulator of NFP companies. For example, 54% of respondents believe it is inaccessible to non-business people.
- Seventy per cent of respondents believe that the *Corporations Act 2001* (Cth) and the way it is implemented by ASIC is more appropriate to 'for-profit' than NFP companies.
- Given both these findings, it seems that dissatisfaction with ASIC is caused by ASIC not being a specialist regulator, rather than the way it carries out its role.

##### Introduction of a new regulator?

- The majority (54%) were in favour of implementing the Charity Definition Inquiry recommendation about the establishment of a new administrative body. This rises to three-quarters (74%) of respondents when the significant 'not sure' group (36%) are excluded.
- Written comments provided by those in the 'not sure' group indicate considerable concern that the introduction of a new regulator would simply increase the regulatory burden. Many wanted more information before expressing a view.

##### Role of a new regulator

- Survey data demonstrated a preference for combining both compliance (58%) and determination of charitable status (58%) with advice (86%), sector advocacy (69%) and training (56%). However, additional feedback suggests that this reflects a desire for increased assistance and support, rather than a well thought out preference for a single regulator body.
- Based on experience in the UK, we do not believe that all these roles should be combined in a regulator.

##### Recommendations

###### Single regulatory regime

- A single Commonwealth statutory regime should be introduced for all corporate bodies (that is, 'for-profit' companies, NFP companies and incorporated associations) by referrals of power from the States to the Commonwealth, along the lines of what has been achieved for company regulation. Such a referral would enable a national approach to NFP regulation, with responsibility for registration and on-going regulation being conferred on ASIC.

###### ASIC's role

As long as ASIC continues to regulate companies limited by guarantee, it should take steps to make itself more friendly to NFP users. Such steps might include:

- the establishment of a specialist unit within ASIC to deal with NFP companies, with further training for ASIC officers about the particular needs of NFP company stakeholders
- a sliding fee structure for NFP companies, based on size
- a plain-language guide for NFP companies.

If ASIC assumes jurisdiction over all incorporated NFP organisations, as recommended in this Report, the need for these steps would be even greater.

###### Establish a NFP advisory body

An independent NFP advisory body should be established to provide a range of support services for NFPs. This would create a centre of expertise in the specialised needs of NFP organisations. It would also underpin improved accountability and corporate governance practices within the sector. The body should be separate from, and independent of, government and the regulators (including any administrative body established to determine charitable status). The types of services that could be provided at low cost or possibly even 'no cost' to some organisations include:

- auditing
- financial and taxation advice
- legal advice
- training
- dispute resolution and mediation services for NFP stakeholders.

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### 1. INTRODUCTION

This Chapter considers the regulatory framework for NFP companies. The survey data outlined in the previous Chapters has highlighted certain distinct characteristics of NFP companies - how they differ from 'for-profit' companies, and the groupings that exist within the NFP sector. These need to be borne in mind when considering issues such as the most appropriate regulator and overall legislative framework for these organisations.

What are the regulatory options? Continue as is - the Australian securities and Investments Commission (ASIC) for companies, and State/Territory regulators for incorporated associations. Or develop a specialist unit within ASIC for NFP companies? Create an independent administrative body for NFP organisations (as recommended by the Charity Definition Report)<sup>1</sup> that works in conjunction with ASIC? Or should this body replace ASIC's role (for example, the organisation's obligations under the *Corporations Act 2001* (Cth) would be satisfied by filing with the NFP administrator)? Should there be a referral of powers by the States such that ASIC was the sole regulator for all corporate bodies, including NFP companies and associations? Some of these options have been raised in the previous Chapter, Legal Structure. This Chapter summarises the survey findings about ASIC and a possible new regulator. At the end of this Chapter, the regulatory options for a national scheme are also canvassed.

### 2. BURDEN OF REGULATION

#### 2.1. NFP context

One of the questions raised repeatedly throughout this Report is whether the burden of regulation is too great for the NFP sector, in particular, for small NFP organisations.

In addition to the effect of the myriad legal structures (outlined in Chapter 1, Introduction), and of taxation laws and fundraising/collection laws in each State, the regulation of NFP bodies varies greatly depending on:

- the nature of the activities of the organisation, and therefore the Acts and regulations that govern their activities
- whether they receive government funding and are, subject to government funding agreements.

With regard to the overall regulatory burden for NFP organisations, the findings in this Report give empirical support to the contention (made mostly recently by Professor Myles McGregor-Lowndes) that, as a consequence of the failure of government (both Federal and State) to consider or be concerned for NFP organisations in their strategy to identify ineffective and inefficient regulation, NFP compliance costs have increased. This increase has been the side effect of those governments focussing on business-oriented reforms.<sup>2</sup>

To elaborate, problems can arise when regulations are amended or new regulations are introduced. These changes can impose significant compliance costs on voluntary organisations. This can be a particular problem for organisations that depend on government funding. Grants and contracts are rarely amended to recognise the impact of such changes. If government wants NFP organisations to play a role in delivering public services it needs to ensure that regulatory changes do not impose unexpected costs on organisations, or that some compensatory mechanism for NFP organisations accompanies the reforms.<sup>3</sup>

One of the central questions in this Report is whether regulation is proportionate to risk, and whether regulation could and should be harmonised. By way of example, feedback on the preliminary findings from this Report suggest that many in the sector are of the opinion that the accounting, reporting and monitoring requirements - particularly for government-funded projects -

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Note: All references in this Report to small and large organisations or companies are based on the definition of "small" and "large" (proprietary companies) as contained in s 45A of the *Corporations Act 2001* (Cth), unless detailed otherwise.

<sup>1</sup> *Report of the Inquiry into the Definition of Charities and Related Organisations*, Charity Definition Inquiry, 2001, available at <<http://www.cdi.gov.au>> Charity Definition Inquiry, p. 294 recommendation 25.

<sup>2</sup> See M. McGregor-Lowndes, *Regulatory Infrastructure for Nonprofit Organisations*, August 2000, Working Paper No. PONC97, Queensland University of Technology. See also S. Woodward 'Not-for-Profit Companies - Some Implications of Recent Corporate Law Reforms' 17 *C&SLJ* 390, 1999.

<sup>3</sup> Similar sentiments were outlined in the UK's National Council for Voluntary Organisations (NCVO), *Response to the Performance and Innovation Unit review of the Legal and Regulatory Framework for Charities and the Voluntary Sector*, December 2000 at <<http://www.ncvo-vol.org.uk>>.

can be excessive. All too often where more than one government funder is involved they all require different information. This is not a matter of regulation, but of good management practice on the part of the government departments concerned. Efforts are being made within government to harmonise funding agreements, however, more could be done. Government departments (and their responsible ministers) ought to review their requirements to ensure that they are proportionate to risk, to be flexible rather than unnecessarily prescriptive in the way information must be presented, and to be aware of any potential overlapping requirements from other government departments or agencies.

## 2.2. How can the law facilitate good governance?

In the corporate law context, regulation theory is concerned with how to regulate corporations so as to facilitate good internal practices. Disclosure is one way of improving accountability. However, we note that requiring companies (whether 'for-profit' or NFP) to provide regular reports, does not necessarily mean that they become open and transparent. Our colleague, Dr Christine Parker wrote recently:

Despite the dominance of organizations in contemporary social life, law is desperately short of techniques, doctrines and institutions that adequately respond to the social features of organizational entities, their impacts on stakeholders, their internal capacity for self-management, their capacity for diffusion and avoidance of accountability. Lack of corporate social and legal responsibility is not just a failure of corporate management. It is also a failure of legal regulatory institutions to interact with corporate organizations to make them open and permeable.<sup>4</sup>

Parker insists that the role of legal and regulatory strategies is to add the 'triple loop' that forces companies to evaluate and report on their own self-regulation strategies so that regulatory agencies can determine whether the ultimate substantive objectives of regulation are being met. Parker argues that regulators and rule-makers will themselves have to revise and improve their strategies constantly in light of the experience and evaluation of corporate self-regulation.

## 3. NFP EXPERIENCES WITH ASIC

### 3.1. Survey question

14.2 The Australian Securities and Investments Commission (ASIC) is the regulator of all companies - 'for profit' and 'not-for-profit'. From your experience, please indicate how much you agree or disagree with the following statements about ASIC:

(1) strongly agree, (4) strongly disagree, (0) not sure

- |   |               |
|---|---------------|
| - is merely a filing agency                           | 1..2..3..4..0 |
| - provides relevant and timely advice if needed       | 1..2..3..4..0 |
| - is concerned to ensure that our company is well run | 1..2..3..4..0 |
| - is inaccessible to non-business people              | 1..2..3..4..0 |
| - imposes substantial fees                            | 1..2..3..4..0 |
| - has an important public information rule            | 1..2..3..4..0 |

*Number of respondents = varied between 1619 - 1636 for each option*

### 3.2. Survey results

To find out about dealings with ASIC, respondents were asked to rate a number of statements about ASIC's role/performance. The questions included an equal number of 'negative' and 'positive' statements. Table 1 shows the results. For the purposes of these results, the 'not sure' responses were excluded and the results were collapsed to 'agree' and 'disagree'.<sup>5</sup>

<sup>4</sup> C. Parker, *The Open Corporation, Effective Self-Regulation and Democracy*, Cambridge Press, 2002, p. 245.

<sup>5</sup> The collapsed chart did not result in any distortion of the refined patterns. However, 30% of respondents were 'not sure' about the statement that ASIC is 'inaccessible to non-business people'. For all the other statements, the 'not sure' group were 16% or less.

Table 1: Respondents' satisfaction with ASIC

Positive statements about ASIC	Negative statements about ASIC
provides timely advice if needed <i>majority (56%) disagreed</i>	is merely a filing agency <i>majority (56%) agreed</i>
is concerned to ensure that our company is well run <i>majority (56%) disagreed</i>	inaccessible to non-business people <i>majority (54%) agreed</i>
has an important public information role <i>majority (74%) agreed</i>	imposes substantial fees <i>majority (57%) agreed</i>

Table 1 shows overall dissatisfaction with ASIC's performance. The majority of respondents have agreed with only one positive statement, namely that ASIC has an important public information role to play (which, of course, is not even a statement about whether the respondents think ASIC is *performing* that role well).

There was no control group of 'for-profit' respondents, so it is not possible to draw any conclusions about whether or not this level of dissatisfaction is higher among NFP companies than 'for-profit' companies. However, as discussed under Heading 4.5, a significant majority of respondents (70%) thought that the *Corporations Act 2001* (Cth) and the way it is implemented by ASIC is more appropriate for those companies that are 'for-profit', than for NFP's.

### 3.3. Significant differences between respondents

Overall, there were very few differences between respondents based on any of the key groupings that we have used for cross-tabulation. Only 'ASIC imposes substantial fees' attracted differences in response between respondents.

#### 3.3.1. ASIC IMPOSES SUBSTANTIAL FEES

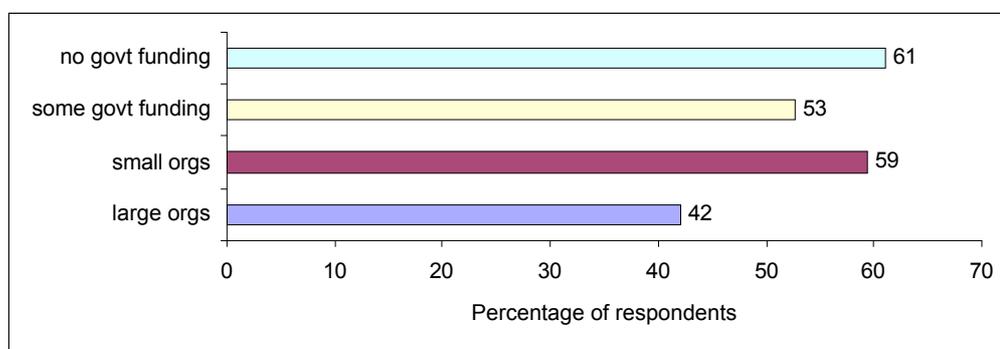
Figure 1 shows that there were significant differences between large organisations and small organisations with respect to views about this assertion. Almost 60% of small organisations thought that ASIC imposes substantial fees, whereas only 42% of large organisations were of this opinion. There were similar differences between those receiving government funding and those that do not. This is likely to be the result of the high correlation between size and the receipt of government funding.

It is logical that a small organisation would find the fees imposed by ASIC more difficult to meet than a large organisation with greater resources. It is also worth noting a recent observation by Professor Mark Lyons:

Several medium sized nonprofits have been bankrupted by fines imposed by ASIC for relatively minor infringements.<sup>6</sup>

These findings support a sliding fee structure based on size for NFP organisations.

Figure 1: ASIC imposes substantial fees, based on key indicators



<sup>6</sup> M. Lyons *The Legal and Regulatory Environment of the Third Sector, Asian Journal of Public Management* forthcoming 2004, p. 8.

**4. A NEW REGULATOR?**

**4.1. Survey questions**

14.3.1 'I agree with the Federal Government Inquiry's recommendation that an independent administrative body to oversee charities and related entities should be established'.

Circle your response.

(1) strongly disagree, (4) strongly agree, (0) not sure  
 1      2      3      4      0

*Number of respondents = 1652*

14.3.2 Do you have any general comments on this recommendation?

*Number of respondents = 107*

14.3.3 If this recommendation was implemented, should such a body have jurisdiction over corporate regulation of not-for-profit companies instead of ASIC?

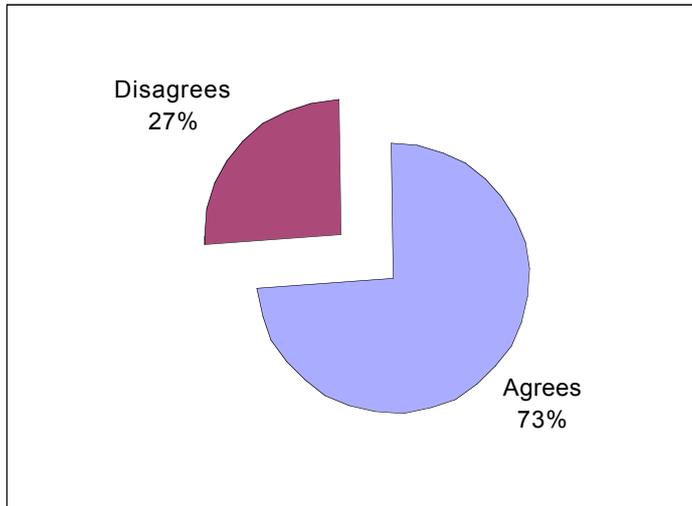
yes,                      no,                      not sure

*Number of respondents = 980*

**4.2. Survey results**

In answer to the question 14.3.1, about the Charity Definition Inquiry recommendation for the establishment of a new administrative body to oversee charities and related entities,<sup>7</sup> the majority (54%) of respondents said 'yes', 20% said 'no', 24% were 'not sure', and 2% did not respond to the question. But by removing the 'not sure' group and non-responses, the proportion in favour of the Inquiry's recommendation is 74% (Figure 2).

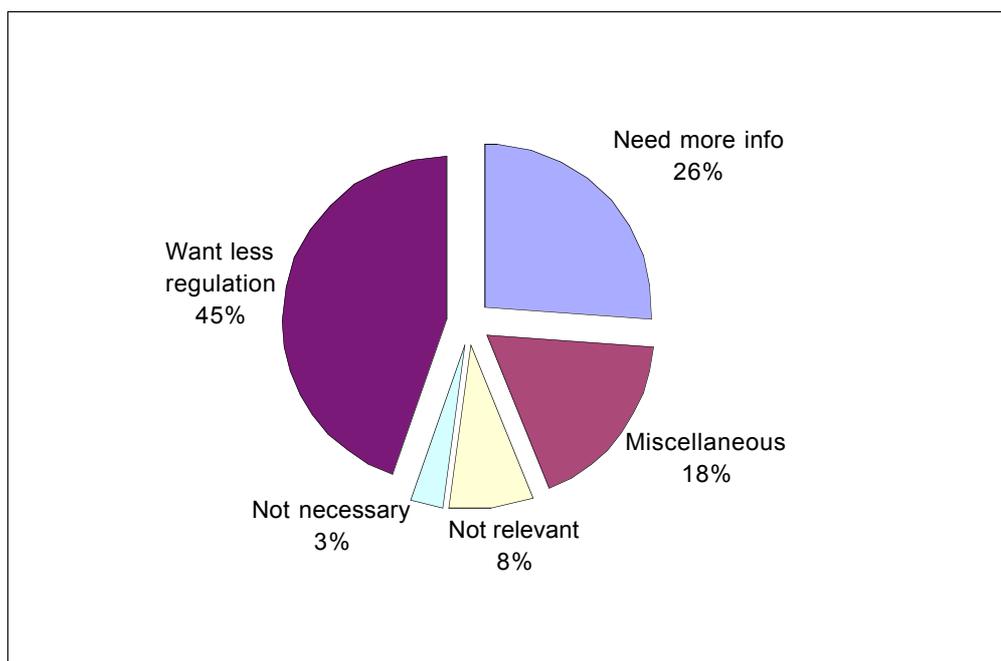
**Figure 2: Agree with Charity Definition Inquiry recommendation for new independent regulator**



Because such a high proportion of respondents said they were 'not sure' (n=405), analysis was carried out of the comments given under question 14.3.2. We looked at those who answered 'not sure' to question 14.3.1 and those who also provided a written comment under question 14.3.2 (n=107). The comments were coded. The results are shown in Figure 3.

<sup>7</sup> Charity Definition Inquiry, n. 1, p. 294, recommendation 25.

Figure 3: Respondents' comments who were 'not sure' about the recommendation



#### 4.2.1. 'DESIRE LESS REGULATION / PAPERWORK'

This was the largest category, with 45% of comments falling into it. In this category, they were of the opinion that the recommendation for a new, specialist NFP regulator would lead to excessive regulation or paperwork. In most cases, these comments suggest that the respondent thought that the independent administrative body would be in addition to ASIC.

This view is encapsulated by the following comment:

Worried: just another organisation. Still have to comply with Company Laws etc. Just another layer.

Some comments included suggestions following their concern about excessive regulation:

We do not need additional workloads or bureaucracies forced on companies which rely on small staffs and volunteers. Any new body would have to replace existing reporting requirements and understand the nature of the sector they are dealing with.

Some comments simply suggested concern about more regulation, but appreciated the need for transparency. For example:

Will charities be LESS regulated or MORE regulated? Generally I am for LESS red tape BUT donations and public funds need to be accounted for.

A few respondents said that they had not had a negative experience of ASIC which would lead them to desire an alternative regulatory body. They suggested working with the existing bodies:

There are other options that can be explored or at very least need more discussion about this. For example, ASIC's role and Office of Fair Trading's involvement possibly. ASIC has been very useful to us and would not want another body that may be more complex.

Likewise, other respondents raised concerns about the administrative costs of developing a new regulatory body:

I am somewhat cynical of bureaucracy. Dealing with ASIC for an organisation our size has not been a problem. The fees are minimal. In those circumstances I am not sure what benefits will be derived by creating a new body. My suspicion is that fees will rise to cover the cost of the new body.

Contrary to this view, other respondents stated a desire to avoid regulation by ASIC:

The only benefit that I can see would be to escape ASIC's unfair administration of late lodgement fees and charges for forms not lodged within the unrealistic timeframes they set. It is difficult for me to get the details about directors when they change in time to meet the 14 days required by ASIC - and they give absolutely no leniency on the 14 days.

A number of respondents stated that any new body should replace State-based Office of Charities, and lead to greater streamlining of reporting. For example:

It would depend on what its role and functions are and how it is funded. It should also not be an extra compliance issue, eg will it replace the NSW Office of Charities?

Likewise, another respondent stated:

If the change results in increased reporting it is unlikely we would support it. Charitable organisations already have substantial reporting and accreditation requirements from Governments and Government Agencies at National and State levels. For example, to run a raffle requires approved processes in each State the tickets will be sold as well as some states requiring approval that our organisation is a bona fide charity. In addition to this in Victoria we need to register annually to obtain authority to fundraise from the public.

And:

Unsure about the ramifications. However, the biggest problem is the reporting to each separate state regulatory body - all have different reporting requirements - being able to provide one set of information in the same form - instead of presenting differently for each state - would be time consuming and less onerous.

#### 4.2.2. 'NOT RELEVANT TO OUR ORGANISATION'

Eight per cent of comments stated that the recommendations by the Charity Definition Inquiry did not apply to them, as they were not charities. For example, one respondent said:

We are not a Charity and consequently have no views on this issue.

#### 4.2.3. 'NEED MORE INFORMATION'

Comments falling into this category included any statement expressing a lack of knowledge about the recommendation, or at least too little information to comment. Twenty-five per cent of comments fell into this category. Most respondents in this category wrote something similar to the following comment:

Was unaware of the government's interest in this matter. Therefore, have no knowledge of detail of what is being proposed.

Other respondents were reluctant to support or be against the recommendation without having a clearer idea of the exact powers of the new body:

Who will control this body?

What regulations will they abide by?

What reporting requirements?

Will our company still require an auditor?

Another said:

As I am unsure what I am agreeing/disagreeing to, it would be beneficial to educate consumers on its purpose and services and its impact on our centre.

#### 4.2.4. 'NOT NECESSARY'

Only three surveys fall into this category:

I do not see the necessity for such a body at this time.

I am wary of a new body may be worse than ASIC.

Can't see what the point would be.

#### 4.2.5. 'MISCELLANEOUS' (MAINLY SUGGESTIONS ABOUT CONTENT)

Comments that fell into this category, which accounted for 18% of comments, varied widely in content, but were similar in so far as they provided an opinion about the role that a new independent body could play.

For example, some comments stressed the training role that it could play:

It depends on their Terms of Reference. There is a need for a body that assists not-for-profits with advice - training for directors - a supportive role - not a policing role. See in this respect [www.ourcommunity.com](http://www.ourcommunity.com) for fundraising related info. This is a good idea that could be built on for training, etc.

Other respondents expressed a desire to ensure that any new body was comprised of NFP representatives, not bureaucrats:

If the Government proceeds down this path it should be comprised of people from the industry and not government bureaucrats.

Others included comments about the level of regulation:

The degree of oversight should be related to how much public money they receive and the amount of income spent in wages / salaries etc and the magnitude of the income of the persons in senior positions.

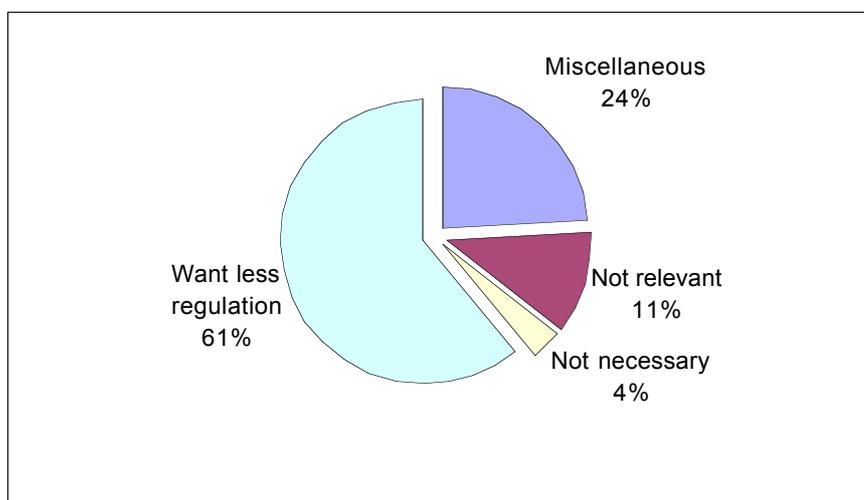
Some respondents were positive about the potential unification of state laws:

There is merit in having one Federal Administrative body to oversee charities rather than have charities registering in each individual state of Australia.

### 4.2.6. FURTHER DISCUSSION CONCERNING COMMENTS

As only 27% might be thought of as genuinely 'not sure', in the sense that they did not know about the Charity Definition Inquiry or wanted more information, the 'need more information' category was removed (shown in Figure 4). Without 'need more information' category, 'desire less regulation / paperwork' accounts for 61% of all comments.

**Figure 4: Respondents' comments who were 'not sure' about the recommendation without needing 'more information'**



### 4.3. Should the new body have jurisdiction over corporate regulation of NFP companies instead of ASIC?

In response to the second question, (question 14.3.3) that is, whether the new body should 'have jurisdiction over corporate regulation of not-for-profit companies instead of ASIC'. The responses were - 33% 'yes', 25% 'no', 36% 'not sure', and 6% did not respond to the question. When the 'not sure' group and non-responses are excluded, the proportion in favour of such a new body taking over ASIC's jurisdiction is 57%.

### 4.4. Two questions combined

Responses to questions 14.3.1 and 14.3.3 were combined as follows: a positive response to both of these questions (that is, agreed with the Inquiry recommendation and in favour of that new body having jurisdiction instead of ASIC) was taken to indicate a desire for a new regulator (n=446). A negative response to both questions was taken to mean the respondent was not in favour of a new regulator (n=169). Likewise, a negative response and a positive response in tandem (regardless of the question order) was taken to mean the respondent was not in favour of a new regulator (n=245) (total negative responses n=414).

When the responses to these two questions were combined in this way, nearly half (49%, n=828) were 'not sure' about having a new regulator, 26% wanted a new regulator and 25% did not. Refining the responses further by taking out the 'not sure' group, the split is 52% vs 48% in favour of wanting a new regulator. This is obviously a very ambivalent pattern.

4.4.1. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Small companies were more likely than large companies to want a new regulator (53% vs 44%). No other significant associations were found. For example, member-serving companies were only very marginally more likely than public-serving companies to want a new regulator (52% vs 51%) and similarly for those with PBI tax status and those without it (48% vs 50%).

4.5. How appropriate is the Corporations Act and ASIC for NFP companies?

4.5.1. SURVEY QUESTION

14.3.4 Do you think that the *Corporations Act* and how it is implemented by ASIC is more appropriate for those companies that are 'for-profit' than for those that are 'not-for-profit'?

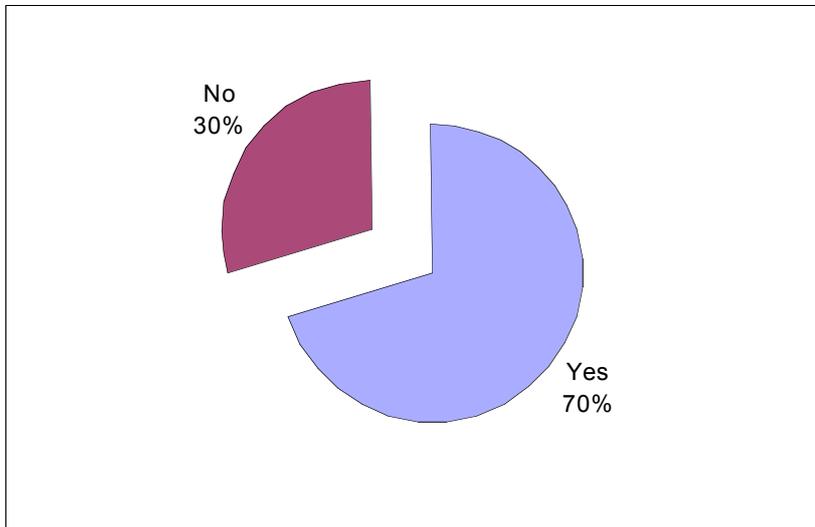
- yes
- no

Number of respondents = 1577

4.5.2. SURVEY RESULTS

A clear majority (70%) answered 'yes', they did think that the *Corporations Act 2001*(Cth) and the way it is implemented by ASIC is more appropriate for those companies that are 'for-profit' than for those that are NFP's. Not surprisingly, those respondents wanting a new regulator (see Heading 4.4) were more likely than respondents who did not to believe that the *Corporations Act* and its implementation by ASIC is more appropriate for 'for-profit' companies than for NFP companies (89% vs 54%). The results for this question suggest that it is the fact that ASIC is not a specialist regulator, rather than the way ASIC carries out its role, that causes the dissatisfaction with ASIC as reported under Heading 3.

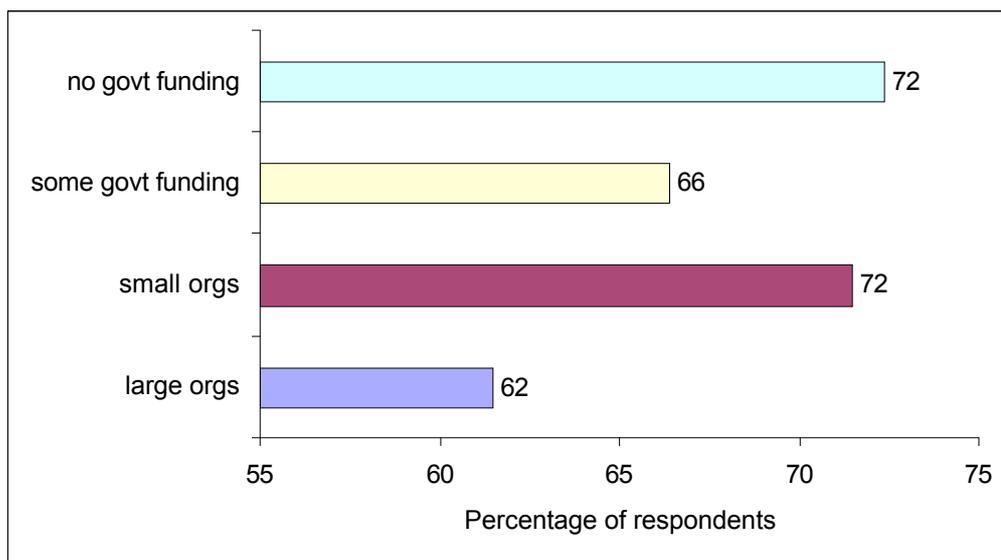
Figure 4: Is the *Corporations Act* more appropriate for 'for-profit' than NFP companies?



4.5.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

The only significant differences between respondents concerning their view of the *Corporations Act* and the way it is administered by ASIC was between large and small organisations (difference of 10%), and those that receive government funding and those that do not (difference of 6%). This reflects the consistent pattern that has emerged concerning small NFP companies' experience of the *Corporations Act*, its disclosure requirements and the way that ASIC imposes fees and fines. These results provide further support for differentiation between small and large organisations to be part of any reform of the regulation of NFP organisations.

Figure 5: *Corporations Act* more appropriate for 'for-profit' than not-for-profit companies, based on key indicators.



#### 4.5.4. OBSERVATION

These results are also consistent with ASIC administrative practice. Professor McGregor-Lowndes reports that:

...the standard reply letter with a model company limited by guarantee constitution for NFP organisations [has been replaced] by one that refers the inquirers to the state based incorporated associations regimes. The ASIC region responsible for such companies in Hobart is remote from the major concentrations of nonprofit activity. Thus, the ASIC give the impression of regarding nonprofit companies as not part of their core client focus.<sup>8</sup>

## 5. ROLE OF NEW REGULATOR

### 5.1. Survey question

14.4 If this recommendation is implemented, which of the following roles do you think such an independent body should have? (*you may tick more than one box*)

- Advice
- Advocacy on behalf of the NFP sector
- Training
- Determiner of charitable status for taxation and other purposes
- Compliance
- None of the above

*Number of respondents = 1577 for each of the options above*

- Other (*please specify*)

*Number of respondents = 64 for this option*

### 5.2. Survey results

In order to establish the respondents' view of the role of a new regulator, the respondents were given a number of options to choose from. The results are shown in Table 2.

<sup>8</sup> See McGregor-Lowndes n. 2 at p. 6.

Table 2: Respondents’ view of the role of a new regulator

Possible role	Selected this option (in descending order of prevalence)
advice	86%
advocacy on behalf of the NFP sector	69%
determiner of charitable status for taxation and other purposes	58%
compliance	58%
training	56%
other	4%

### 5.3. Significant differences between respondents

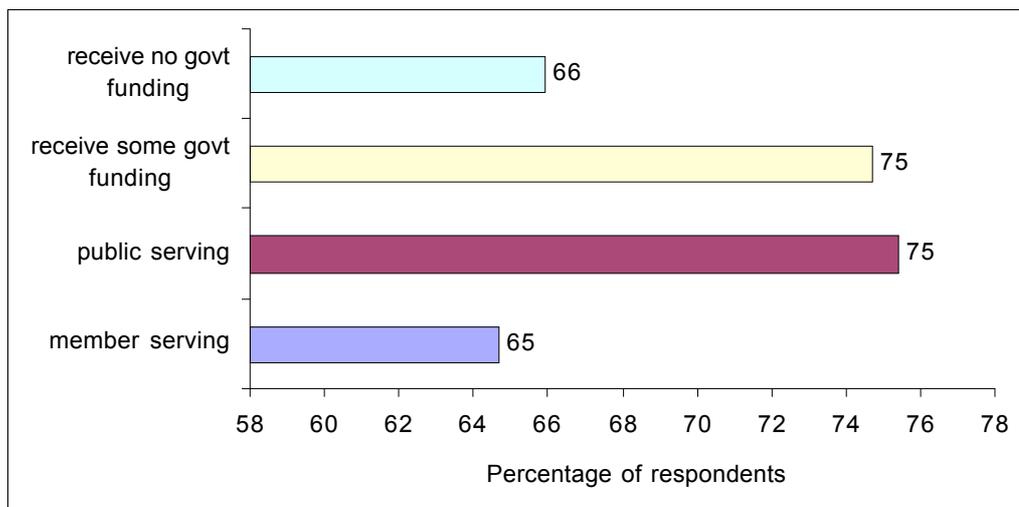
#### 5.3.1. ADVICE AND TRAINING

Eighty-six per cent of respondents said that they wanted a specialist NFP regulator to provide advice. Small organisations were much more likely than large organisations to desire the regulator to play this role (87% vs 80%), and small organisations were also more likely to desire training than large organisations (58% vs 47%). These results point to the difficulties that small NFP organisations have in obtaining timely and accessible advice and training.

#### 5.3.2. ADVOCACY

Public-serving organisations and those receiving some government funding were more likely to think that the new independent regulator should provide advocacy on behalf of the NFP sector, as shown in Figure 6. This may be because those organisations receiving government funding feel that they require independent representation to government that does not threaten their funding position.

Figure 6: Advocacy for NFP organisations, based on key indicators



### 5.3.3. DETERMINER OF CHARITABLE STATUS

A majority, 58% of respondents, thought that a new specialist regulator should have the power to determine the charitable status of NFP bodies. Public-serving bodies (63%) were slightly more likely than member-serving bodies to think that an independent regulator should play this role.

### 5.4. Observation - combination of roles

It appears from the data that the majority of respondents were in favour of combining all roles in one, new body. In particular, they were in favour of combining both compliance (58%) and determination of charitable status (58%) with advice (86%), sector advocacy (69%) and training (56%). From general feedback, however, it may be that what respondents have been keen to indicate in this question, is the need for all these services to be provided to the sector, rather than necessarily wanting them to be provided by one body. For example, that 86% of respondents want a body providing advice may be more of an indication of the extent to which many organisations are struggling to navigate the current regulatory framework, than it is a clear indication that they want one body to determine charitable status *and* provide advice.

The apparent keenness for one body may also reflect the frustration many in the sector have expressed to us about having to deal with many government bodies (ATO, ASIC, government funders, activity-based government regulators such as aged care etc.) It should not necessarily be taken to reflect a well thought-out preference for a combination of all these roles. For a sector often trumpeting its independence from government as important,<sup>9</sup> it may well be that if this question had been expressed differently, the preference would not be to combine the regulatory roles (determiner of taxation status and compliance) with support services and sector advocacy.

#### 5.4.1. ATO VIEW ON COMBINED ROLES

We believe that the dual role of the ATO in determining the charitable status of NFP bodies and revenue-raising gives rise to a conflict of interests. This point was made in the Australian Taxation Office's submission to the Charity Definition Inquiry:

[Para 8] It is our view that the current system of tax concessions provides an unnecessary layer of administrative cost and complexity, and lacks transparency...

[Para 9] Additionally, administration would be better served by a single, independent common point of decision making on definitions leading to conclusions about whether organisations are charitable or non-profit, such as occurs with the Charities Commission in the UK for example. That independent, objective decision making could then serve as the criterion determining the level of funding and/or concession to which an organisation would be entitled. Such a body would of course need to be established and funded accordingly, and could serve as a focus for any direct outlays program.

#### 5.4.2. UK EXPERIENCE

It is important to note that experience from the United Kingdom (which has had a Charities Commission for over 40 years)<sup>10</sup> suggests that combining the roles in this way can create tensions. In particular, the National Council for Voluntary Organisations (NCVO), a major sector body in the United Kingdom, has questioned the United Kingdom Commission's dual role in its submission to a government review of the sector:

NCVO has long had concerns about the dual role performed by the Charity Commission. We believe that the dual role inevitably creates conflicts of interest and that it can cause the Charity Commission to concentrate on one function at the expense of the other. Nor are we convinced by the Charity Commission's arguments that the two are part of a continuum and that their effective functioning would be impaired if they no longer provided an advice service. We therefore consider that the regulatory and the wider advisory functions of the Charity Commission should be separated.<sup>11</sup>

<sup>9</sup> The most recent example of this has been the outcry from many NFP organisations regarding advocacy and lobbying activities under the draft *Charities Bill 2003*. See 'Speaking out While They Can', *The Melbourne Times* Issue 35, 10 September 2003, pp. 8–9. Also information contained on the Philanthropy Australia website at <[www.philanthropy.org.au/advocacy/draft.htm](http://www.philanthropy.org.au/advocacy/draft.htm)>.

<sup>10</sup> See Charity Definition Inquiry, n. 1, Ch. 32, p. 284 and Appendix I, pp. 419–27 for a clear overview of the nature and role of the UK Charities Commission.

<sup>11</sup> National Council for Voluntary Organisations, *Response to the Performance and Innovation Unit Review of The Legal and Regulatory Framework for Charities and the Voluntary Sector*, 2001, para. 5.1 at <[http://www.ncvo-vol.org.uk/main/about/does/policy/pdfs/CLR\\_PIU\\_submission.pdf](http://www.ncvo-vol.org.uk/main/about/does/policy/pdfs/CLR_PIU_submission.pdf)>.

However, the most recent United Kingdom Cabinet Report has recommended, among other things, that the United Kingdom Charities Commission should retain its advisory role although it 'should be more precisely defined and focused on the issues over which it has regulatory responsibility.'<sup>12</sup>

### 5.5. Recommendation for an independent advisory body

In the Australian context, it is hoped that a body such as the National Nonprofit Round Table<sup>13</sup> will take on an advocacy role on behalf of the sector. Although still in a fledgling stage and in need of stable funding itself, it could also be appropriate for the National Nonprofit Round Table to auspice a national sector body suitably equipped to provide advice and training. In view of our data, and the observations we have made under Heading 5.4, we believe that there is a clear need for NFP organisations to be able to draw on specialist, independent advice on a range of areas. A new advisory body would be able to generate at least some of its funding from fees for service. One would hope that any shortfall could come from a far-sighted philanthropic source and possibly, in part, from government. We are of the opinion that such a body is needed, whether or not an independent administrative body is established as recommended by the Charity Definition Inquiry.

In our opinion, the establishment of a new, independent advisory body would be of particular benefit to small to medium NFP organisations and would serve to strengthen the accountability and capacity of the sector.

#### Recommendation: Establish an independent NFP advisory body

An independent NFP advisory body should be established to provide a range of support services for NFP organisations. This would create a centre of expertise in the specialised needs of these organisations. It would also underpin improved accountability and corporate governance practices within the sector. The body should be separate from, and independent of, government and the regulators (including any administrative body established to determine charitable status). The types of services that could be provided at low cost or possibly even 'no cost' to some organisations are:

- auditing
- financial and taxation advice
- legal advice
- training
- dispute resolution and mediation services for NFP stakeholders.

## 6. OPTIONS FOR NEW REGULATOR

In terms of regulation of NFP companies, it is suggested that there are two main options that warrant consideration and debate:

- a) the creation of a specialist unit within ASIC; or
- b) the creation of an independent, specialist NFP regulator that takes over the regulation of NFP companies from ASIC.

### 6.1. Feedback

Following the release of our Preliminary Findings,<sup>14</sup> which included an outline of these options, a large amount of correspondence was received about the recommendations. Further workshops were carried out to obtain feedback on the recommendations.

<sup>12</sup> United Kingdom Cabinet Office, Strategy Unit Report, *Private Action, Public Benefit - A Review of Charities and the Wider Not-for-Profit Sector*, 2002, para. 7.48 at <<http://www.piu.gov.uk/2002/charity/report/index.htm>>(UK Report).

<sup>13</sup> Formation in June 2002 of a National Nonprofit Round Table (initially called the 'Third Sector Round Table'). See 'Non-Profit Groups Link up to Present United Front', *Financial Review*, 26 June 2002, p. 11 and E. Cham, National Director Philanthropy Australia Inc, 'A New Focus for Australia's Non-Profits', 2002, 50 *Australian Philanthropy Journal* 3.

<sup>14</sup> The Preliminary Findings were sent to all the respondents who provided contact details for this purpose. See Appendix 1, Methodology, for further details concerning the way in which feedback on the Preliminary Findings was sought and received.

### 6.1.1. ACROD FEEDBACK

First, data was obtained in May 2003 from participants at a conference of Chief Executive Officers of disability organisations who are members of the peak body ACROD (National Industry Association for Disability Services), at which Ms Woodward was invited to deliver a presentation on the Project. Participants were asked to complete a brief feedback form for ACROD. From the 125 responses (out of about 140 who attended the session), the majority, 68, were incorporated associations and 46 were companies limited by guarantee. It is worth noting that 95% were in favour of government reporting requirements being streamlined and being made to one specialist government regulator. The ACROD feedback supports the Project's survey data and is significant because it provides responses from a *group of incorporated associations* to show that they are even more strongly in favour of a new specialist NFP structure and regulator. Indeed, whether the feedback was obtained from representatives of incorporated associations or companies limited by guarantee, there was general desire (with very few exceptions) for a centralised regulation and place of lodgement for the legal reporting requirements for NFP organisations, including fundraising reports and annual returns.

### 6.1.2. FREEHILLS SEMINAR

Secondly, Ms Woodward and Ms Marshall were invited to present a seminar about the Project on behalf of Freehills, solicitors, (as part of their pro bono services). This seminar was held in Sydney on 17 June 2003 and was attended by approximately 70 people from a variety of NFP organisations and some advisors to NFP organisations. After a presentation about the Project, people were divided into groups to discuss some of the preliminary recommendations. There was clear agreement from participants that national uniformity was necessary and that there should be a centralised place for lodgement of reports, including fundraising reports.

## 6.2. Specialist in NFP issues

The feedback received was split as to whether a new specialist NFP regulator should be created to perform these functions, or whether a specialised unit should be created within ASIC. The survey results discussed in this Chapter show that whilst ASIC is not generally thought of as providing a satisfactory service to NFP bodies. This may be because the *Corporations Act 2001* (Cth) and the way it is administered by ASIC are more suited to 'for-profit' companies than NFP organisations. If steps were taken to create a specialised NFP unit within ASIC that was more user-friendly, and understood the particular needs of NFP bodies, this dissatisfaction would be allayed.

#### Recommendation: ASIC's role

As long as ASIC continues to regulate companies limited by guarantee, it should take steps to make itself more friendly to NFP users. Such steps might include:

- the establishment of a specialist unit within ASIC to deal with NFP companies, with further training for ASIC officers about the particular needs of NFP company stakeholders;
- a sliding fee structure for NFP companies, based on size
- a plain-language guide for NFP companies.

If ASIC assumes jurisdiction over all incorporated NFP organisations, as recommended in this Report, the need for these steps would be even greater.

## 7. NATIONAL REGULATORY FRAMEWORK

### 7.1. Options to consider

In terms of regulation of both associations and NFP companies, we suggest that there are three main options that warrant consideration and debate:

- a) Retention of the existing dual regime but with uniform State and Territory-based incorporated associations legislation (along the lines of what has been achieved for cooperatives);
- b) Retention of the existing dual regime, but with uniform State and Territory incorporated associations' legislation *and* legislative amendments enabling ASIC to assume jurisdiction over incorporated associations; or

- c) Introduction of a single, Commonwealth statutory regime for all corporate bodies (that is, 'for-profit', NFP, companies and incorporated associations) by referrals of power from the States to the Commonwealth (along the lines of what has been achieved for company regulation) which would also enable national regulation by ASIC *and* the possible development of a specialist form of corporate entity for NFP organisations generally.

## 7.2. Uniform incorporated associations' legislation

Others have already made the call for uniform legislation for incorporated associations.<sup>15</sup> It is an appealingly logical notion but there seems to have been little push for it. This point is made by Professor McGregor-Lowndes:

Any reform agenda would have to be led by a federal government with considerable political will to drive through reforms that would involve the co-operation of the states and territories. A similar resolve to that required to achieve the national corporations regimes would be needed over a sustained period. The task of politically managing such a process of reform at present seems difficult given the lack of a peak association for the whole of the sector or a broad coalition of peak bodies that any government could interact with concerning the reform process. Another essential element of the recent reform agendas of both corporations and taxation reform has been a broad community agreement that both areas were "broken and needed fixing". Whether the public perception of a nonprofit regulatory environment in need of reform is present or could be evoked is also not clear. Many powerful and vocal nonprofit organisations would actively oppose the creation of such a perception because it would directly impact upon their trustworthiness in the community and hence their access to donations, sponsorship and volunteers.<sup>16</sup>

The survey data as outlined in Chapter 3, Legal Structure, provides some evidence of problems with an incorporated association as the legal structure for some NFP organisations (even small ones). In particular, peak (national) bodies or the national body for a group of State/Territory organisations<sup>17</sup> are often companies limited by guarantee because of the ease of operating under a national regime, but this means one 'group' needs to manage and appreciate both regimes as well as the differences between the various associations' legislation. In its final report, the Industry Commission considered uniform State associations' legislation as one option to improve accountability, but concluded that it was 'not the best way to ensure public accountability for CSWOs [community social welfare organisations]'. The Commission reached this conclusion for two reasons: (a) because of the difficulties of achieving and maintaining uniformity between States; and (b) because not all CSWOs are incorporated associations and therefore making the legislation uniform 'would not encompass all CSWOs and hence would not provide a consistent set of reports for all CSWOs. Nor would it lead to a comprehensive database'.<sup>18</sup> This report was published in June 1995 so it is possible to surmise that if the Commission had had the benefit of recent experience with the referrals of power for the *Corporations Act 2001*(Cth),<sup>19</sup> it would have felt that reason (a) (above) could be overcome, but presumably its conclusion would not have been altered because reason (b) (above) would still apply.

The following is an elaboration of some of the main problems with a continuation of the current State and Territory-based scheme.

<sup>15</sup> For example, S. Sievers, *Incorporation and Regulation of Non-Profit Associations in Australia and other Commonwealth Law Jurisdictions*, 13 *AJCL* 124 at 142, 2001; M. McGregor-Lowndes see n. 2; and M. Lyons *The Legal and Regulatory Environment of the Third Sector*, *Asian Journal of Public Management*, forthcoming 2004.

<sup>16</sup> See McGregor-Lowndes, n. 2, p. 8.

<sup>17</sup> For example, the Nursing Mothers' Association has State incorporated associations with a small national body that is a company limited by guarantee.

<sup>18</sup> See Industry Commission 1995, *Charitable Organisations in Australia*, Report No. 45, AGPS, 1995, pp. 211–12.

<sup>19</sup> See for example, H.A.J. Ford et al., *Ford's Principles of Corporations Law*, 10th edn, Butterworths, Sydney, 2001, paras 2.230–2.250, 2.306, 2.310, 3.060–3.090; and R. Tomasic, J. Jackson and R. Woellner, *Corporations Law: Principles, Policy and Process*, 4th edn, Butterworths, 2002, pp. 21–72, especially para. 1.8.

### 7.2.1. FORUM SHOPPING

A lack of uniformity can potentially lead to forum shopping. By choosing the State or Territory of incorporation carefully, it would be possible for unscrupulous associations to avoid any requirement to maintain proper accounting records and comply with appropriate standards of financial reporting.<sup>20</sup> Public disclosure obligations and financial recording keeping should be consistent across States and Territories. Lessons need to be learnt from the development of company law in Australia. It is imperative to have a nationally consistent approach based on a well thought-out public policy decision about the most appropriate disclosure regime for NFP organisations, in order to promote accountability and good corporate governance.

### 7.2.2. DUPLICATION OF ADMINISTRATION

The need for separate Registrars in each State and Territory results in significant duplication of administrative effort and cost. Yet, as far as we have been able to ascertain, there is no significant net revenue gain for the States. We note that, in view of the overall public benefit derived from the operation of NFP organisations,<sup>21</sup> it would be inappropriate for the incorporation of associations to be relied upon as a source of significant (net) revenue.

Further, the Department and the relevant government Minister whose portfolio covers incorporated associations, varies between jurisdictions and, again, adds to the complexity for an organisation that needs to operate in two or more jurisdictions.

### 7.2.3. DISTINGUISHING BETWEEN ORGANISATIONS ON THE BASIS OF SIZE

A national regulatory regime for all incorporated NFP organisations within the auspices of the *Corporations Act 2001* (Cth) would enable the issue of graded reporting obligations to be addressed, dependent for example on size). This would prevent avoidance of reporting obligations merely because of its legal structure and/or place of incorporation/registration.

## 7.3. Uniform incorporated associations' legislation with ASIC as regulator

The second option is to retain the existing dual regime but with both uniform State associations' legislation *and* power over incorporated associations being conferred on ASIC. This is the intermediate of the three options, similar to what existed for companies under the *Corporations Law* scheme, prior to the recent referrals of power. It would require each of the States to confer regulatory power on ASIC under their incorporated associations' legislation and for the Commonwealth to amend the *ASIC Act 2001* (Cth). It has the advantage of allowing an existing experienced regulator<sup>22</sup> to take responsibility for the regulation of all bodies corporate (that is, 'for-profit', NFP, companies and incorporated associations), while retaining a specialist form of incorporation familiar to the majority of NFP organisations. The survey data in Chapter 3, Legal Structure, showed that almost a third (31%) of respondents identified a preference for ASIC 'rather than State regulator' as an important factor in their choice of incorporated legal form.<sup>23</sup> NFP expertise could be developed if this option also facilitated the creation of a specialist unit within ASIC to deal with NFP companies and associations. We suggest that the development of such expertise is likely to satisfy many of the concerns about ASIC's role as expressed by respondents to the survey. An example of this was the concern expressed by 54% of respondents that ASIC is 'inaccessible to non-business people'<sup>24</sup>. However, this option would presumably raise the same constitutional issues as the former *Corporations Law* scheme faced - Federal courts could not exercise enforcement powers under the respective State Acts<sup>25</sup> and breaches could not (at least with total certainty) be prosecuted by the Commonwealth Director of Public Prosecutions.<sup>26</sup>

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<sup>20</sup> A. Sievers, 'Incorporation of Non-Profit Associations: The Way Ahead?' 18 C&SLJ 311–25 at p. 320.

<sup>21</sup> This benefit is acknowledged in *Review of the Associations Incorporations Act 1984 - Consultation Paper*, NSW Office of Fair Trading, April 2003, p. 7.

<sup>22</sup> ASIC also has in place streamlined processes for electronic lodging and searching of documents etc.

<sup>23</sup> However, we do not have any substantive data concerning the reasons why organisations chose to incorporate as associations rather than companies limited by guarantee.

<sup>24</sup> See Heading 3.2.

<sup>25</sup> See *Re Wakim: Ex parte McNally*, 199, 198 CLR 511: 'the States have no power, with or without the consent of the Parliament of the Commonwealth, to invest State jurisdiction or judicial power in federal courts' per J. McHugh at [56].

<sup>26</sup> See *R v Hughes* (2000) 34 ACSR 92.

#### 7.4. Commonwealth legislation administered by ASIC

The third option would be the introduction of a single, Commonwealth statutory regime for all corporate bodies (that is, 'for-profit', NFP, companies and incorporated associations) by referrals of power from the States to the Commonwealth. This is along the lines of what has been achieved for company regulation, with national regulation by ASIC. This would be the most drastic but, it is suggested, the most satisfactory of the three options canvassed. Because it is the most drastic, it may also be the most unrealistic due mainly to lack of political will. However, unlike business name registrations, regulation of incorporated associations is not a revenue earner for the States and, therefore, there may not be anywhere near the resistance to such a referral as was experienced with corporations' powers. Of course, forceful lobbying by the NFP sector itself (for example under the auspices of the newly formed National Nonprofit Round Table) would be essential.

There are several advantages to this third option:

First, a single regulatory body such as ASIC would enable the creation of a specialist unit to meet the particular needs of NFP bodies. While this advantage also exists for the second option (ASIC-enforcement of State associations incorporations legislation), the third option would allow for cross-vesting and the same enforcement regime as provided for under the *Corporations Act*, without fear of constitutional challenge. Given that ASIC already deals with the registration and on-going compliance by over 10,000 NFP companies, this expanded role would not involve ASIC (that is, the Commonwealth) in a completely new regulatory role or a service delivery system. ASIC's established on-line lodgement and searching facilities could be used to streamline the paperwork for, and to enhance disclosure by, incorporated associations.

Second, because the Federal Government has not adopted the Charity Definition Inquiry's recommendation for an independent administrative body,<sup>27</sup> State referrals of power may be the most realistic and revenue-neutral option. Indeed, some of the submissions by NFP organisations to both the Industry Commission and the more recent Charity Definition Inquiry have suggested reforms along this line.

Third, and perhaps even more importantly, this option would facilitate the introduction of a specialist form of corporate structure available only to NFP organisations. While there are many overarching provisions in the *Corporations Act 2001* (Cth) that should apply to all companies (particularly, directors' duties), the unique issues faced by NFP companies could be addressed in specialist provisions. A plain-language guide for NFPs along the lines of the Small Business Guide could make an enormous difference. At the time that the associations' incorporations legislation was introduced, the simplification of requirements and filings for small business had not been introduced into the corporations' regime. The concept of replaceable rules under the *Corporations Act* is not dissimilar to that of model rules under the various State and Territory associations' incorporations Acts. In the way that some replaceable rules apply only to public companies, there could be some designed specifically for NFP bodies - picking up the best of the incorporated associations model rules framework.

#### 7.5. Feedback

In addition to the feedback received from the ACROD and Freehills seminars referred to under Heading 6.1 which strongly supported a national regime, we received considerable support for this recommendation after releasing it as a preliminary finding in March 2003. By way of example, an email saying:

I am a registered company auditor who has worked exclusively [in a particular part of the NFP sector] for 25 years. I endorse wholeheartedly your comment [for] the introduction of a single, Commonwealth statutory regime for all corporate bodies (that is, 'for profit' and NFP companies and incorporated associations) by a referrals of power from the States.

Another email from the Executive Officer of peak body:

One important underlying issue, I suggest, is that there should be uniformity within the regulatory regime thereby enhancing public confidence. Ideally a single statutory regime for all corporate bodies should be established under the guise of the Commonwealth government.

<sup>27</sup> See Peter Costello, The Treasurer, Commonwealth of Australia, Government Response to Charities Definition Inquiry, Press Release, No. 049, 29 August 2002, available at <<http://www.treasurer.gov.au/tsr/content/pressreleases/2002/049.asp>>.

### **Recommendation: Single regulatory regime**

A single Commonwealth statutory regime should be introduced for all corporate bodies (that is, 'for-profit' companies, NFP companies and incorporated associations) by referrals of power from the States to the Commonwealth, along the lines of what has been achieved for company regulation. Such a referral would enable a national approach to NFP regulation, with responsibility for registration and on-going regulation being conferred on ASIC.

## 8. CONCLUSION

The regulatory framework underpins accountability, which in turn underpins confidence in the sector. It is a core issue that needs to be considered even before the related issue of disclosure. The particular needs of NFP organisations must be reconsidered. In recent times, these have often been overlooked or inadvertently worsened by changes made at the behest of, or for the benefit of, business.<sup>28</sup> Efficiencies and improvements in the legislative regime are long overdue. The existing two-tiered regulatory system (State and Territory-based incorporated associations and a Commonwealth company law regime) is inefficient, costly and does not meet the needs of small or large NFP organisations. A specialist regulator, or at least, a specialist unit within ASIC is also necessary to improve accountability and regulation of NFP organisations in Australia.

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<sup>28</sup> See for example, M. McGregor-Lowndes n. 2 at p. 7 when he refers to Federal Government policy requiring Regulatory Impact Statements. The definition of 'business' in the guidelines for these statements effectively excludes the need to consider the non-profit making or non-commercial transactions of an NFP organisation.

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# CHAPTER 5: BOARD SIZE, COMPOSITION, REMUNERATION AND EXPERIENCE

## *Does size matter?*

### SUMMARY OF KEY FINDINGS IN THIS CHAPTER

#### The 'typical' Board of directors

- Comprised 8 non-executive directors, however, there was significant variation between groups based on factors such as principal activity, size, receipt of government income and member-serving or public-serving.
- Did not pay their non-executive directors, but 8% said that their non-executive directors received payment in addition to out-of-pocket expenses.
- Was predominantly male: only 26% of directors were female, although three-quarters had at least one female director on their Board.
- Comprised directors aged between 40–72 years: only 3% had a male, and 2% with a female, aged between 18-24 years.
- Spoke English as their first language: 2% of all female, and 2% of male, directors were Aboriginal, Torres Strait Islander or a descendant. Of all directors whose 'first learnt language was not English', 10% were male and 6% were female.

#### Independence

- Seventy-seven per cent of all respondents were from Boards comprised entirely of non-executive directors.
- Almost invariably the Chair was a non-executive director (91%).
- Just under half (45%) of all CEOs were directors. But the position was different in large organisations where only 23% of CEOs were directors.

#### Remuneration of non-executive directors

- Despite the fairly widespread assumption that all *non*-executive NFP directors provide their services to the Board on a voluntary basis, the data highlighted a small, but possibly growing group, who do receive payment in addition to out-of-pocket expenses. However, there was significant variation based on the principal activity and size of the organisation.
- Of those not paying their non-executive directors, only 15% thought they should be paid.

#### Representation of stakeholders at Board level

- Whilst not the majority, a significant number of Boards have directors appointed to represent the interests of particular (non-member) stakeholders.
- Fifteen per cent of respondents reported that a director on the Board was a substantial donor or an associate of a substantial donor, a feature that distinguishes NFP Boards from 'for-profits'.
- The issue of potential conflicts of interest in the NFP context needs further research.

#### Appointment process

- There is very little consistency across organisations in the methods of appointing directors.
- Board elections are not often contested - 64% said that they are 'rarely' contested. Board elections are much more likely to be contested in member-serving organisations.

#### Recruiting and retaining Directors

- Nearly a third (29%) of respondents reported difficulty recruiting directors and around a third (28%) of respondents had unfilled Board positions.
- Sixteen per cent of respondents reported difficulty in retaining directors.
- There were significant differences between respondents based on size and principal activity. As a general observation, small organisations had greater difficulties both recruiting and retaining directors than large organisations.

### Board skills and knowledge

- Generally, CEOs consider the skills of the Board to be adequate for their organisation's needs.
- Respondents believe the Board understood their personal liability as directors. And this was consistent across sub-groups.

## RECOMMENDATIONS

### Board size

As a 'best practice' guideline, Boards need to periodically review their size to make sure they are small enough to work effectively as a group, but large enough to contain an appropriate mix of skills and perspectives. While there is no ideal size, it is unlikely that very large Boards work effectively or efficiently. One popular method among NFP organisations for dealing with this is the establishment of a smaller management group. However, this option can be problematic. Directors who are insufficiently involved and informed expose themselves to potential risks under their liabilities as a director. NFP organisations with very large Boards need to consider whether there are more effective ways of involving stakeholders in the organisation. Options such as involving experts or stakeholders as specialist advisors on an advisory panel might usefully be explored by such Boards. This is an issue that it would be appropriate for the advisory body recommended in this Report (see Chapter 4, Regulatory Framework) to develop.

### Board recruitment methods

There is a demonstrated need for materials, training and other assistance for NFP Boards in their recruitment of Board members, as well as an ongoing assessment of the directors' mix of skills, experience and perspective. In general, NFP company Boards currently comprise people from a narrow demographic. Many NFP organisations could benefit from the broader range of the skills and experience that are available in the general community. Assistance with this issue would be a useful role for the NFP advisory body recommended in this Report (see Chapter 4, Regulatory Framework).

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## 1. INTRODUCTION

This Chapter reports on the survey data collected about the profile of the Boards of NFP respondent companies limited by guarantee. It covers the size of the Boards, how independent they are, and the experience and skills of directors. In order to inquire about Board independence, questions were asked about the balance of executive or non-executive directors, and whether directors are recruited to represent stakeholders or major donors. Size, independence and skills are all factors that contribute to the type of Board and the role that it plays within the organisation.

The independence of Boards has been identified as a key issue in the good governance of corporations, and successive guidelines released in the USA, the UK and Australia have insisted that Boards should be as truly independent as possible. However, the data reported in this Chapter suggests that the likelihood of a NFP organisation having an independent Board is affected by its size. For example, the Chair of NFP a small organisation is more likely to be an executive member than in a larger organisation.

The gender, age and ethnicity of the directors of NFP Boards are also considered in this Chapter. Having a diverse Board is seen to be an important factor contributing to a vibrant NFP Board that is responsive to the needs of clients and other stakeholders. The Chapter also considers the ways that directors are appointed and whether NFP organisations have problems recruiting directors and retaining them.

## 2. BOARD COMPOSITION

### 2.1. Number of directors on Board

#### 2.1.1. SURVEY QUESTION

7.1.1 How many directors are currently on your Board?  
..... (write the total number of directors)

*Number of respondents = 1674*

#### 2.1.2. SURVEY RESULTS

Over half (57%) of the NFP Boards had 8 or more directors. The average number of directors was 8 and the mean number was 8.5.

**Table 1: Number of directors**

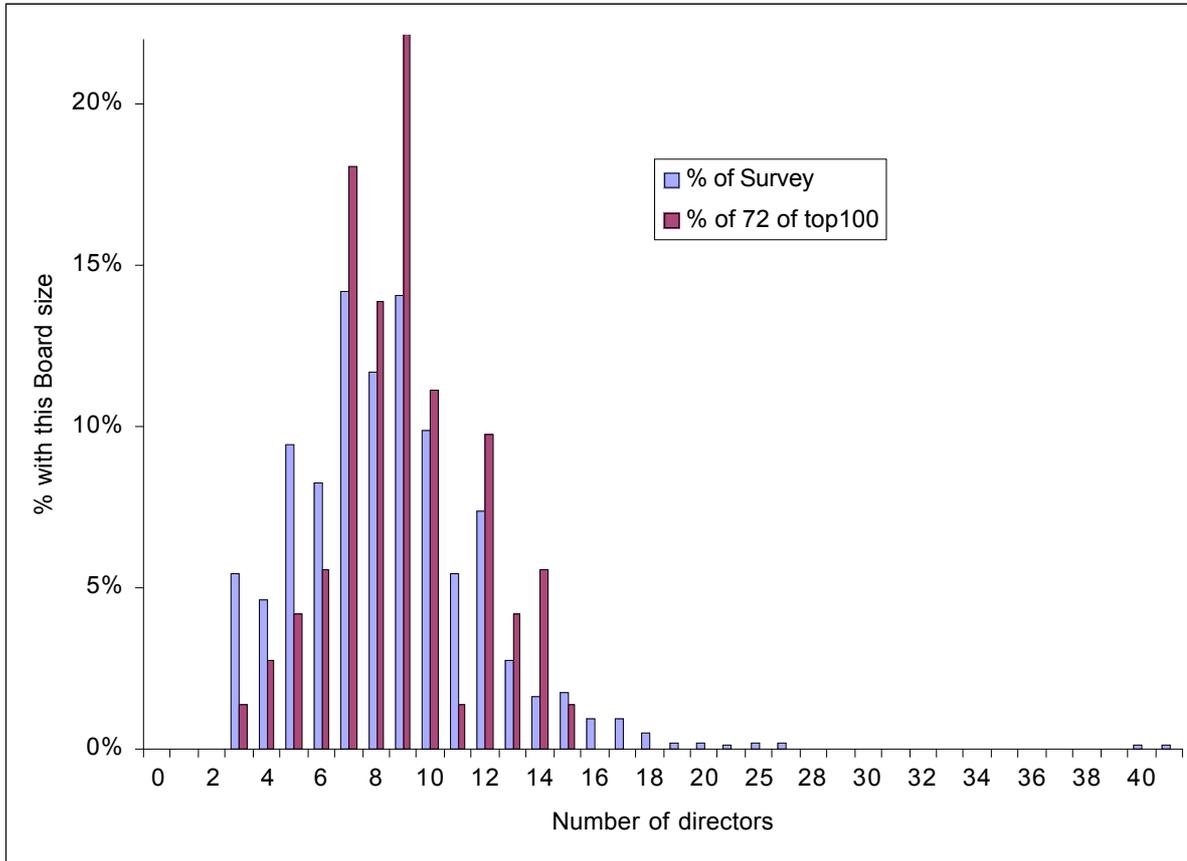
<b>Number of directors</b>	<b>Frequency</b>	<b>Per cent</b>
3 or fewer	109	7
4 or 5	257	15
6 or 7	351	21
8 or 9	421	25
10 to 15	470	28
16 or more	66	4
no answer given	14	
<b>total</b>	<b>1688</b>	<b>100</b>

Note: All references in this Report to small and large organisations or companies are based on the definition of "small" and "large" (proprietary companies) as contained in s 45A of the *Corporations Act 2001* (Cth), unless detailed otherwise.

2.1.3. COMPARISON WITH 'TOP 100' COMPANIES

The survey responses were compared with those of a survey of the 'Top 100' listed 'for-profit' companies conducted by Stapledon & Fickling in March 2001.<sup>1</sup> These figures are shown in Figure 1. Although these 'for-profit' companies are unlike the survey group in many obvious ways (including size),<sup>2</sup> the comparison was thought to be of interest given that both groups should arguably have a high degree of public accountability and a high standard of corporate governance.

Figure 1: NFP Board size compared with 'Top 100' Board size



The comparison showed that, in terms of Board size, the average number of directors on the Boards of the respondent NFP companies was 9,<sup>3</sup> which was similar to the 'Top 100' average of nine. There were, however, some significant differences at either end of the spectrum. Only one of the 'Top 100' Boards had the legal minimum of three directors, compared with 6% of the NFP Boards. At the other end of the spectrum, the largest 'Top 100' Board had 15 directors, but 4% of the NFP group had more than 15 directors, including one respondent with 40 and one with 45.

2.1.4. COMPARISON WITH UK

Based on our data, the average Australian NFP company Board is smaller than that of the typical UK charity. A survey carried out by Chris Cornforth<sup>4</sup> in 2001 found that the average size of a charity Board in the UK was 9.5.

<sup>1</sup> G. Stapledon & J. Fickling, *Board Composition and Pay in the Top 100 Companies*, paper presented to the CMSF Conference, Institutional Analysis Pty Ltd, March 2001, at <<http://www.institutionalanalysis.com>>. The 'Top 100' companies were ascertained by reference to their market capitalisation. At the time of conducting the survey, March 2001, this was the most recent data on 'for-profit' Boards.

<sup>2</sup> See heading Chapter 2, Profile Data.

<sup>3</sup> This result was different to that found in the earlier study by P. Steane & M. Christie, 'Nonprofit Boards in Australia: A Distinctive Governance Approach', 2001, 9 *Corporate Governance* 48 which found an average Board size of 12.5.

<sup>4</sup> C. Cornforth, 'Recent Trends in Charity Governance and Trusteeship: The results of a survey of governing bodies of charities', NCVO and The Open University Business School, 2001, p. 5.

## Chapter 5 - Board Size, Composition, Remuneration and Experience

### 2.1.5. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

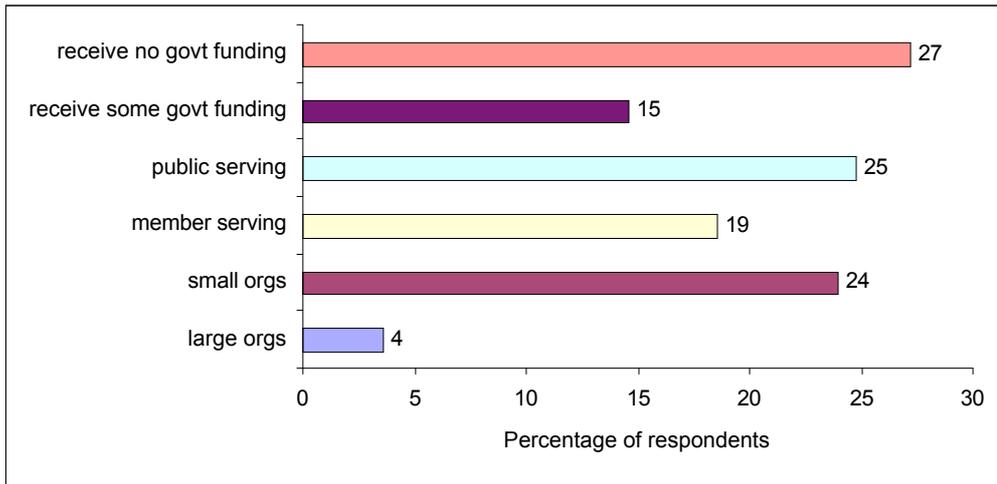
The size of the organisation had a significant effect on Board size. Figure 2 shows the percentage of respondents reporting that their Board had 5 or fewer directors. Overall, 22% of respondents had 5 or fewer directors on their Boards, but small organisations are 20% more likely to have 5 or fewer directors than large organisations (24% vs 4%). Overall, 32% have Boards with 10 or more directors, but again there is a significant difference between large and small organisations. The majority (52%) of large organisations have (large) Boards constituted by 10 or more directors, compared with 30% of small organisations (shown in Figure 3).

The presence of any government funding also has an impact on Board size. Organisations not receiving government funding are more likely than those that do, to have 5 or fewer directors on their Boards, whereas organisations that do receive government funding are 9% more likely than those that do not to have 10 or more directors on the Board.

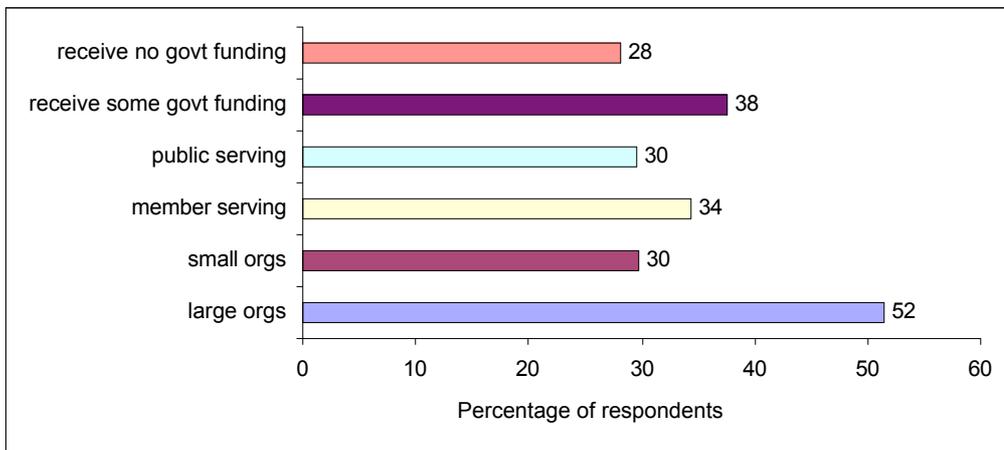
Similarly, public-serving organisations were more likely than member-serving organisations to have five directors or less on their Boards, whereas member-serving organisations were 5% more likely than public-serving organisations to have 10 or more directors on the Board.

With regard to variation in Board size based on principal activity, we note that Religious organisations and Education Related organisations were the groups most likely to have a small Board (5 or fewer) - 58% of Religious and 38% of Education related organisations, compared with only 10% of Sports and Recreation organisations. Education organisations (45%) and Interest Group organisations (46%) were most likely to have larger Boards (10 or more), compared with 32% overall.

**Figure 2: Five or fewer directors (small Board), based on key indicators**



**Figure 3: Ten or more directors (large Board), based on key indicators**



## 2.2. Recommendation - Board size

While the data shows that the average NFP company Board size is 8 directors, further analysis shows that, particularly for large organisations, the Board can be quite large (10 or more directors). Sometimes there may be very good reasons for a larger Board and the typical 'Top 100', 'for-profit' company model should not be assumed to be the best model for NFP organisations. However, the issue warrants further consideration especially in the light of the legal duties and liabilities directors face.

### Recommendation: Board size

As a 'best practice' guideline, Boards need to periodically review their size to make sure they are small enough to work effectively as a group, but large enough to contain an appropriate mix of skills and perspectives. While there is no ideal size for Boards, it is unlikely that very large Boards work effectively or efficiently. One popular method among NFP organisations for dealing with the problem is the establishment of a smaller management group.<sup>5</sup> However, this option can be problematic. Directors who are insufficiently involved and informed expose themselves to potential risks under their liabilities as a director. NFP organisations with very large Boards need to consider whether there are more effective ways of involving stakeholders in the organisation. Options such as involving experts or stakeholders as specialist advisors on an advisory panel might usefully be explored by such Boards. This is an issue that it would be appropriate for the independent NFP advisory body recommended in this Report (see Chapter 4, Regulatory Framework) to develop.

## 3. EXECUTIVE/NON-EXECUTIVE SPLIT

### 3.1. Theoretical context

Theory about independent Boards has developed from the notion of the Board as a watchdog, and is central to the 'agency' model of the Board. The underlying thesis is that outside directors are better, more objective monitors of managerial behaviour and, therefore, firms with greater outside representation on the Board are run more in the interests of the firm's members and less in the interests of self-serving managers. According to this view, the independence of the Board increases the likelihood that the CEO will be replaced in the event that they are incompetent. In contrast, executive (or non-independent) directors may either be the CEO, or at least may not have the will to terminate the CEO.<sup>6</sup>

Expanding literature attempts to link the composition of the Board of directors to firm performance<sup>7</sup> and this view has been encoded in various 'best practices' and 'standards' in recent years, including the ASX's *Principles of Good Corporate Governance and Best Practice*<sup>8</sup>, the Australian Standards' AS 8000 *Good Governance Principles*,<sup>9</sup> and the US Business Round Table's *Principles of Corporate Governance*.<sup>10</sup> The US Business Round Table, for example, proposes that companies adopt a number of best practices including ensuring that a substantial majority of the Board of directors comprises independent directors both in fact and appearance, and requiring that only independent directors sit on the Board committees that oversee the three functions central to effective governance - audit, corporate governance and compensation.<sup>11</sup> Similarly, the ASX

<sup>5</sup> Survey data on the existence of smaller management groups within NFP boards is discussed in Chapter 6, Board Structure, Procedures and Role.

<sup>6</sup> See, for example, J. Cotter et al., 'Do Independent Directors Enhance Target Shareholder Wealth During Tender Offers?', 1997, 43, *Journal of Fin. Econ.* 195; S. Oster & K. O'Regan, 'Does the Structure and Composition of the Board Matter? The Case of Nonprofit Organisations', Working Paper #04, Working Paper Series, Yale School of Management at <[http://papers.ssrn.com/abstract\\_id=334121](http://papers.ssrn.com/abstract_id=334121)>, p. 4; and J. Lawrence & G. Stapledon, 'Do Independent Directors add value?' 1999, Research Report, Centre for Corporate Law and Securities Regulation, University of Melbourne.

<sup>7</sup> M. Bradley, C. Schipani, A. Sundaram & J. Walsh, 'The Purpose and Accountability of the Corporation in Contemporary Society: Corporate Governance at a Crossroads', 1999, 62:3 *Law and Contemporary Problems* 9, p. 12.

<sup>8</sup> See ASX Corporate Governance Council - Principles of Good Corporate Governance and Best Practice Recommendations, March 2003, at <<http://www.asx.com.au/corporategovernance>>.

<sup>9</sup> These can be downloaded at <[www.standards.com.au](http://www.standards.com.au)>.

<sup>10</sup> These can be found at <<http://www.brtable.org/document.cfm/704>>.

<sup>11</sup> Business Round Table Principles of Good Governance, p. 19 at <<http://www.brtable.org/pdf/704.pdf>>.

## Chapter 5- Board Size, Composition, Remuneration and Experience

Guidelines recommend 'a majority of the Board should be independent', that 'the chairperson should be an independent director', and that 'the roles of chairperson and chief executive officer should not be exercised by the same individual'.<sup>12</sup> Much of the debate, at least in the Australian context, is around what constitutes and 'independent director'. It is clear that simply being a non-executive director is not, of itself, sufficient.

The relevance of these 'standards' and of the underlying theory for NFP companies is a matter for further exploration.

### 3.2. Proportion of executive and non-executive directors

#### 3.2.1. SURVEY QUESTION

7.2.1 Of the total number of directors (as stated in question 7.1.1), how many are non executive directors (that is, those directors who are not employees of the company)?

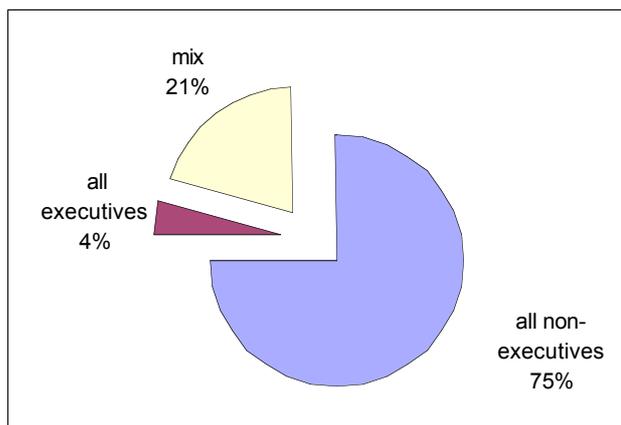
.....(write the total number of non-executive directors)

Number of respondents = 1650

#### 3.2.2. SURVEY RESULTS

Three-quarters (75%, n=1234) of respondent companies had Boards comprised entirely of non-executive directors.

Figure 4: Executive, non-executive split



#### 3.2.3. COMPARISON WITH 'TOP 100' COMPANIES

The typical pattern for the 'Top 100' companies is a majority of non-executive directors and one or two executive directors.<sup>13</sup> Only one of the 'Top 100' had a Board comprised entirely of non-executive directors and this was due to the resignation of the CEO just prior to the sample date. By way of contrast, 75% of NFP respondents had Boards comprised entirely of non-executive directors. This was a higher figure than that found in the earlier Steane & Christie study<sup>14</sup> and may reflect a trend towards greater use of non-executive directors. The NFP survey data also showed that 21% of NFP companies in the sample had a mix of executive and non-executive directors and only 4% were comprised solely of executive directors.

<sup>12</sup> See ASX Principles of Good Corporate Governance and Best Practice, n. 8, recommendations 2.1, 2.2 and 2.3.

<sup>13</sup> Stapledon & Fickling, n. 1, p. 18.

<sup>14</sup> Steane & Christie found 55% of Boards were comprised exclusively of non-executive directors, see n. 3, p. 54.

3.2.4. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Education Related organisations (66%) and Religious organisations (67%) had a higher percentage of executive directors than other respondents. Generally, however, there was little difference between other organisations based on the principal activity.

3.3. Executive directors

3.3.1. SURVEY QUESTION - NUMBER OF EXECUTIVE DIRECTORS

7.3.1 Of the total number of directors (as stated in question 7.1.1), how many are executive directors (that is, those directors who are employees of the company)?

.....(write the total number of executive directors)

Number of respondents = 1649

3.3.2. SURVEY RESULTS

Around three-quarters (77%, n=1266) reported having no executive directors. Twenty-nine per cent of respondents said that all the directors on the Board of their organisation were executive. On average, 6% of the directors of the Boards were executive.

Table 2: Number of executive directors on Board

<i>Per cent of executive directors</i>	<i>Frequency</i>	<i>Per cent</i>
0	1266	76.8
1–33%	293	17.8
34–66%	53	3.2
67–99%	8	0.5
100%	29	1.8
no answer given	39	
Total	1688	100

3.3.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

The only significant difference based on the principal activity of the organisations was for Religious organisations. The average number of executive directors for Religious organisations was 20%, which was considerably higher than the overall average of 6%.

3.3.4. SURVEY QUESTION - FULL OR PART-TIME EMPLOYEES

7.3.2 Of these executive directors, how many are full-time employees and how many are part-time employees? Please write a number, including '0' if applicable, for EACH.

..... full-time ..... part-time

Number of respondents = 367                      Number of respondents = 367

3.3.5. SURVEY RESULTS

As Table 3 indicates, the majority of Boards fall into two groups: those Boards where *all* executive directors are full-time (243 Boards, or 66% of the total), and those Boards where *all* executive directors serve in a part-time capacity (100 Boards, or 27% of all Boards).

## Chapter 5 - Board Size, Composition, Remuneration and Experience

**Table 3: Executive directors' employment status**

<b>Boards in which....</b>	<b>Number of Boards</b>	<b>Per cent of all Boards</b>
all executive directors are full-time employees	243	66
majority of executive directors are full-time	6	2
half are full-time, half are part-time	11	3
majority are part-time	7	2
all executive directors are part-time	100	27
total	367	100

### 3.3.6. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Again, there were significant differences based on the size of the organisation. An average of 66% of executive directors of small organisations were full-time employees, whereas an average of 93% of the executive directors of large organisations were full-time employees: a difference of 27%.

## 3.4. Chair

### 3.4.1. SURVEY QUESTION

7.3.3 Is the Chairperson of the Board an executive director (that is, company employee) or a non-executive director (that is, not a company employee)?

- executive director OR
- non-executive director

*Number of respondents = 1532*

### 3.4.2. SURVEY RESULTS

The vast majority of Chairs of the Board, 91% (n=1394), were non-executive directors.

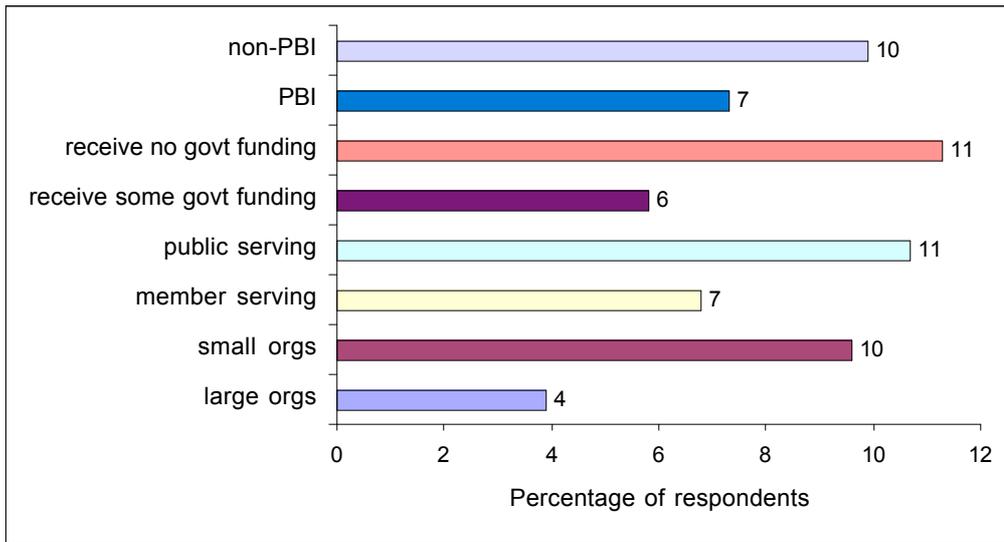
**Table 4: Is the Chair of the Board executive or non-executive?**

<b>Executive / non-executive</b>	<b>Frequency</b>	<b>Per cent</b>
executive director	138	9
non-executive director	1394	91
no answer given	156	
total	1688	100

### 3.4.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

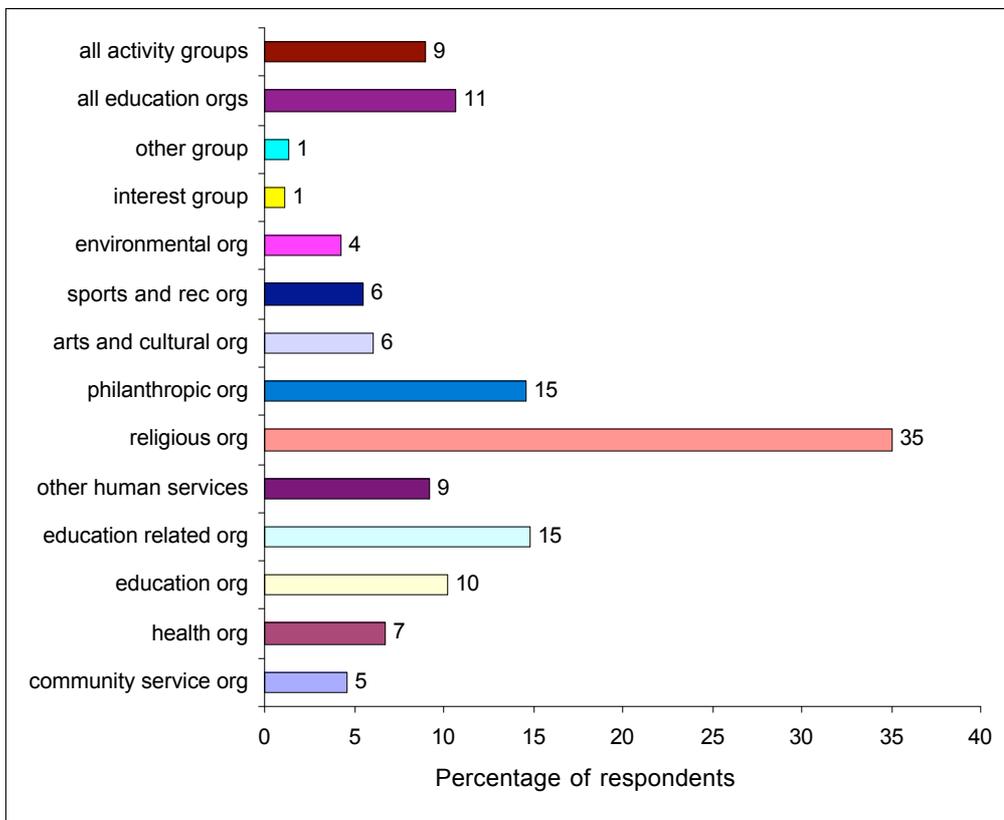
Bearing in mind the small number of respondents reporting that the Chair was an Executive director (n=138), there were considerable differences between small and large organisations, with large organisations less likely to have an executive Chair (10% vs 4%). Those organisations receiving no government funding were also much more likely to have an executive Chair (11% vs 6% overall).

Figure 5: Chair of the Board is an executive, based on key indicators



Again, bearing in mind the small number of respondents with an executive Chair (n=138), there were also considerable differences between organisations based on their principal activity. Figure 6 shows that Religious organisations are by far the most likely to have an executive Chair - just over a third of the Chairs of Religious organisations were executive. In contrast, only 1% of the Chairs of Interest Group organisations were executive, demonstrating that there are very different practices with regards to the independence of Chairs in the NFP sector.

Figure 6: Chair of the Board is an executive, based on principal activity



## Chapter 5 - Board Size, Composition, Remuneration and Experience

### 3.4.4. OBSERVATION - ASX GUIDELINES

In relation to the respondents whose Chair was an executive director, we note the discussion on this issue in the ASX's *Principles of Good Governance and Best Practice Recommendations*, March 2003. In particular, recommendation 2.2 states that the Chair 'should be an independent director' which would, at the very least, mean a non-executive director.<sup>15</sup>

## 3.5. Chief Executive Office

### 3.5.1. SURVEY QUESTION

7.3.4 Is the Chief Executive Officer (or equivalent) a director (that is, a voting member of the Board rather than a person who attends Board meetings because of their position)?

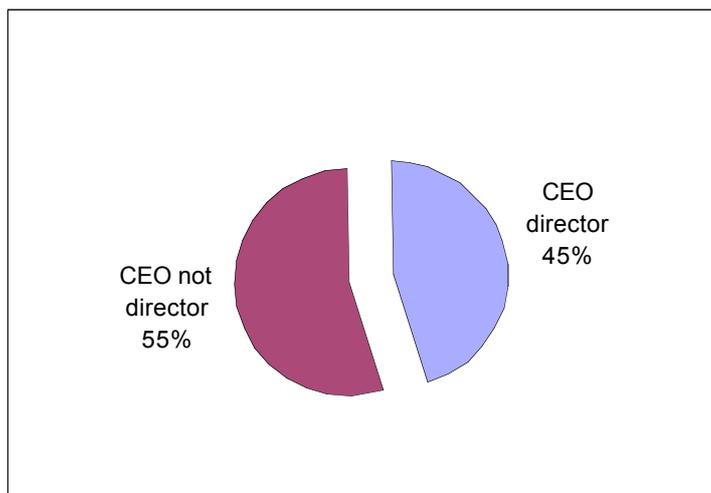
- yes, a Director OR  
 no, not a Director

*Number of respondents = 1531*

### 3.5.2. SURVEY RESULTS

The split between those whose CEO was a director and those whose was not a director was fairly even.

Figure 7: Is the CEO a director?



### 3.5.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Once again there was a very significant difference between small organisations and large organisations. Small organisations were much more likely to have a CEO who was a director (48%) compared to only 23% of large organisations. This suggests that the governance policy of large organisations - possibly their concern to ensure that the Board of directors is independent from management - differs from small, or at least smaller, organisations.

<sup>15</sup> See n. 8.

**4. REMUNERATION**

**4.1. Non-executive directors**

4.1.1. SURVEY QUESTION

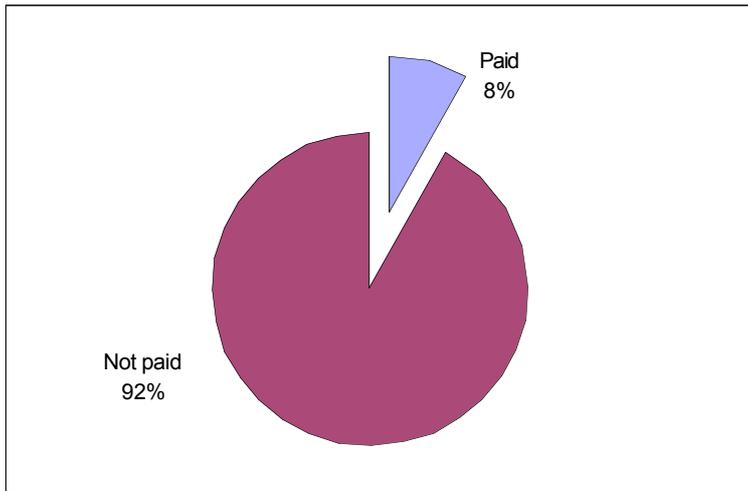
- 7.2.2 Are any of the non-executive directors paid directors' fees (other than out-of-pocket expenses) by the company? 'Yes' or 'No'.
- 7.2.3 If 'yes', please give a general indication of the total annual fees paid to the non-executive director(s) in the company's last financial year.  
\$.....

*Number of respondents = 1665*

4.1.2. SURVEY RESULTS

Eight per cent (n=133) of NFP companies in the sample said that their non-executive directors received payment in addition to out-of-pocket expenses.<sup>16</sup> While there may well be some response error rate within this percentage,<sup>17</sup> it is unlikely to explain the full 8%. There was a large range in the amount these respondents reported paying their non-executive directors (shown in Figure 9): from \$100 to \$480,000 (presumably a total for all their non-executive directors), with 20 respondents paying \$80,000 or more.

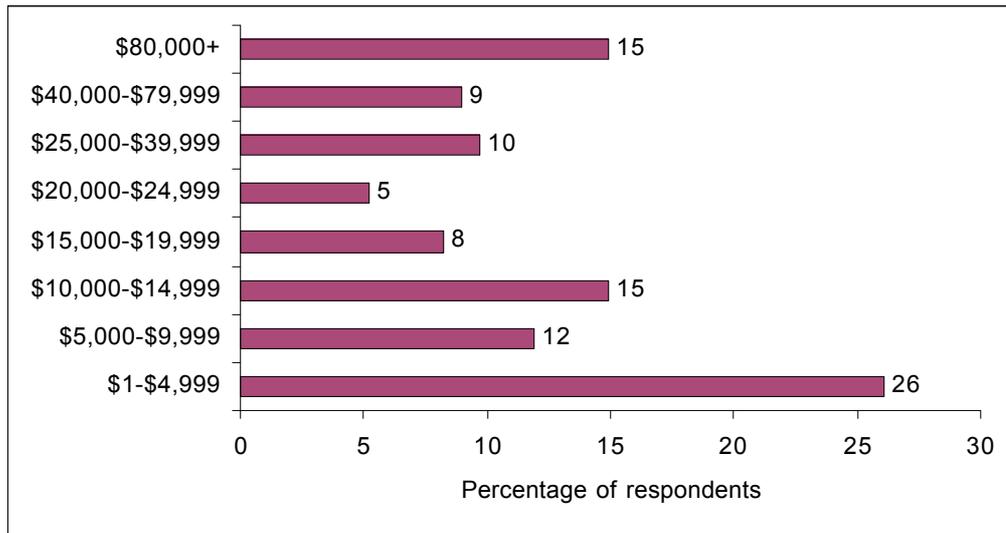
**Figure 8: Non-executive directors paid fees**



<sup>16</sup> Steane & Christie, n. 14, noted that most directors 'appear to volunteer their time, with only six chairs indicating that any sort of remuneration was paid for services', p. 54.

<sup>17</sup> That is, respondents who, despite the wording of the question, answered 'yes' even though all that they pay is in fact a reimbursement of expenses reasonably incurred in, say, attending an interstate Board meeting.

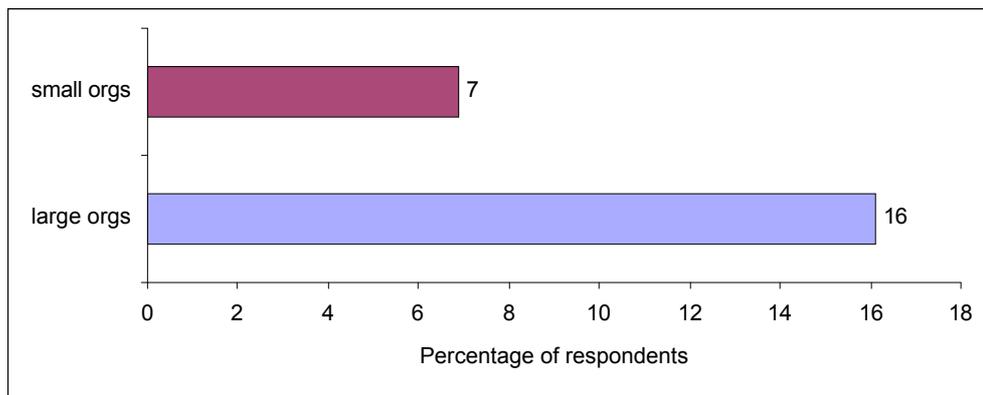
Figure 9: Total amount of fees paid to non-executive directors of those remunerating non-executive directors (n= 134)



Significant differences between respondents

Large organisations (Figure 10) are 9% more likely to pay their non-executive directors than small organisations.

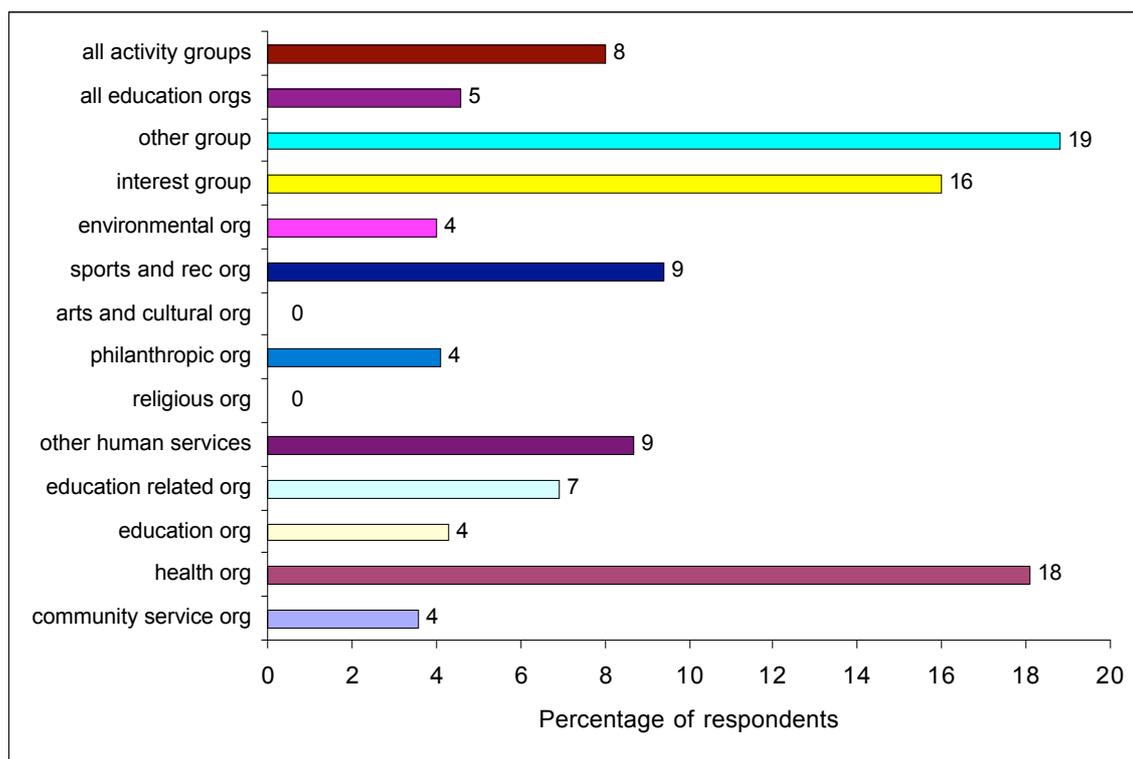
Figure 10: Non-executive directors paid fees, based on size



There are substantial differences between activity groups in the payment of their non-executive directors (Figure 11). Health organisations, Other organisations (which includes business services, accommodation, books and publishing and emergency services) and Interest Group organisations are far more likely than other organisations to pay their non-executive directors. Arts and Cultural organisations and Religious organisations almost never pay their non-executive directors.

Drilling down further, the data supports anecdotal evidence that there is a growing trend among some of the NFP employment agencies to pay their non-executive directors - 17% of employment agencies (n =24) said that they paid their non-executive directors, compared with the overall rate of 8%.

Figure 11: Non-executive directors paid fees, based on principal activity



## 4.2. Should non-executive directors be paid?

### 4.2.1. SURVEY QUESTION

7.2.4 If 'no', do you believe any of the company's non-executive directors should be paid director's fees?

- yes
- no

Number of respondents = 1506

### 4.2.2. SURVEY RESULTS

The respondents reporting that they did not pay their non-executive directors were asked whether they thought non-executive directors should be paid. Of this group the vast majority, 85% (n=1282) said that they should *not* be paid.

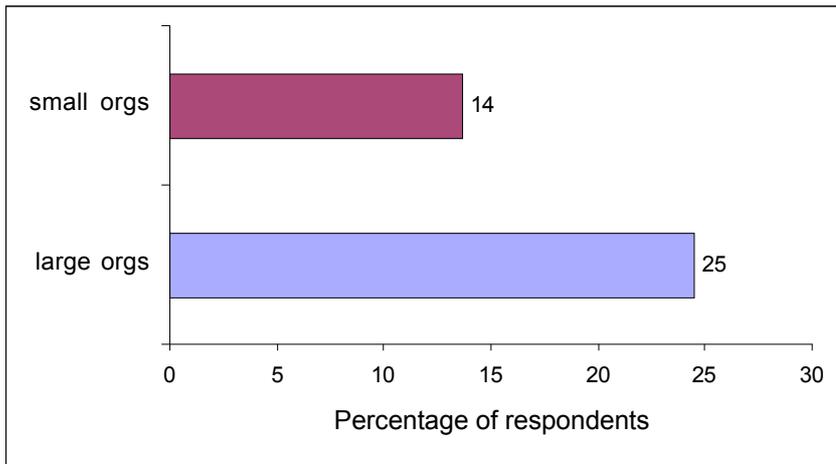
### 4.2.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

There was a substantial difference between large and small organisations on this point (11%). The larger the organisation, the greater the responsibility entailed for the Board. This may provide greater argument for remunerating directors. Many large NFPs can be at least as complex as 'for-profit' businesses of equivalent size, and the legal duties and liabilities are the same. (See Chapter 8, Disclosure).

Large NFP organisations are often able to attract highly experienced and high profile members of the corporate world to sit on their Boards, and this can bring significant advantages to the organisation. For example, in 2001 the Salvation Army's Board included Reserve Bank of Australia director Jillian Broadbent, Sydney City Council identity Kathryn Greiner, millionaire Ian Darling and Caltex Chair Malcolm Irving. These high-flyers sit side by side on the Board with uniformed Salvation Army officers and ordained ministers of religion.<sup>18</sup> For an organisation of the Salvation Army's size, it is important to have directors who are accustomed to managing large organisations and large amounts of money.

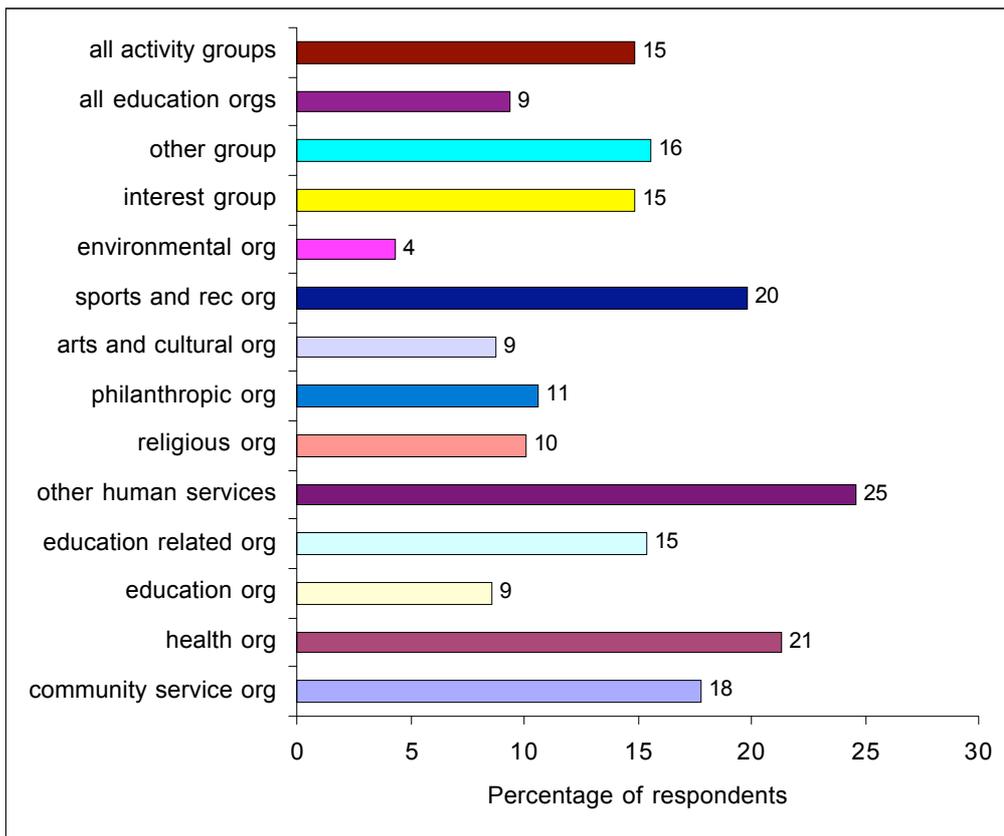
<sup>18</sup> 'Australia - Salvation Inc - Inside the Salvation Army', *The Australian*, Dossier, 23 June 2001.

Figure 12: Should non-executive directors be remunerated, based on size?



There were also substantial differences between organisations based on their principal activity. Figure 13 shows that respondents from Health organisations, Sports and Recreation organisation and Other Human Services organisations were most likely to think that non-executive directors should be paid.

Figure 13: Should non-executive directors be remunerated, based on principal activity?



#### 4.2.4. OBSERVATION

That NFP Board members are, on the whole, unpaid volunteers may have a variety of consequences affecting the management of NFP organisations; in particular, the relationship and roles of Board members and staff. Dr Diana Leat<sup>19</sup> outlines a few:

- the voluntary status of the directors may mean that they have limited time for meetings and for preparation;
- as volunteers themselves, they may explicitly or implicitly believe that staff pay and hours should also include a voluntary element and may be resistant to the notion of offering competitive salaries;
- the ethos of voluntarism, subscribed to and exemplified by Board members, may lead them to distance themselves from the responsibilities of being employers leaving the employment function to staff themselves to handle; and
- more generally, the volunteer Board members may display a bias against 'managerialism' and/or the need for professional staff.

Leat also observes that a difficulty for NFP organisations may stem from the fact that Board members tend to be drawn from limited social strata. In many instances these are very different from those of both staff and users of the organisation's services. She speculates that the voluntary nature of the Board members' role may contribute to a preponderance of Board members from high social strata. This is insofar as only those with another source of income, or a job or position which permits paid time off, are likely to be available. The payment of Board members may enlarge the potential social pool from which Board members can be drawn. Whilst our data did not ask what the social strata of the NFP service users/clients was, it did ask about the social profile of the directors. The skills, age, ethnicity and gender of directors are reported under Heading 8. (It was not possible to inquire into the 'class' of the directors, as such an inquiry is not suitable for survey based studies of this type.) In summary, this data shows that there is a lack of diversity amongst directors - they are overwhelmingly males and aged between 40 and 72 years of age. We suggest that it is unlikely that this predominance is mirrored in users/clients of the NFP sample.

While acknowledging the limitations of drawing directors from different social strata from members, clients and employees, there may be some advantages. It may be useful to have directors whose experience, outlook and interests are different from those of management. These members may be detached from operations, making them more effective and more able to challenge the overall management strategy. They may also have greater experience in management, law and finance that are needed for the organisation in a competitive funding environment.

### 4.3. Disclosure of payment

#### 4.3.1. SURVEY QUESTION

10.10.5 If any directors' fees are paid, do the company's accounts disclose this fact?

- yes
- no

*Number of respondents = 777*

#### 4.3.2. SURVEY RESULTS

With regard to disclosure, 83% of respondents said that if any directors' fees were paid, (that is, whether paid to non-executive directors or executive directors) it was disclosed in the company's annual accounts (n=645). It would have been better to ask about disclosure of executive and non-executive remuneration as separate questions.

<sup>19</sup> D. Leat, *Managing Across Sectors: Similarities and Differences Between For-Profit and Voluntary Non-profit Organisations*, City University Business School, 1993, pp. 27–9.

## Chapter 5 - Board Size, Composition, Remuneration and Experience

### 4.3.3. OBSERVATION

It should be borne in mind that those companies holding a name licence under s 150 of the *Corporations Act 2001*(Cth) must have a constitution that prohibits the company 'paying fees to its directors'.<sup>20</sup> For NFP companies without a name licence, there is no general *Corporations Act* requirement to disclose directors' fees in the annual directors' report - s 300A(1)(c) only applies to listed companies.<sup>21</sup> Thus, the majority of respondents who say that they disclose the payment of directors' fees in their annual accounts (83%) are doing so voluntarily, or at least, not because of any *Corporations Act* requirement.

The disclosure of directors' remuneration is also discussed in Chapter 8, Disclosure. We believe it is an important area that warrants further consideration.

#### Issue for further deliberation: Disclosure of directors' remuneration

Where directors, trustees or committee members or related parties (that is, relations or associates) receive benefits of any kind (including salaries, fees, honoraria, and in-kind compensation), these should be publicly disclosed. Consideration should be given to the application of Chapter 2E of the *Corporations Act 2001* (Cth)(related party transactions) to all NFP organisations. That is, removing the existing exemption for companies limited by guarantee that hold a licence to omit the word 'limited' from their name. This would be in addition to finding the most effective way of ensuring that all NFP organisations disclose remuneration of directors and officers.

## 4.4. Non-executive directors paid for other services

### 4.4.1. SURVEY QUESTION

10.10.6 Are any of the non-executive directors or their associates paid by the company for other work, for example, for legal or accounting advice?

yes

no

10.10.7 If 'yes', please give a general indication of the type of work undertaken.....

*Number of respondents = 1659*

### 4.4.2. SURVEY RESULTS

The vast majority (86%, n=1429), said non-executive directors or their associates had not been paid for services.

### 4.4.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

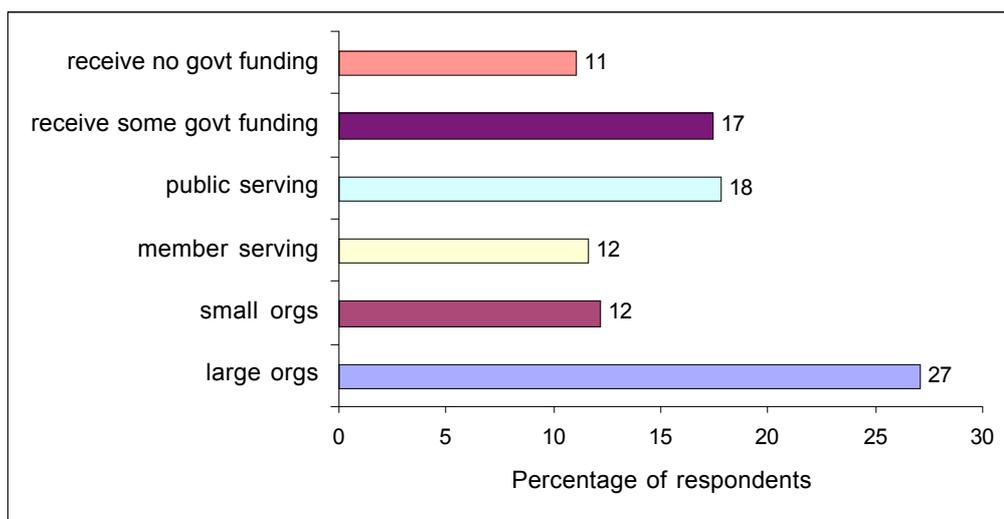
These figures change considerably when organisations are distinguished on the basis of whether they are small or large, receive government funding or not, and whether they are member-serving or public-serving. The biggest difference is between small and large organisations - a 15% difference (shown in Figure 14). This is quite significant given that overall only 14% of all respondents said that non-executive directors had been paid for services. It is not surprising that larger organisations - that is, those with greater income and assets, might be able to pay their directors for any services they render to the organisation.

The fact that there is a difference between those that receive government funding and those that do not may be because of the correlation between the receipt of government funding and the size of income (and therefore assets, etc.) of the organisation (Chapter 2, Profile Data).

<sup>20</sup> However, executive directors, for example, the CEO, can be paid in their capacity as an employee rather than as a director.

<sup>21</sup> Note: (a) s 300(1)(d) requires share options granted to directors as part of their remuneration to be disclosed in the annual directors' report; and (b) there is a general requirement for all companies (s 202B(1)) that directors' remuneration must be disclosed if those members with 5% or more of the votes, or 100 or more members, pass a resolution requiring the disclosure.

Figure 14: Are any of the non-executive directors paid for other work, based on key indicators?



4.4.4. OBSERVATION

Paying a director for providing other services to the organisation (for example, legal advice or training) may, in the circumstances, be of benefit to the organisation. In fact, it may mean that the services are obtained at a discount to what the organisation would pay if the services were provided by an ‘outsider’. However, there is potential for abuse. This concern underlies the related party transaction provisions of the *Corporations Act 2001* (Cth).<sup>22</sup> The related party transaction provisions require member approval (after full disclosure and exclusion of the related party from voting) *unless* one of a number of exceptions apply. The main exception that is of relevance is where a financial benefit is given on ‘arm’s length’ terms.<sup>23</sup> If the terms are no more favourable than would be given by the company to an outsider, then member approval is not required.

While the related party transaction provisions are aimed at protecting members from potential abuses, these provisions do not apply to all NFP companies limited by guarantee. Those NFP companies limited by guarantee that hold a licence to omit the word ‘Limited’ from their name<sup>24</sup> are not legally required to comply with the related party transaction provisions. This follows from para. (b) of the definition of ‘public company’ contained in the *Corporations Act 2001* (Cth), s 9.

This continued differential treatment is hard to understand. However, we do not believe it is simply a matter of changing the definition in s 9 so that all companies limited by guarantee are covered. The related party transaction provisions contained in the *Corporations Act* are complex and not easily understood. The NFP context is different and that must be taken into account in order to properly deal with potential conflicts of interest. As Professor De Mott states:

...it is foolish to import for-profit norms respecting self-dealing generally into the nonprofit context. Governance mechanisms are so much weaker in the nonprofit sector that loose controls on self-dealing create unacceptably high risks of misconduct. Such misconduct, if it becomes visible, has reputational consequences unlikely to be restricted to a particular nonprofit. Betrayed once, donors’ altruism may be jeopardized and all nonprofits will suffer as a result.<sup>25</sup>

The issue of how best to regulate or deal with ‘self-dealing’ or potential conflicts of interest is linked closely with the issues of disclosure and stakeholders, and is also discussed in Chapters 7 and 8 of this Report.

<sup>22</sup> See s 207 *Corporations Act 2001* (Cth) that states ‘The rules in this Chapter are designed to protect the interests of a public company’s members as a whole, by requiring member approval for giving financial benefits to related parties that could endanger those interests’.

<sup>23</sup> See s 210 *Corporations Act 2001* (Cth).

<sup>24</sup> See *Corporations Act 2001* (Cth), ss 150–1.

<sup>25</sup> See D.A. DeMott, ‘Self Dealing Transactions in Nonprofit Corporations’, 1993, 59 *Brooklyn Law Review* 13947, p. 147.

**Issue for further deliberation: disclosure of payments to directors**

Where directors, trustees or committee members or related parties (that is, relations or associates) receive benefits of any kind (including salaries, fees, honoraria, and in-kind compensation), these should be publicly disclosed. Consideration should be given to the application of Chapter 2E of the *Corporations Act 2001* (Cth) (related party transactions), or possibly new conflict of interest type-provisions, to all NFP organisations. That is, removing the existing exemption for companies limited by guarantee that hold a licence to omit the word 'limited' from their name. This would be in addition to finding the most effective way of ensuring that all NFP organisations disclose remuneration of directors and officers.

## 5. COMPANY SECRETARY

### 5.1. Is the company secretary a director, employee or person from outside the company?

#### 5.1.1. SURVEY QUESTION

12.1 Is the company secretary (appointed for the purposes of the Corporations Act): (please tick only one box)

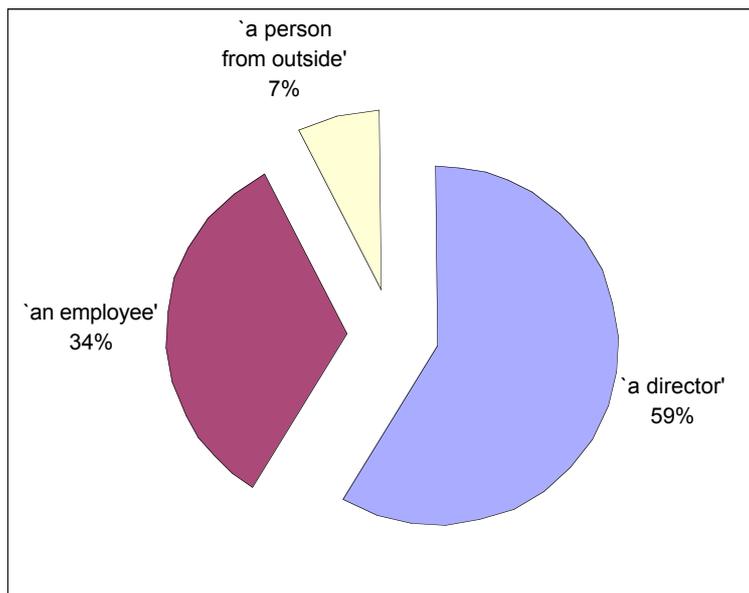
- a director
- an employee
- a person from outside the company

Number of respondents = 1629

#### 5.1.2. SURVEY RESULTS

For 951 respondents (59%) the company secretary was a director, for 557 respondents (34%) the company secretary was an employee, and for 121 respondents (7%) the company secretary was a person from outside the company.

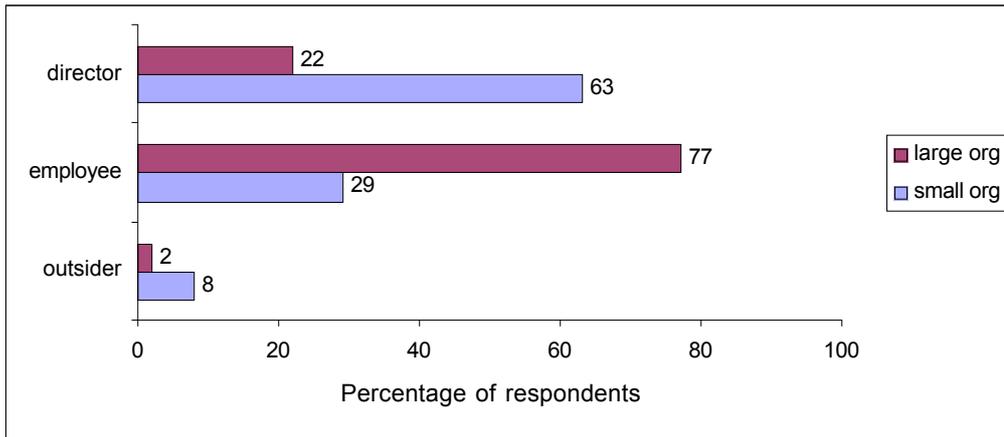
Figure 15: Company secretary



5.1.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

These figures look very different once the data is cross-tabulated based on the size of the organisation. Figure 16 shows that only 22% of respondents from large organisations said the company secretary was a director, compared with 59% overall. In contrast, 77% of respondents from large organisations said the company secretary was an employee, compared with 34% overall. This data shows that large organisations are in a better position to employ someone to fulfil the role of the company secretary, which in turn means that greater resources are available to their Boards and that directors' time is freed up to concentrate in other key Board functions. However, in a small organisation (as in small 'for-profit' companies) there may not be a significant role for a company secretary. There was no control group of 'for-profit' companies, so we are not able to say if this is a distinguishing feature of NFP companies.

Figure 16: Company secretary, based on size



5.2. Company secretary's experience and training

5.2.1. SURVEY QUESTION

12.2 Does the company secretary have any experience or training in: (you may tick more than one box or none at all)

- law
- accounting
- management
- other (please specify).....

Number of respondents = 1625

5.2.2. SURVEY RESULTS

Seventy per cent of respondents said that the company secretary had experience in management, 45% said that he/she had experience in accounting, and 20% said the company secretary had experience in law.

5.2.3. OBSERVATIONS

For the majority of respondents, a director is performing the dual role of director/company secretary. This is particularly so in small organisations. Given that the majority of directors are volunteer non-executives, the need to prepare agendas and Board papers, to record minutes of meetings, and to keep abreast of ASIC filing obligations etc. could be seen as a considerable extra commitment. We note that Chartered Secretaries Australia<sup>26</sup> run training courses for company secretaries of NFP companies, but this role could be expanded with greater access for those outside the major cities. The independent NFP advisory body recommended in this Report (see

<sup>26</sup> A professional body for company secretaries, see <<http://www.caaust.com/>>.

## Chapter 5 - Board Size, Composition, Remuneration and Experience

Chapter 4, Regulatory Framework) could liaise with professional bodies (such as Chartered Secretaries Australia) in this regard.

A plain-language guide outlining the general obligations of NFP companies (as recommended in Chapter 4, Regulatory Framework) could be of great assistance to the company secretary, especially given that only 20% said that they had experience in law.

### 6. RECRUITING AND RETAINING DIRECTORS

#### 6.1. Method of appointment

##### 6.1.1. SURVEY QUESTION

7.5.1 Of the total number of directors currently appointed, how many are: (*please put a number of a zero on each line.*)

.....appointed by members

*Number of respondents = 1622*

.....appointed by an organisation or individual (for example, pursuant to a clause in the company's constitution)

*Number of respondents = 1647*

.....appointed by the Board (for example, to fill a casual vacancy or co-opted for a particular skill)

*Number of respondents = 1643*

##### 6.1.2. SURVEY RESULTS

The practices concerning the appointment of directors amongst NFP companies are quite diverse:

- the majority of organisations (56%) said that all directors are appointed by members (Table 5). However, 24% of respondents said that members appointed none of their directors
- twenty per cent of respondents said some directors were appointed by an organisation or individual (for example, pursuant to a clause in the company's constitution) (Table 6). Eight per cent of these respondents said that an organisation or individual appointed all the directors
- twenty-eight per cent of respondents said that the Board appointed some of the directors. Of these, 12% said that the Board appointed the entire Board (Table 7).

**Table 5: Percentage of directors appointed by members**

<i>Per cent appointed by members</i>	<i>Per cent</i>
0	23.5
>20	1.5
>40	2
>60	5
>80	5
>80 but <100	7
100	56
no answer given	66 respondents
total	100

Table 6: Percentage of directors appointed by an organisation or individual

<i>Per cent appointed by an organisation or individual</i>	<i>Per cent</i>
0	80
>20	3
>40	3.5
>60	2.5
>80	2
>80 but <100	1.5
100	7.5
no answer given	41 respondents
total	100

Table 7: Percentage of directors appointed by the Board

<i>Per cent appointed by Board</i>	<i>Per cent</i>
0	72
>20	8
>40	4
>60	1.5
>80	1.5
>80 but <100	1
100	12
no answer given	45 respondents
total	100

### 6.1.3. ADDITIONAL FEEDBACK

After the Summary of Preliminary Findings for the Project was released in March 2003, we received this feedback from the CEO of a large, well established dementia and aged care organisation. His comment highlights the difficulties of either a solely member-appointed or solely director-appointed Board:

At one extreme [organisation A] for example has an Association that is also the Board. To do that job well, you need excellent and continuous and rigorous succession planning systems and appraisal systems. I know that one of their Directors is tasked with that job. At the other end of the spectrum you have, say, [organisation B], where anyone who wants to pay \$25 can become a member and participates in AGMs and elects Boards. That is a dangerous model that leads to actual or potential instability. You and 50 of your mates could take over [organisation B] and change the course of what they are doing. Even if that does not occur, you can get a constantly changing of the guard at Board level.

My organisation is somewhere in between. An Association of about 20 elects a Board, all members of which must be members. The challenge is identifying the role of the Association members and that is achieved through sub-committees and, secondly, as you identified, the challenge of getting good Board members.

### 6.1.4. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

There was a significant difference between member-serving and public-serving organisations in who appointed the majority of Board members. Public-serving organisations were significantly (16%) more likely than member-serving organisations to have directors appointed by the existing Board, whereas, members were more likely (19%) to appoint directors in a member-serving organisation. These results might have been anticipated, as it might be assume that directors would be drawn from, and voted on by, the membership of a member-serving organisation.

## Chapter 5- Board Size, Composition, Remuneration and Experience

### 6.1.5. OBSERVATION: COMPARISON WITH UK CHARITIES

It would have been interesting to inquire into the methods used to advertise and recruit Board members. The Cornforth study found that by far the most common way of finding and recruiting new Board members is through word of mouth and networking. This method was used by about 93% of UK charities, with little variation between charities of different size. The next most common method was using the charities' own communications, such as newsletters, which was used by about 24% of charities overall. External advertising for Board members was used by about 4% of charities overall, but this figure varied quite widely between 2.5% in the smallest charities to just over 20% in the largest. Only 1% of charities used some form of external recruitment agency or brokerage to help find trustees.<sup>27</sup>

## 6.2. Board elections contested

### 6.2.1. SURVEY QUESTION

7.5.2 In your experience of the company, are Board elections contested?

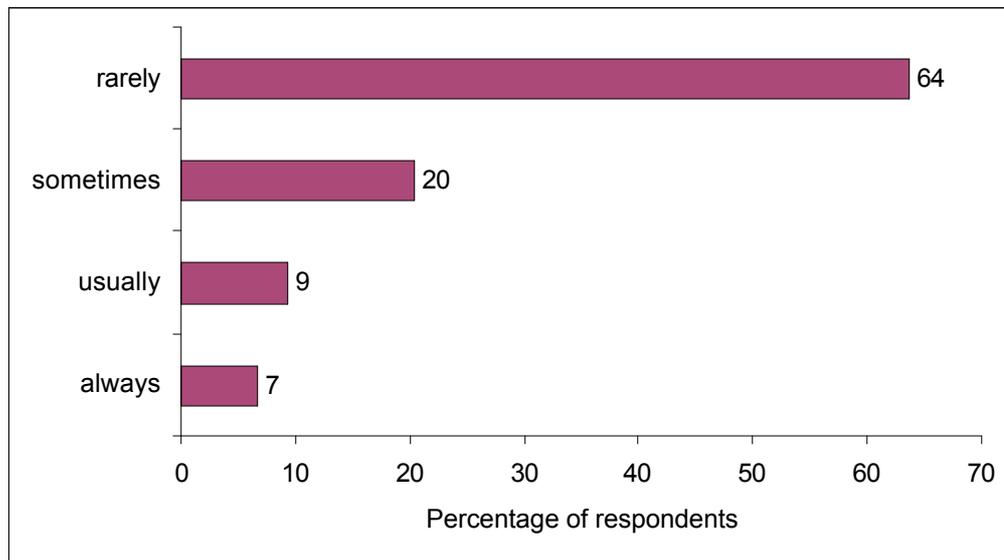
- always
- usually
- sometimes
- rarely

Number of respondents = 1611

### 6.2.2. SURVEY RESULTS

The majority of organisations (64%, n=1024) said that elections were 'rarely' contested. Twenty percent said that elections were 'sometimes' contested. Seven percent (n=108) of respondents said that Board elections were 'always' contested.

Figure 17: Are Board elections contested?



### 6.2.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

When the categories 'always' and 'usually' were combined, there was a significant difference between member-serving and public-serving organisations (difference of 17%). Only 7% of respondents from public-serving organisations said that Board elections were 'always' or 'usually' contested, compared with 24% of member-serving organisations. This may reflect factional tendencies in member-serving organisations, but further qualitative research would be instructive.

<sup>27</sup> See Cornforth n. 4 at p. 9.

### 6.3. Problems recruiting Board members

#### 6.3.1. SURVEY QUESTION

7.8.2 Has there ever been difficulty **recruiting** Board members?

yes

no

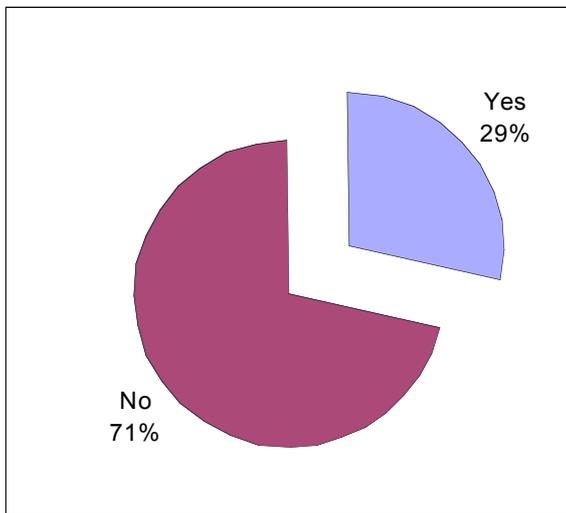
Number of respondents = 1560

7.8.3 If 'yes', why?

### 6.4. Survey results

Nearly a third (29%, n=450) of respondents reported difficulty recruiting directors.

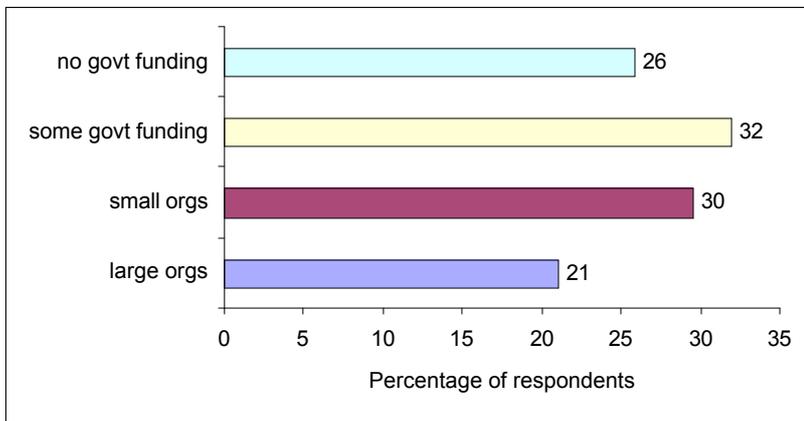
Figure 18: Ever had difficulty recruiting Board members?



#### 6.4.1. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

As might be expected, small organisations were more likely to have trouble recruiting directors than large organisations (30% vs 21%), as were those organisations not receiving government funding compared with those that do (26% vs 32%). This is to be expected given the correlation between government funding and size.

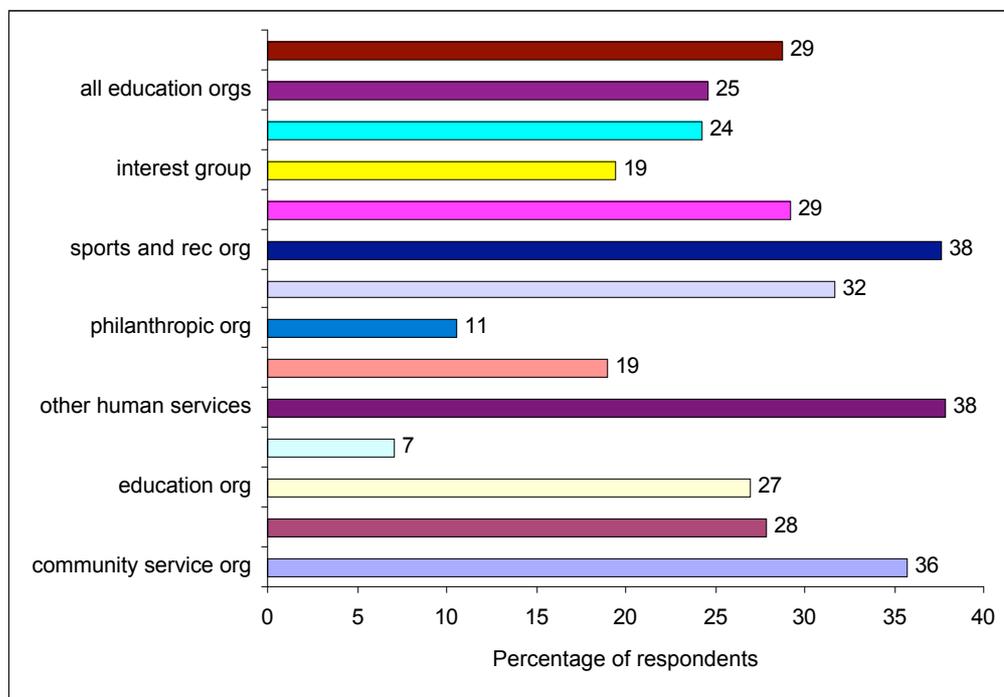
Figure 19: Difficulty recruiting directors, based on key indicators



## Chapter 5 - Board Size, Composition, Remuneration and Experience

Thirty-eight percent of both Sports and Recreation organisations and Other Human Services reported difficulty recruiting directors. Thirty-six per cent of Community Services organisations, and 39% of Disability Services Organisations (a subset of Community Services organisations) also reported difficulty recruiting directors. In contrast, Philanthropic organisations (11%) and Education Related organisations (7%) seem to have much less difficulty recruiting directors.

**Figure 21: Difficulty recruiting directors, based on principal activity**



### 6.4.2. OBSERVATION: COMPARISON WITH UK CHARITIES

It would be interesting to ascertain whether it has become more difficult to recruit Board members in recent years. The Cornforth survey of charities found that although 60% of Boards reported no change in the difficulty of recruiting Board members, 39% reported that they found it more difficult, compared with 1% saying that it was less difficult. That survey also found that 41% of the smallest charities (income of less than £10,000) compared with 12% of the largest charities (income of £10 million and over) were of the view that recruiting Board members had become more difficult.<sup>28</sup>

## 6.5. Problems retaining Board members

### 6.5.1. SURVEY QUESTION

7.9.1 Has there ever been difficulty *retaining* Board members?

yes

no

*Number of respondents = 1556*

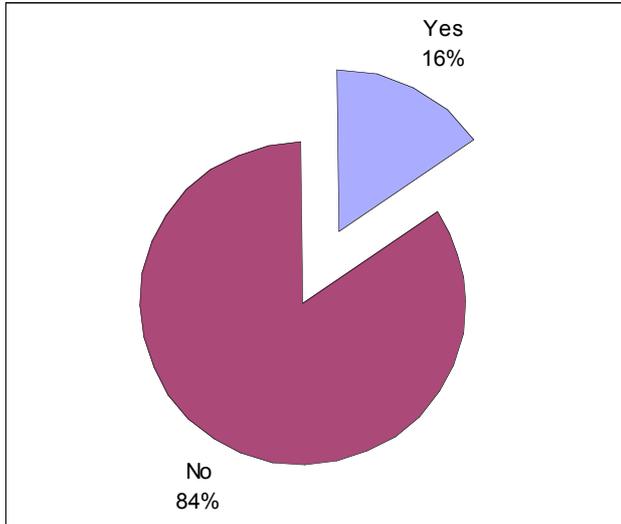
7.9.2 If 'yes', why?

<sup>28</sup> See Cornforth n. 4, p.9.

6.5.2. SURVEY RESULTS

Once directors are recruited, 16% (n=244) of respondents reported difficulty in retaining them.

Figure 20: Ever had difficulty retaining Board members?



6.5.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Again, small companies were more likely to have difficulty than large companies (16% as against 9%). Twenty-three per cent (n=66) of Sports and Recreation organisations reported problems retaining Board members, which was much higher than the overall figure. Twenty per cent (n=13) of Disability Services organisations (a subset of Community Services organisations) reported difficulty retaining directors.

6.5.4. OBSERVATION

An analysis of the independence of NFP Boards, and the multiple stakeholders they represent, needs to occur in the context of the difficulties NFP companies experience retaining and recruiting directors. Being a director of a NFP company is a big commitment, and NFP Boards often oversee complex service provision organisations. For example, in the case of disability services organisations or aged care, for example, the responsibility is to ensure not only that the financial aspects of the company are being well run, but also that appropriate standards of care are provided in compliance with legislative requirements and community expectations - considerable responsibility for a voluntary director.

6.6. Unfilled Board positions

6.6.1. SURVEY QUESTION

7.1.2 Are there currently any unfilled Board positions?

- yes
- no

Number of respondents = 1673

7.1.3 If 'yes', what is the total number of current, unfilled Board positions?  
 .....(write the total number of current, unfilled Board positions)

Number of respondents = 441



## Chapter 5 - Board Size, Composition, Remuneration and Experience

### 6.6.2. SURVEY RESULTS

Just under a third (28%, n=467) of respondents said their organisation had unfilled Board positions. If they said they had any unfilled Board positions, respondents were then asked to write the total number of current, unfilled Board positions. The responses are shown in Table 8. For some organisations it would seem a serious problem - 60 respondents said that nearly a third (30%) of positions on their Board were unfilled.

Table 8: Number of unfilled Board positions for those respondents that have any unfilled

<i>Unfilled Board positions</i>	<i>Frequency</i>	<i>Per cent</i>
10% or less	119	27
20% or less	176	40
30% or less	86	19.5
more than 30%	60	13.5
no answer given	1247	
Total	1688	100

## 6.7. Removal of Board members

### 6.7.1. SURVEY QUESTION

7.10.1 Within the last five years, has a director ever been removed from their position on the Board before the expiration of their term? (For example, by a resolution of the members.)

yes

no

*Number of respondents = 1566*

7.10.2 If 'yes', by whom?

7.10.3 Why?

### 6.7.2. SURVEY RESULTS

Only a small number of respondents (5%, n=75) said that a director had been removed from their position on the Board before the expiration of their term in the last five years. There were no significant differences between organisations based on their principal activity.

## 7. STAKEHOLDER REPRESENTATION AT BOARD LEVEL

### 7.1. Observation

The data reported under this Heading concerns the way that NFP organisations structure their Boards to respond to the multiple accountabilities of the organisation. The questions asked in the survey were designed to inquire whether directors had been appointed to the Boards to represent the interests of particular stakeholders.

The voluntary nature of the Boards combined with their multiple and complex accountability foci (for example, their accountability to grant givers, members, clients and regulatory bodies), have been identified by several social science academics as significant impediments to good corporate governance practices in NFP organisations.<sup>29</sup> An UK report titled *Corporate Governance in the*

<sup>29</sup> For example, D. Leat, 'Voluntary Organizations and Accountability: Theory and Practice' in H.K. Anheier and W. Seibel (eds), *The Third Sector: Comparative Studies of Nonprofit Organizations*, New York, Walter de Gruyter, 1990. For a summary of the arguments, see C. McDonald, *Board Members' Involvement in Nonprofit Governance*, Working Paper No 16, Program on Nonprofit Corporations, Queensland University of Technology, 1993. See also A. Twaits, 'The Duties of Officers and Employees in Non-Profit Organisations' (1998) 10 *Bond Law Review* 320.

*Public and Voluntary Sectors*<sup>30</sup> found that the most important issue for NFP organisations is about the balance between performance and the need to respond to those who use the service.

The data reported below shows that it is not uncommon for Board members to be recruited to maximise one particular type of focus, for example, to consumers. While that Board member may possess characteristics uniquely suited to maximising that focus, the capacity for NFP companies to recruit and retain Board members possessing the characteristics to address *all* types of accountability might be limited.<sup>31</sup>

## 7.2. Directors who are substantial donors

### 7.2.1. SURVEY QUESTION

7.5.3 Is any director a substantial donor or an associate of a substantial donor?

yes

no

Number of respondents = 1662

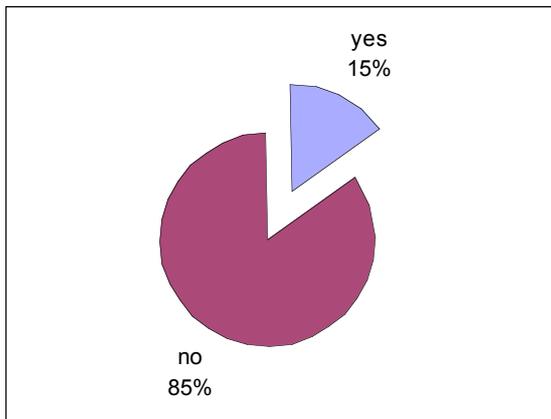
7.5.4 If 'yes', how many directors?

.....(write the total number)

### 7.2.2. SURVEY RESULTS

Fifteen per cent of respondents said that a director on the Board was a substantial donor or an associate of a substantial donor. This significant group highlights a difference between NFP organisations and 'for-profit' companies.<sup>32</sup>

Figure 21: Is any director a substantial donor or an associate of a substantial donor?



### 7.2.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Figure 22 shows that there were substantial differences between small organisations and large organisations in this respect, with small organisations being 6% more likely to have a donor or associate of a donor on the Board. The most significant difference, however, was between public-serving and member-serving organisations. Public-serving organisations are 10% more likely to have a donor or their associate on the Board. This is a very significant difference given that only 15% of respondents overall answered 'yes' to this question.

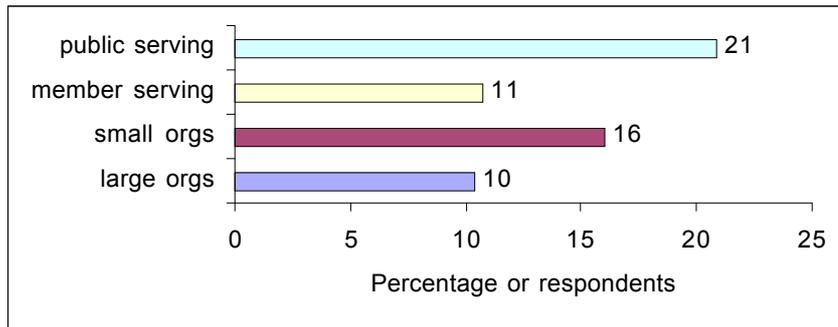
<sup>30</sup> P. Fitzgerald, *Corporate Governance in the Public & Voluntary Sectors*, The Royal Society for the Advancement of Arts, Manufactures and Commerce, 2002, p. 68. See also, 'Charity trustees should be paid says new RSA report', 14<sup>th</sup> February, 2002, RSA Press Releases, at <<http://www.rsa.org.uk/news>>.

<sup>31</sup> See McDonald, n. 15 at p. 3.

<sup>32</sup> Although, 'for-profit' organisations may have lenders on Boards, for example, a Bank representative however, may choose not to because such representation comes with potential directors' liability.

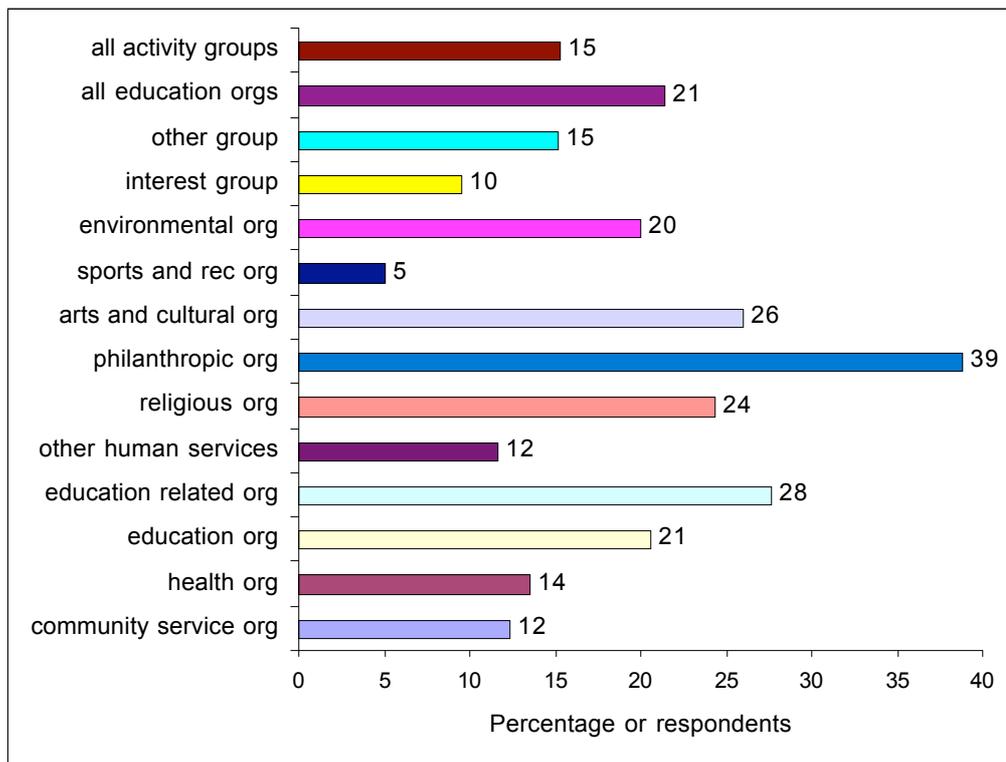
## Chapter 5- Board Size, Composition, Remuneration and Experience

**Figure 22: Director a substantial donor or an associate of a substantial donor, based on key indicators?**



There were also significant differences between organisations based on their principal activity. Thirty percent of Philanthropic organisations had donors or their associates on the Board, as did 26% of Arts and Cultural organisations and 24% of Religious organisations. In contrast, only 5% of Sports and Recreation organisations said that they had donors or their associates on the Board (Figure 23).

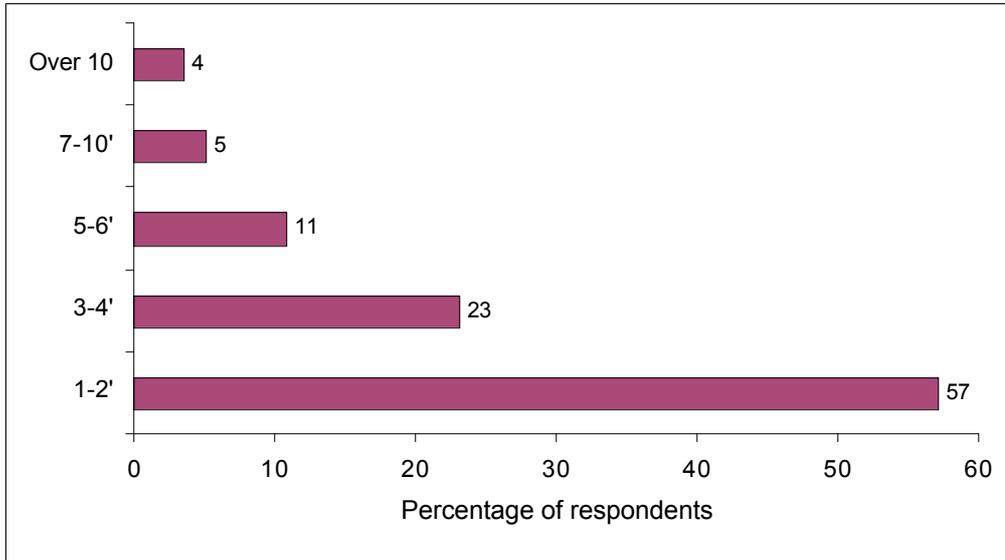
**Figure 23: Is any director a substantial donor or an associate of a substantial donor, based on principal activity?**



### 7.2.4. NUMBER OF DIRECTORS WHO ARE DONORS

Of those organisations that had a director who represented a substantial donor or associate of a substantial donor on the Board (n=254), the mean number of such directors on the Board was three. The majority (57%) had between one and two. The most interesting result was that nine respondents (4%) said that they have over 10 directors on the Board who are substantial donors. The stakeholder issues become very complex in such organisations, from a legal point of view, especially if donors are not also members of the company. The duty of a director is to the company as a whole, and this is defined primarily with reference to the interest of the members.

Figure 24: How many directors are donors? (n=254)



### 7.3. Appointment of directors to represent non-member stakeholders

#### 7.3.1. SURVEY QUESTION

- 7.6.1 Assume that members are one of the company's stakeholders and that all directors represent the interests of members. Has any director been appointed primarily for the purpose of representing the interests of any of the company's other stakeholders (including, but not limited to, other non-member stakeholders listed in question 6)?
- yes
  - no

Number of respondents = 1645

- 7.6.2 If yes, please specify how many directors for which of the stakeholders(s).
- number of directors .....
  - stakeholder .....

Number of respondents = 315

- number of directors .....
- stakeholder .....

Number of respondents = 119

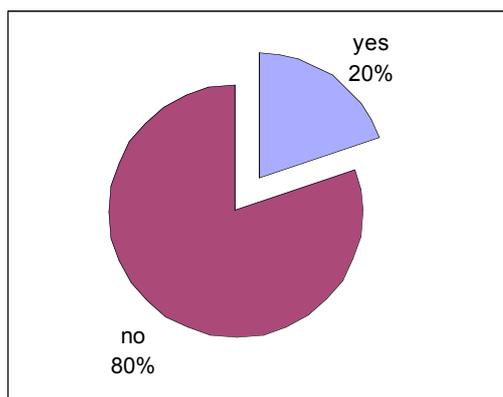
- number of directors .....
- stakeholder .....

Number of respondents = 40

#### 7.3.2. SURVEY RESULTS

The survey data revealed that while the appointment of directors to represent the interest of a particular non-member stakeholder in NFP companies does not occur in the majority of organisations, it is not uncommon. Twenty per cent (n=326) said that a director had been appointed to represent the interests of a particular non-member stakeholder.

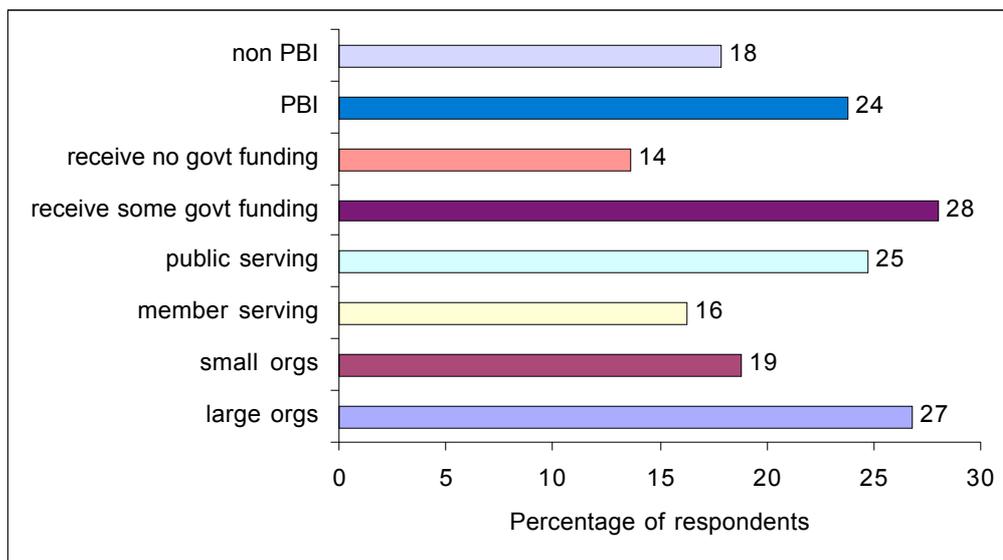
Figure 25: Has any director been appointed to represent the interests of a particular non-member stakeholder?



### 7.3.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Large organisations are 8% more likely than small organisations to have a director who has been appointed to represent the interests of a non-member stakeholder. There was a similar difference between public-serving and member-serving organisations - public-serving organisations are 8% more likely to have non-member stakeholder interests represented on the Board. Likewise, those that receive some government funding were also much more (14%) likely to have a non-member stakeholder represented on the Board than those that receive no government funding.

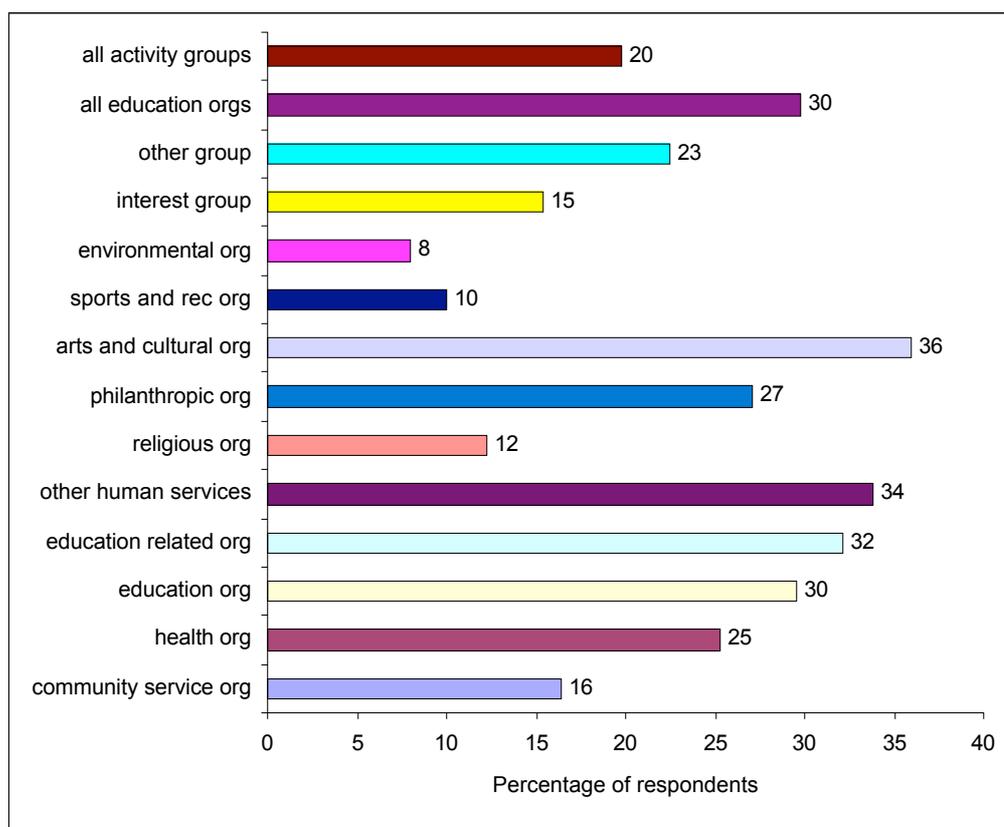
Figure 26: Has any director been appointed to represent the interests of a non-member stakeholder, based on key indicators



Education, Arts and Cultural and Other Human Services organisations are most likely to have a director on the Board who has been appointed to represent the interests of a non-member stakeholder. The difference between Other Human Services organisations and Community Organisations (34% vs 16%) is interesting, as these groups normally follow a similar pattern. The data showed that Religious organisations and Sports and Recreation organisations are unlikely to have non-member stakeholder interests represented in this way.<sup>33</sup>

<sup>33</sup> Only two Environment organisations reported having a director appointed to the Board to represent the interests of a non-member stakeholder. Twenty-three Environmental organisations answered 'no' to this question. Because the sample size is so small, it is not a statistically significant number by which we can determine whether the proportions are likely to remain stable in a larger sample.

Figure 27: Has any director been appointed to represent the interests of a non-member stakeholder, based on principal activity?



7.3.4. NUMBER OF DIRECTORS

Of those organisations that said that a director had been appointed to represent the interests of a particular non-member stakeholder, the mean number of directors that were appointed to represent the interests of non-member Stakeholder A was 3.5, Stakeholder B was 2.8 and Stakeholder C was 2.

7.3.5. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

The mean number of directors that were appointed to represent the interests of non-member Stakeholder A for Religious organisations was 5.4, which was significantly higher than for other organisations based on principal activity.

For those respondents who had at least one non-member stakeholder, we compared the total number of directors on the Board with the number of directors appointed to represent a non-member stakeholder. We wanted to find out whether directors appointed to represent non-member stakeholders constituted a significant proportion of the total number of directors on the Board. Table 9 shows the results.

Table 9: Proportion of non-member stakeholder representatives on Board

<i>Proportion of non-member stakeholders on the Board</i>	<i>Frequency</i>	<i>Per cent</i>
>0 to <25%	93	30.5
25 to <50%	68	22
50 to <75%	39	13
75 to <100%	22	7
100%	84	27.5
total	306	100

## Chapter 5 - Board Size, Composition, Remuneration and Experience

For 28% (n=84) the entire Board was comprised of directors appointed to represent non-member stakeholders. Yet, under the *Corporations Act 2001*(Cth), the *members* (not other stakeholders) are the only group with the power to appoint and remove directors.<sup>34</sup> This tension needs to be further explored in the NFP context.

### 7.4. Representation of certain interests on the Board

#### 7.4.1. SURVEY QUESTION

- 7.6.3 Is there a clause in the company's constitution that provides for certain interests to be represented on the Board?
- yes
- no
- If 'yes', we would appreciate if you could enclose a photocopy of the clause in the Reply Paid envelope with this questionnaire.

*Number of respondents = 1610*

#### 7.4.2. SURVEY RESULTS

In general, where a company had non-member stakeholders represented on the Board, this appears to be provided for in the constitution of the organisation. Seventeen per cent of respondents (n=273) said that the constitution of their organisation provided for certain interests to be represented on the Board. Of those Boards with a clause providing for interests to be represented, 52% have in fact appointed such directors appointed. Thirteen per cent of Boards lacking such a clause, nevertheless had directors appointed to represent particular stakeholder interests.

### 7.5. Representation of suppliers or purchasers of goods and services

#### 7.5.1. SURVEY QUESTION

- 7.7.1 Has any director been appointed primarily for the purpose of representing the interests of a substantial supplier or purchaser of goods/services to/from a company?
- yes
- no
- Number of respondents = 1639*
- 7.7.2 If 'yes', please specify how many directors for which goods/services.
- number of directors .....
- goods/services .....
- number of directors .....
- goods/services .....

#### 7.5.2. SURVEY RESULTS

Representation of suppliers and purchasers is not common. Overall, only 2% of respondents said that a director had been appointed to represent the interests of a substantial supplier. This was much higher for organisations that received some government funding (4%) and for Arts and Cultural organisations (8%).

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<sup>34</sup> See s 203D *Corporations Act 2001*.(Cth)

7.5.3. NUMBER OF DIRECTORS

For those respondents who answered ‘yes’, the mean number of directors that were appointed to represent the interests of a substantial supplier was 2.5.

7.6. Observation: conflicts of interest

The survey data shows that Board members of NFP companies sometimes represent sectional or stakeholder interests (for example, clients or, in the case of a peak body, State or divisional groups). Whilst these directors may not be in the majority, they are not unusual (20%). These directors (known as nominee directors) may find themselves in a position of conflict - conflict between the interests/concerns of their nominators and their legal duties to the company.<sup>35</sup>

The legal framework for the regulation of directors’ conflicts under Australian law involves three levels of regulation - general law principles, the company’s constitution (which can modify the general law principles) and statutory provisions contained in the *Corporations Act 2001* (Cth).<sup>36</sup>

The statutory provisions are more onerous for public companies than private companies. Thus, bearing in mind that a company limited by guarantee is a public company,<sup>37</sup> the issue of compliance with these statutory provisions will be pertinent to NFP companies. However, any concerns NFP companies have will not be homogeneous because, even within the category of companies limited by guarantee, there is differential treatment. Companies limited by guarantee that hold a licence to omit the word “limited” from their name<sup>38</sup> are not bound to comply with the related party transaction provisions contained in Chapter 2E.<sup>39</sup> (The related party transaction provisions aim to prevent public companies from entering into uncommercial transactions with related parties who include, for example, the company’s own directors.) The existence of this differential treatment and, indeed, the appropriateness of applying ‘for-profit’ company standards in relation to related party transactions to NFP companies, is an important research topic,<sup>40</sup> which deserves further attention.

8. GENDER, AGE AND ETHNICITY

8.1. Survey question

7.8.1 Please complete the following information about the Board. Please write the number (including ‘0’ if applicable) on EACH line for (A) and (B) to show the number of Board members of each gender, age group and background.

.....female  
 Number of respondents = 1620

.....18 – 24 yrs	.....	25 – 39 yrs
.....40 – 59 yrs	.....	60 – 72 yrs
.....72+ yrs		
.....	English not first learnt language	
.....	Aboriginal or Torres Strait Islander or descendant	

<sup>35</sup> The duties of nominee directors raise complex legal issues. See, for example, P. Redmond, ‘Nominee Directors’, 1987, 10 *University of New South Wales Law Journal* 194; S. Sievers, ‘Finding the Right Balance: The 2GB Case Revisited’, 1993, 1 *Australian Journal of Corporate Law* 1; P. Crutchfield, ‘Nominee Directors: The Law and Commercial Reality’, 1992, 20 *Australian Business Law Review* 109; Companies and Securities Law Review Committee, *Nominee Directors and Alternate Directors*, Report No. 8, 1989.

<sup>36</sup> See H.A.J. Ford, R.P. Austin & I. M. Ramsay, *Ford’s Principles of Corporations Law*, 9<sup>th</sup> edn, 1999, Butterworths, Ch. 9.

<sup>37</sup> See *Corporations Act 2001* (Cth), s 112(1).

<sup>38</sup> See *Corporations Act 2001* (Cth), ss 150–1.

<sup>39</sup> This follows from para (c) of the definition of ‘public company’ contained in *Corporations Act*, s 9.

<sup>40</sup> See D.A. DeMott, ‘Self Dealing Transactions in Nonprofit Corporations’, 1993, 59 *Brooklyn Law Review* 13947 and, in relation to public policy considerations about name licences under ss 150–1, see Woodward at pp. 392–7.

## Chapter 5 - Board Size, Composition, Remuneration and Experience

.....male	
Number of respondents = 1614	
.....18 – 24 yrs	..... 25 – 39 yrs
.....40 – 59 yrs	..... 60 – 72 yrs
.....72+ yrs	
.....English not first learnt language	
.....Aboriginal or Torres Strait Islander or descendant	

### 8.2. Survey results

Nearly three-quarters (74%) of NFP respondents had at least one female director on their Board. The sample NFP group covered 14,159 directors. Overall, only 26% of these directors were female.<sup>41</sup> The mean number of women on the Boards of NFP companies was 2.2.

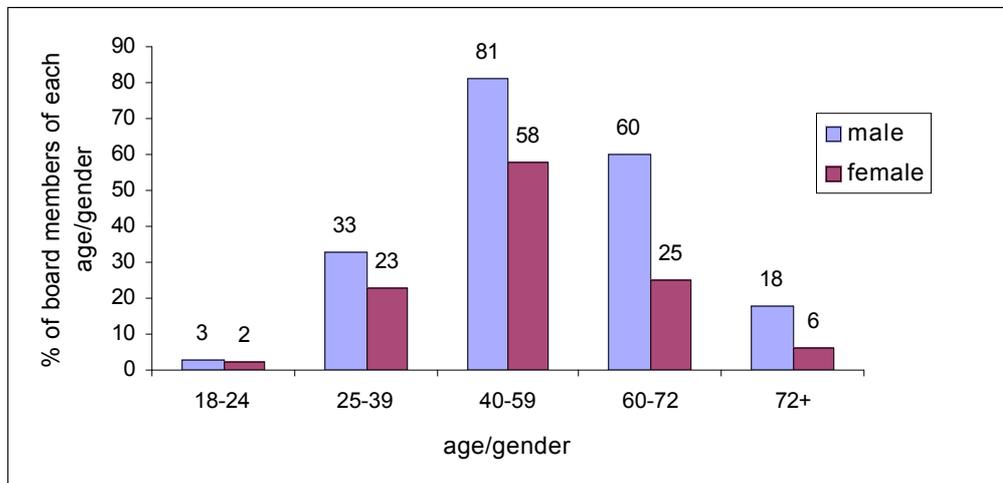
### 8.3. Comparison with 'Top 100'

When compared to the 'Top 100' group, this was a significantly higher proportion – in the 'Top 100' only 7% of the total number of directors surveyed were female.<sup>42</sup>

Figure 28 shows the data for age groupings and gender of directors. With regard to youth representation, only 3% of NFP Boards had a male and 2% had a female, aged between 18-24 years.<sup>43</sup> Males aged 40-72 years (particularly 40-59 years) are overwhelmingly the most represented group. This is consistent with the Steane & Christie study. They reported an average age of respondents as 47 years.<sup>44</sup>

With regard to ethnicity, 2% of all female, and 2% of male directors, were Aboriginal, Torres Strait Islander or a descendant.<sup>45</sup> Of all directors whose 'first learnt language was not English', 10% were male and 6% were female. This is less than Steane & Christie, who reported 18% of directors were 'people from non-English speaking backgrounds'.<sup>46</sup> This difference may be to do with the different definitions used - the survey reported in this article used 'English not first learnt language' compared with Steane & Christie who used the potentially broader definition of people 'from non-English speaking background'.

**Figure 28: Board composition, based on age and gender**



<sup>41</sup> Compared with Steane & Christie who found that 40% of the 1405 directors covered by their study were females: n. 14, p. 54.

<sup>42</sup> Stapledon & Fickling, n. 1, p. 10.

<sup>43</sup> This data supports recent papers presented at the first major, Australian NFP sector governance conference, *Building Better Boards - A Dialogue on Nonprofit Governance*, Nonprofit Governance & Management Centre, Sydney, 13–14 July 2002. See especially, T. Akpeki, 'Diversity in the Board Room', unpublished paper.

<sup>44</sup> Steane & Christie, n. 3, p. 52. The Cornforth study found that UK Charity Boards tend to be dominated by people over the age of 45. Overall, about 71% of trustees are aged 45 and over (see above, n. 4, p.13).

<sup>45</sup> This is less than Steane & Christie, who reported 6% of directors were 'indigenous people': n. 3, p. 52.

<sup>46</sup> See n. 3, p 52.

#### 8.4. Significant differences between respondents

The mean number of women on the Boards of NFP companies was 2.2. Public-serving organisations were more likely to have more females on the Board than member-serving organisations. The mean number of women on public-serving organisations' Boards was 2.5 compared with 2 on the Boards of member-serving organisations.

Community Services Organisations (mean=3), Other Human Services (mean=2.8), Arts and Cultural organisations (mean=3.3) and Education organisations (mean=3) had more women on their Boards than other organisations. In contrast, Religious (mean=1.7) and Sports and Recreation organisations (mean=1.3) had fewer women on their Boards.

Interestingly, the difference between the numbers of women on the Boards of large organisations compared with small organisations was not significant.

#### 8.5. Comparison with UK charities

The Cornforth study found that the ratio of male to female trustees increases with the size of the charity. For charities with an income of less than £100,000 the gender balance is fairly even, with 47–48% female members. For the larger charities with an income of over 250,000 pounds this has decreased to about 30% female Board members. Overall, 45% of Board members are female, but men tend to dominate the Boards of charities that control the greatest financial resources.

#### 8.6. Observation

Ensuring that there is a diverse mix of people on a Board is crucial to ensuring that there is a mix of experiences and skills to be drawn on. Drawing on people from a diversity of professions is one aspect of this strategy. This is relevant not only to the Board's resource gathering, but also to its monitoring and compliance function. Complex service provision and the compliance issues that come with them require knowledge in such areas as accounting, finance, management and law. Providing access to such knowledge can be seen as part of the Boards' resource gathering function. Board members may either possess such knowledge themselves or have access to credible external sources.

Drawing on people from different backgrounds increases the number of interlocking relationships with other organisations and groups of people that may be useful in providing new information, resources, such as clients, credit, funding, advice and supplies.

There are other aspects to Board diversity strategies. Ms Tesse Akpeki defines strategic diversity as 'having a Board which leads the organisation into a desire to be responsive to people who use the service'.<sup>47</sup> Bringing new perspectives to a Board may be a catalyst for change within an organisation. Recruiting people from outside the institutional culture of the organisation may assist the organisation in assessing its strategic direction.

In order to ensure that diverse perspectives are represented on the Board, Akpeki recommends carrying out a skills audit.

The skills audit is a way of asking what skills and knowledge are missing from the board in a good and systematic way and looking at the gaps on the board. If there are not minorities on the board, if there are gaps, what prevents the minorities from serving on the board?

Akpeki points out that often the prospective candidates for the Board are already involved in the organisation. They may be clients or volunteers or members of staff. In order to ensure that a broader mix of backgrounds and experiences are represented on the Board, new recruiting techniques need to be employed.

#### 8.7. Recommendation - recruitment methods

##### **Recommendation 12: Board recruitment methods**

There is a demonstrated need for training materials and other assistance for NFP Boards in their recruitment of Board members, as well as an ongoing assessment of the directors' mix of skills, experience and perspective. In general, NFP company Boards are currently composed of people from a narrow demographic. Many NFP organisations could benefit from the broader range of the skills and experience that are available in the general community. Assistance with this issue would be a useful role for the NFP advisory body recommended in this Report (Chapter 4, regulatory Framework).

<sup>47</sup> T. Akpeki, 'Diversity in the Boardroom', Building Better Boards Conference, unpublished conference paper, Sydney, 2002.

## 9. BOARD EXPERIENCE, SKILLS AND KNOWLEDGE

### 9.1. Rating of experience and skills of Board

#### 9.1.1. SURVEY QUESTION

8.1 How would you describe the experience and skills of your Board as a group in each of the following areas:

**(1) very inadequate, (4) very adequate, (0) not relevant**

understanding of consumer/client perspective	1..2..3..4...0	(1518)
management/governance	1..2..3..4...0	(1616)
law	1..2..3..4...0	(1582)
fundraising	1..2..3..4...0	(1399)
understanding of carer perspective	1..2..3..4...0	(1022)
government relations	1..2..3..4...0	(1464)
accounting/finance	1..2..3..4...0	(1621)
social work	1..2..3..4...0	(1023)
education	1..2..3..4...0	(1263)
medical	1..2..3..4...0	(943)
marketing/media	1..2..3..4...0	(1457)
human resources	1..2..3..4...0	(1399)
information technology	1..2..3..4...0	(1477)
business/community partnerships	1..2..3..4...0	(1394)
investment	1..2..3..4...0	(1374)
philanthropic	1..2..3..4...0	(1169)
other (please specify any other skill that you think is necessary for your Board)		
.....		

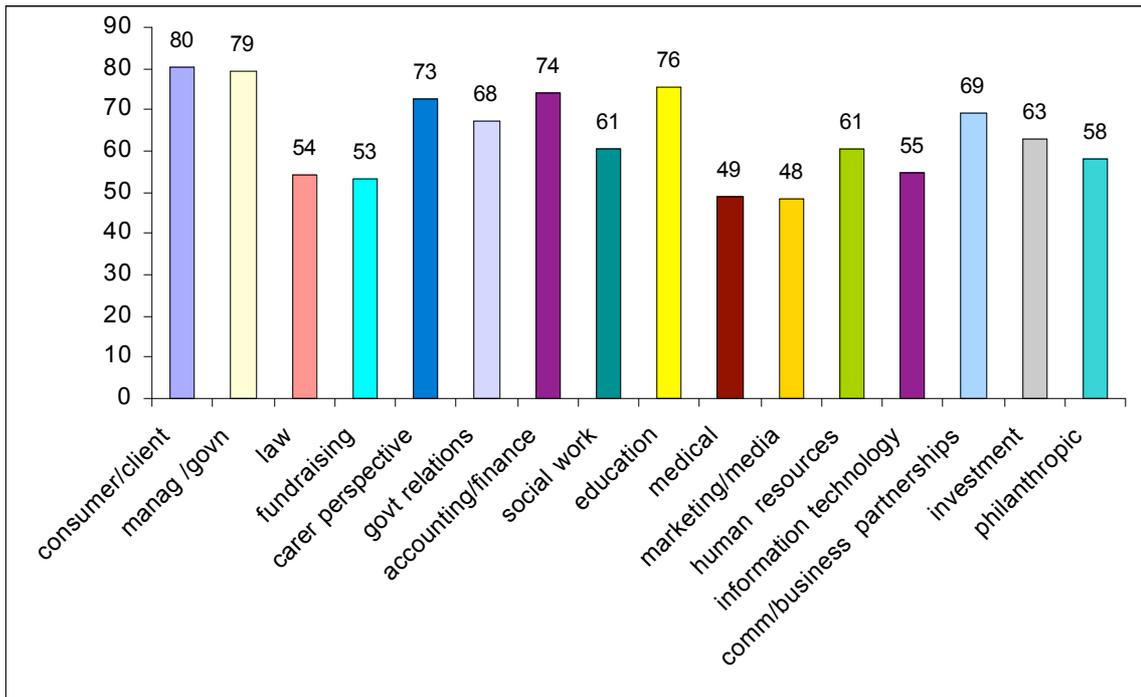
*Number of respondents = as shown in brackets next to each response option*

#### 9.1.2. SURVEY RESULTS

The results for (3) 'adequate' and (4) 'very adequate' were combined to ascertain the overall satisfaction with the Board's experience, skills and knowledge. Respondents (the majority of whom were CEOs) were generally positive about the experience and skills of their Board as a group. Eighty per cent said that the Board had an adequate understanding of consumer/client perspective and more than three quarters (79%) said that their management /governance skills and experience of were adequate. Only just over half of respondents were positive about fundraising and law skills and experience. This finding should be distinguished from the later findings concerning the knowledge of directors about their liabilities (Heading 9.3).

There were only two areas in which majority of respondents did not feel that the skills and experience of Board members were adequate. Only 49% of respondents said that medical experience and skills were adequate (where it was relevant), and 48% said that marketing/media skills were adequate.

Figure 29: Board experience, skills and knowledge



9.1.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

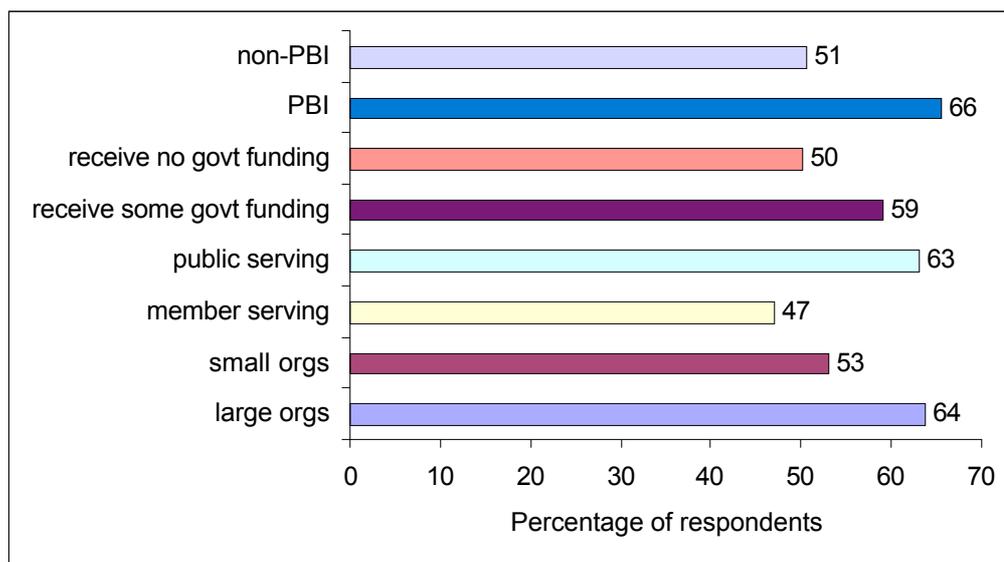
As might be hoped, 75% of respondents from Human Services organisations said that the medical experience and skills of the Board was ‘adequate’ or ‘very adequate’ compared with the overall 49%. 62% of respondents from Arts and Cultural organisations, and 60% of Other organisations said that marketing/media skills were adequate, which is considerably higher than the overall figure of 48%.

Respondents from public-serving organisations were more likely than respondents from member-serving organisations (79% compared with 70%) to say that the accounting/finance skills of the Board were ‘adequate’ or ‘very adequate’.

Figure 30 shows that:

- Respondents from large organisations were more likely than those from small organisations to say that the law skills of the Board were ‘adequate’ or ‘very adequate’ (difference of 11%).
- Respondents from public-serving organisations were more likely than those from member-serving organisations to say that the ‘law’ skills of the Board were ‘adequate’ or ‘very adequate’ (difference of 16%).
- Respondents from organisations that received some government funding were more likely than those from organisations receiving no government funding to say that the ‘law’ skills of the Board were ‘adequate’ or ‘very adequate’ (difference of 9%).
- Respondents from organisations with PBI status were more likely than those from organisations without PBI status to say that the ‘law’ skills of the Board were ‘adequate’ or ‘very adequate’ (difference of 15%).
- Only 45% of respondents from Sports and Recreation organisations said that the ‘law’ skills of the Board were ‘adequate’ or ‘very adequate’. This is quite low compared with the overall 55%.

Figure 30: Law experience and skills, based on key indicators



## 9.2. Law governing directors' duties in the NFP context

The *Corporations Act 2001* (Cth) and the general law impose duties on directors and officers of all companies, regardless of whether they are NFP or 'for-profit' companies. It is clear (at least since the important decision of *Commonwealth Bank of Australia v Friedrich* (1991) 5 ACSR 115; 9 ACLC 946) that being an honorary director will not, of itself, be sufficient to exonerate a director from liability. In that case, J. Tadgell stated:

There is nothing in the Code [now *Corporations Act 2001* (Cth)] to suggest that the standard to be expected of a part-time non-executive director of a company not for profit is different from the standard expected of any other director of a profit-making company: both are required...to exercise a reasonable degree of care and diligence in the exercise of their powers and the discharge of their duties.<sup>48</sup>

One can easily appreciate the policy reasons for this approach. There should be a high degree of accountability for directors of NFP organisations that receive donations from the public and/or government funding (as was the situation in the *Friedrich's case*).<sup>49</sup> Directors' legal duties are one accountability mechanism. Indeed, their importance is arguably greater in the context of a NFP company because many of the other accountability mechanisms (for example, stock exchange regulation, dividends/returns to members and the influence of institutional investors) do not apply.<sup>50</sup>

In order to gather some data about this issue, the questionnaire asked respondents (who were, in the majority of cases, CEOs who were not members of the Board)<sup>51</sup> about the level of Board awareness of personal liability as directors.

<sup>48</sup> *Commonwealth Bank of Australia v Friedrich* (1991) 5 ACSR 115 at 197. Although the court was not prepared to use its discretionary powers under s 535 of the *Companies Code* (now s 1318 of the *Corporations Act 2001* (Cth)) to relieve the non-executive director in that case (Mr Eise) from liability, J. Tadgell did treat the voluntary nature of his position as a relevant factor.

<sup>49</sup> *Commonwealth Bank of Australia v Friedrich* (1991) 5 ACSR 115 at 198. See also M. McGregor-Lowndes, 'Nonprofit Corporations – Reflections on Australia's Largest Nonprofit Insolvency', 1995, 5 *AJCL* 417.

<sup>50</sup> See D.A. DeMott, 'Self Dealing Transactions in Nonprofit Corporations', 1993, 59 *Brooklyn Law Review* 139.

<sup>51</sup> See Heading 3.1.

### 9.3. Understanding of personal liabilities

#### 9.3.1. SURVEY QUESTION

- 8.2 Do you believe that the Board members understand that, under the Corporations Act, they can be personally liable – for example, if they act without sufficient care and diligence or if they allow the company to continue to trade when it is unable to pay its debts? Please tick ONE box and, if possible, add a comment about the level of the Board’s awareness and knowledge of their legal duties as directors.
- all Board members aware
  - most of the Board members aware
  - only some of the Board members aware
  - none of the Board members aware
- comment .....

Number of respondents = 1648

#### 9.3.2. SURVEY RESULTS

The vast majority of respondents (n=1305) said the Board of their organisation understood their personal liability. The results were very consistent, regardless of principal activity.

**Table 10: Board members aware of their liability under the Corporations Act?**

<i>How aware of liability</i>	<i>Frequency</i>	
all aware	1305	79
most aware	261	15.8
some aware	78	5
none aware	4	0.2
no answer given	40	
<b>Total</b>	<b>1688</b>	<b>100</b>

## 10. CONCLUSION

The survey shows that the vast majority of NFP company Boards comprise a majority of non-executive directors. Thus, at least in theory, they are likely to be more independent and better, more objective monitors of managerial behaviour. Indeed, NFP companies fared better overall than the ‘Top 100’ in this respect. However, there are some issues of director independence that are NFP specific - for example, the role of donors on Boards.

Although NFP Boards might be independent of management, NFP bodies might still consider how they can actively increase the pool of potential directors. Our study shows that it is often difficult for NFP companies, especially smaller ones, to recruit Board members. Further, the profile of NFP directors is quite narrow. Younger people, women and people from non-English speaking backgrounds are under-represented on Boards, despite the important contribution they might potentially make to NFP bodies. The pool of potential Board members might be widened by advertising and other recruitment methods.

Periodic assessment of whether the Board is constituted so as to provide the right balance of expertise and skills is important. To this end, Boards need to consider whether the current appointment process leads to the right mix of skills, experience and perspectives. It may be possible, and indeed desirable, to foster the skills of other volunteers so they have the skills and confidence to serve effectively on the Board. Alternatively, co-option or other methods can be used to fill gaps in terms of skill or experience on the Board.

A related and emerging issue for the NFP sector is the remuneration of non-executive directors. While there are a small group of generally larger organisations that are paying non-executive directors for their services to the Board (over and above out of pocket expenses), the majority of respondents were not in favour of this practice.

## CHAPTER 6: BOARD STRUCTURE, PROCEDURES AND ROLE

### *Hard working volunteers?*

#### SUMMARY OF KEY FINDINGS IN THIS CHAPTER

##### Organisational size matters

- The data shows that many Board characteristics vary with the size of the organisation. For example, the size and complexity of the structure of the Board tends to increase with organisational size, and so does the support available for Board members.
- This data supports the need for a specialist NFP advisory body, recommended in Chapter 4, Regulatory Framework, which could provide training, advice for directors of NFP organisations.

##### Smaller management group

- Almost half (46%) of the NFP respondent companies have a group of directors, or a Board committee, that deals with management matters on behalf of the Board. A small management group is more common among those NFP companies with a large Board (9 or more directors). This data supports anecdotal evidence that a smaller management group is a distinguishing feature of NFP Boards.
- The legal position of those directors who are not part of the smaller management group is cause for concern. For example, are they keeping themselves sufficiently informed about the company's affairs?

##### Frequency and length of meetings

- The study showed that being a volunteer director of an NFP company is a big commitment - around half the Boards meet once monthly or more frequently, and almost all (92%) Boards meet for an hour or more.
- On average, large Boards (those with nine or more members) meet more frequently than smaller Boards.
- In general, attendance at Board meetings appears to be good with three quarters of directors attending all Board meetings in most (88%) NFP companies.

##### Decision making

- Around three quarters of Boards always receive minutes, financial reports and reports on activities before meetings.
- Forty-one per cent of Boards use email or fax to make decisions.
- Ninety-one per cent of Boards use some form of consensus in their decision making.

##### Induction of new directors

- Most (80%) respondent companies provide a copy of the last annual report and the constitution, and ensure that briefing by senior staff is conducted when a new director is appointed to the Board.
- Overall, directors of larger organisations are better resourced (at least in terms of formal documentation) than those of smaller organisations. For example, only 60% of small organisations provide new directors with strategic and business plans compared with 84% of large organisations.

##### Role of the Board

- The vast majority of respondents agree that the role of the Board is to:
  - s determine strategic direction and monitor performance against the business plan (91%)
  - s guide and monitor the company's financial position (90%)
  - s act as a general advisory body (85%)
  - s appoint and review the performance of the CEO (82%).

- Interestingly, the majority of respondents also thought it was part of the Board's role to:
  - s bring together individuals to assist fundraising (65%)
  - s represent the interests of a particular stakeholder (59%)
  - s participate in management (53%)
  - s monitor and advise on government policy environment(55%).

### **RECOMMENDATION**

#### **Board training**

Support for Board members with training and induction is required. Smaller NFP organisations, in particular, should be targeted as they do not receive the same level of introductory material and training as their larger cousins. Consideration should be given to reaching and assisting the Boards of small NFP organisations. This is an area that would benefit from the independent NFP advisory and training body recommended in this Report (see Chapter 4, Regulatory Framework).

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## 1. INTRODUCTION

This Chapter focuses on the processes followed by NFP company Boards in their meetings. It reports on the data showing how often Boards meet, how they make decisions and how well informed they are prior to meetings. The results covered in this Chapter provide solid evidence about whether NFP Boards are in a position to fulfil their roles. Whilst the data does not tell us about the content of meetings, it does tell us whether an appropriate framework is in place in relation to frequency of meetings and information provided to directors.

The survey results show that generally Boards of NFP companies limited by guarantee meet very regularly, although there are significant exceptions which are reported under Heading 3.1.3. The data also shows that meetings generally take over an hour, and the directors receive a range of material before the meeting. However, the Boards of small organisations appear to be at a significant disadvantage when it comes to formal resources. The Boards of small organisations were between 8-20% less likely to receive financial reports, reports on activities or previous minutes. Likewise, when new directors are appointed to the Board, large organisations are much more likely to provide a comprehensive induction, including site visits, providing strategic and business plans, the constitution and the annual report, and briefings by senior staff. While there was great variation between organisations in their method of decision making, almost all organisations use some form of consensus.

The final section of this Chapter concerns the organisational role of the NFP Board. The data suggests that NFP Boards usually have additional roles to those of a typical 'for-profit' company Board. For example, the majority of respondents believe the Board have an important fundraising role. This suggests that the organisational role of the Board as understood and practised by NFP companies, differs significantly from 'for-profit' companies.

## 2. BOARD STRUCTURE

### 2.1. Smaller management group

#### 2.1.1. SURVEY QUESTION

9.1.1 Does a group of directors, or a Board committee, deal with management matters on behalf of the Board?

- yes
- no

*Number of respondents = 1649*

9.1.2 If 'yes', how often does this group meet? *(please tick only one box)*

- daily
- weekly
- monthly
- other (please specify) .....

*Number of respondents = 770*

#### 2.1.2. SURVEY RESULTS - FREQUENCY

Forty-six per cent of respondents had a smaller management group within their Board.

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Note: All references in this Report to small and large organisations or companies are based on the definition of "small" and "large" (proprietary companies) as contained in s 45A of the *Corporations Act 2001* (Cth), unless detailed otherwise.

### 2.1.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

There were no significant differences between respondents based on principal activity or other discernible factors such as size, tax status, etc.

The data showed that if the Board is larger than the average of eight directors, they are more likely to have a smaller management group. Organisations that have a 'large Board' (nine or more directors) are more likely to have a Board committee that deals with management issues on behalf of the Board than organisations with a 'small Board' (less than 9 directors) (50% vs 42%). Therefore the data supports the notion that having a 'large Board' often makes it necessary to have some issues delegated to a smaller 'executive' group.

### 2.1.4. OBSERVATION

Prior to conducting the survey, we received anecdotal evidence that a smaller management group within the Board was a distinguishing feature of NFP Boards. While not quite the majority (46%, n=753), the data does support this anecdotal evidence.

The legal position of those directors who are not part of the smaller management group is cause for concern. Do they still keep themselves sufficiently informed about the company's affairs?<sup>1</sup> In particular, do they regularly monitor the company's financial position? They are at risk of personal liability if they rely on the smaller management group and do not keep abreast of the company's affairs sufficiently to act appropriately if there are reasonable grounds to expect that the company will not be able to pay all its debts when they fall due.<sup>2</sup>

The data on the frequency of a smaller management group, and concern about the legal position of those directors who are not part of the smaller management group, support the recommendation on Board size made in Chapter 5, Board Size, Composition, Remuneration and Experience.

### 2.1.5. SURVEY RESULTS - MEETINGS

Of those respondents with a smaller management group (n=770), 56% said that it met at least monthly, while ten per cent said that it met on a daily or weekly basis. For this latter sub-group, it can be assumed that they are actively managing the company's day-to-day operations rather than the overseeing and strategic role envisaged, for example, by Drucker.<sup>3</sup>

**Table 1: How often does this group meet?**

<i>How often meeting</i>	<i>Frequency</i>	<i>Per cent</i>
daily	26	3
weekly	50	6.5
monthly	352	46
other	342	44.5
no answer given	918	
total	1688	100

### 2.1.6. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

The data was then cross-tabulated to see if there were any significant differences between respondents based on whether the smaller management group meets at least monthly. Sports and Recreation organisations were much more likely than other organisations, based on principal activity, to have smaller management group meeting at least once a month. This was 76% compared with the overall figure of 56%.

<sup>1</sup> See generally *Commonwealth Bank of Australia v Friedrich* (1991) 5 ACSR 115, especially pp. 125- 6 and p. 197.

<sup>2</sup> This overarching duty to 'be informed' cannot be delegated to an executive group of directors. Thus, for example, they would be in breach of their director's duties to prevent insolvent trading under s588G *Corporations Act 2001*. See also comments by J. Tadgell in *Commonwealth Bank of Australia v Friedrich* (1991) 5 ACSR 115.

<sup>3</sup> Drucker, see n. 18

## 2.2. Other committees

### 2.2.1. SURVEY QUESTION

9.1.3 Does the Board have any other committee?

yes

no

*Number of respondents = 1631*

### 2.2.2. SURVEY RESULTS

Half of all respondents (50%, n = 819) said their Board had other committees.

### 2.2.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

The most significant difference between respondent organisations was based on size. Large organisations were more likely to have an additional committee than 'small' organisations - a difference of 38%.

Public-serving organisations were 9% more likely than member-serving organisations to have a committee, and those receiving some government funding were 16% more likely than those receiving none to have at least one other Board committee. Sixty-five per cent of Health organisations and 64% of Interest Group organisations had committees, compared with only 21% of Religious organisations.

### 2.2.4. COMPARISON WITH UK CHARITIES

The recent Cornforth study found that the percentage of Boards with sub-committees varies from 25% in organisations with an income of less than £10,000, to 93% in organisations with incomes of more than £10 million. The UK study also found that the number of sub-committees had increased.<sup>4</sup>

### 2.2.5. FEEDBACK

We received feedback from a legal practitioner experienced in dealing with a large range of NFP organisations. This was that, as a general rule, he advises larger NFPs to 'enshrine an Audit Committee of the Board (but with at least some outside people) in the constitution.'

## 3. BOARD MEETINGS AND PROCEDURES

### 3.1. Meeting frequency

#### 3.1.1. SURVEY QUESTION

10.1 How often does the full Board of Directors meet? (*please tick only one box*)

fortnightly (or more often)

monthly

every two months

quarterly

twice yearly

yearly

other (*please specify*) .....

*Number of respondents = 1655*

<sup>4</sup> C. Cornforth, 'Recent Trends in Charity Governance and Trusteeship: the results of a survey of governing bodies of charities', *NCVO: Voice of the voluntary sector*, 2001, p. 15.

3.1.2. SURVEY RESULTS

Almost exactly half the respondents said that the full Board of their organisation met monthly or more frequently.

Table 2: Frequency of full Board meetings

<i>How often meeting</i>	<i>Frequency</i>	<i>Per cent</i>
Fortnightly	41	2.5
Monthly	785	47.5
every two months	230	14
Quarterly	287	17
twice yearly	96	6
Yearly	85	5
Other	131	8
no answer given	33	
Total	1688	100

3.1.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Again, size was a significant factor in relation to the frequency of committee meetings. Large organisations were 17% more likely than small ones to meet on a monthly or more frequent basis.<sup>5</sup>

In terms of principal activity, 62% of Community Service organisations and 82% of Sports and Recreation organisations had full Board meetings on a monthly or more frequent basis. In contrast, only 31% of Education organisations, 32% of Religious, 18% of Philanthropic, 20% of Environmental and 24% Interest Group organisations met on a monthly or more frequent basis. It seems, therefore, that because of the great number of Sports and Recreation organisations and Community Services organisations in the overall statistical body (both categories make up 40% of all respondent organisations), the frequency of meetings figure was somewhat skewed by their presence. For example, without Sports and Recreation organisations, the overall percentage of organisations meeting on a monthly or more frequent basis was 42% compared with the overall figure of 50%.

3.1.4. DOES BOARD SIZE AFFECT THE FREQUENCY OF MEETINGS?

We looked at two measures in order to see if Board size affects the frequency of meetings. First, using the overall number of directors covered by the survey (n=14,159), we calculated the average size of the Boards that meet 'frequently'. Second, we looked at what percentage of Boards meeting 'frequently', could be classified as a 'small Board'. For the purposes of these calculations, a Board was taken to meet 'frequently' if it met monthly or more often.<sup>6</sup>

By reference to the first measure, we calculated that the average Board size of those Boards meeting 'frequently' (n=826) is 8.7 directors. This is larger than the average of 8.1 directors for those Boards meeting less frequently (that is, less often than monthly)(n=697), and the overall average Board size of 8.5.<sup>7</sup> Although this is a small numeric difference, it is a statistically significant result<sup>8</sup> that suggests that larger Boards meet more frequently.

The data using the second measure also supports this observation. Cross-tabulations were run using a definition of a 'small Board' as eight or less directors, and a 'large Board' as nine or more directors. Based on this definition, just under half (47%) of 'small Boards' met at least monthly, compared with almost two-thirds (63%) of all 'large Boards'.<sup>9</sup> In other words, having nine or more directors on the Board a 'large' number by NFP and 'for-profit' standards - did not inhibit attendance. On the contrary, 'large Boards' seem to meet more frequently than 'small [or at least smaller] Boards'.

<sup>5</sup> This is a different result from that found the Cornforth study of UK charities, which found that the number of Board meetings varies little with the size of the charity. As above, n. 4, p. 16.

<sup>6</sup> Those that choosing 'other' as their option under question 10.1 (n=131) were excluded for the purposes of these calculations.

<sup>7</sup> See Chapter 5, Board Size, Composition, Remuneration and Experience.

<sup>8</sup> Statistically significant on a T-Test at the 0.01 level of significance.

<sup>9</sup> Significant at the 0.01 level on a Chi-Square test of independence.

### 3.2. Electronic mechanisms used

#### 3.2.1. SURVEY QUESTION

10.2 Are Board meetings ever held by any of the following means:

telephone conference

yes

no

*Number of respondents = 1638*

video conferencing

yes

no

*Number of respondents = 1607*

decision made by email or fax, then ratified at next Board meeting

yes

no

*Number of respondents = 1624*

other electronic means (please specify) .....

*Number of respondents = 32*

#### 3.2.2. SURVEY RESULTS

The survey results for this question show that, whilst not a particularly high take-up, electronic technology is being used to facilitate decision making for NFP Boards. Email and fax are most frequently used. Forty-one per cent of respondents said that email or fax was used to make Board decisions.<sup>10</sup>

**Table 3: Board meeting held by alternative means**

	<i>Frequency</i>	<i>Per cent 'Yes'</i>
telephone conference	485	29.5
video conferencing	14	1
Decision by email or fax	658	40.5
other electronic means	32	2
Total	1189	73

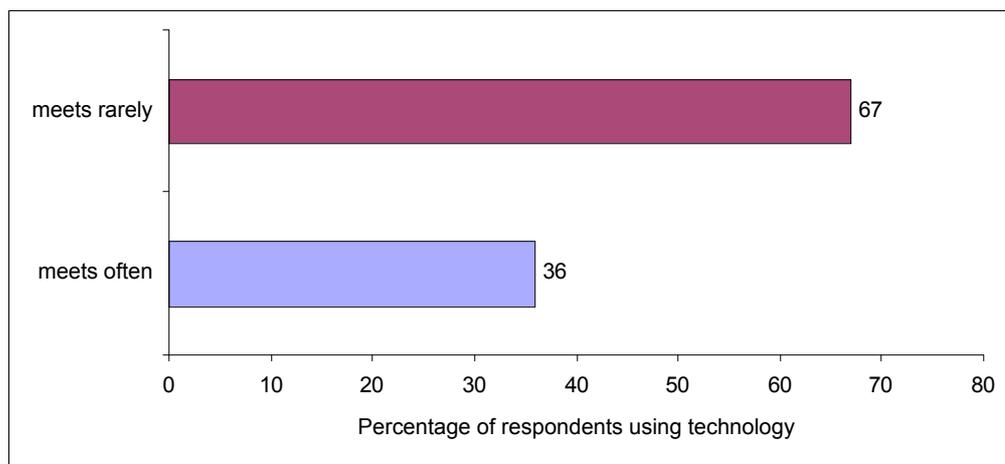
#### 3.2.3. DOES THE USE OF TECHNOLOGY AFFECT FREQUENCY OF MEETINGS?

The data concerning the frequency of meetings was combined with the data concerning the use of technology in order to examine whether or not the use of technology increases the frequency of meetings. The data showed that 'rarely meeting' (every two months or longer) Boards are more likely to use the phone (43%) as against only 16% of 'often meeting' (monthly or more) Boards. Similarly, Figure 3 shows that when all types of technology were combined, 36% of the 'often meeting' Boards used *some* form of technology for holding Board meetings compared with two-thirds (67%) of the 'rarely meeting' Boards.

Thus, the data shows that there is an inverse relationship between the use of technology and the frequency of Board meetings. Namely, the more frequent the use of technology as a means of holding a Board meeting, the fewer the number of Board meetings. This may mean that because Boards are making decisions via email etc, they are not meeting as frequently. Alternatively, it may be that organisations have greater difficulty meeting frequently, such as multi-State organisations, are the organisations that have been taking up the use of technology. The data collected does not reveal whether the use of technology has increased or decreased the frequency of meetings.

<sup>10</sup> The use of technology has been specifically permitted by legislation since 1 July 1998. See s248D *Corporations Act 2001* (Cth).

Figure 1: Frequency of Board meetings held by any electronic means



### 3.2.4. OTHER STUDIES

This data confirms previous research on the use of technology in group decision making. Research on decision making has found that groups linked by computer make fewer remarks and take longer to reach decisions than groups meeting face-to-face.<sup>11</sup> Kiesler & Sproul, for example, found that meetings conducted through computers result in greater delays, and that time-constrained groups exchanged much less information when meeting electronically than when meeting face-to-face.<sup>12</sup>

## 3.3. Distribution of material before the meeting

### 3.3.1. SURVEY QUESTION

10.3 Please indicate which, if any, of the following papers are distributed before Board meetings:

(1) never, (2) one in four times, (3) two in four times, (4) always

- previous minutes 1...2...3...4
- report on all activities 1...2...3...4
- financial report 1...2...3...4
- other (please specify) .....

Number of respondents = 1644

### 3.3.2. SURVEY RESULTS

NFP respondent organisations generally have good practices in relation to the distribution of papers before meetings. Ninety per cent of respondents said that previous minutes are always distributed, 73% of respondents said that reports on activities are always distributed before Board meetings, and 77% of respondents said that financial reports are always distributed before Board meetings. We note that the majority of respondents were CEOs and, therefore, there may have been some bias in favour of responding in this way. However, we do not expect any significant bias, given that the survey was confidential.

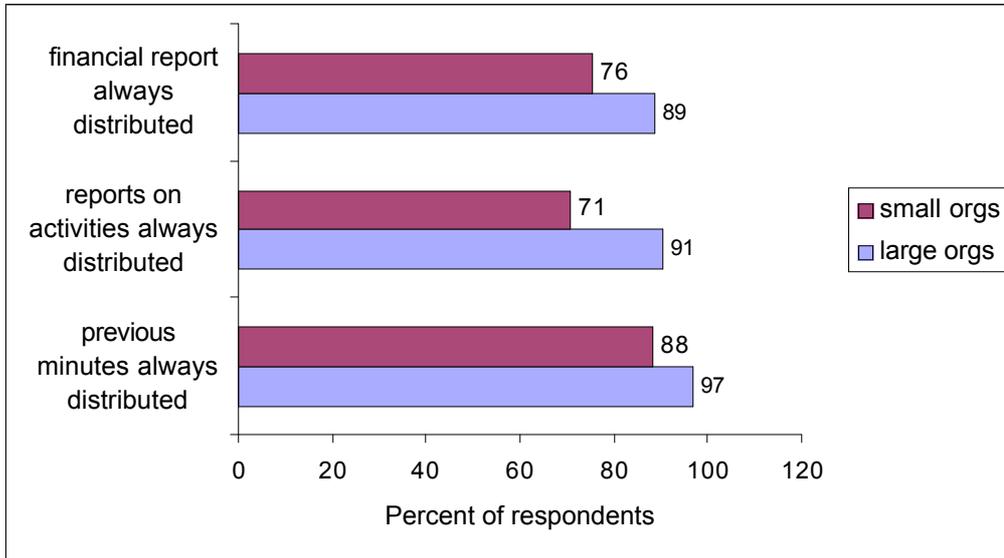
<sup>11</sup> Hiltz et al., 'Experiments in Group Decision Making: Communication Process and Outcome in Face-to-Face versus Computerized Conferences', (1986) 13 Human Communication Research 225.

<sup>12</sup> S. Kiesler & L. Sproul, 'Group Decision Making and Communication Technology', 1992, 52 *Org. Beh. & Human Decision Processes* 96, p. 108

3.3.3. SIGNIFICANT DIFFERENCES BETWEEN ORGANISATIONS

Figure 2 shows that Board papers are consistently more likely to be distributed before meetings in large organisations than papers in small organisations. This may simply be a result of the difference in resources available to the organisation to provide secretarial and other kinds of support to the Board. There were similar differences between those organisations that receive government funding and those that do not. There were no significant differences between organisations based on principal activity.

Figure 2: Differences in distribution of papers before Board meetings, based on size



3.3.4. FEEDBACK

We received feedback from a lawyer experienced in acting for a range of NFP organisations who said that he advises NFP directors that they should insist on:  
 being given accurate and up-to-date financial statements each month. In my experience, if this occurs the company is being sufficiently well run that it is unlikely to get into serious financial difficulty.

3.4. Length of meetings

3.4.1. SURVEY QUESTION

- 10.4 Typically, how long do Board meetings take? (please tick only one box)
- less than 1 hour
  - 1- 2 hours
  - more than 2 hours
  - other (please specify) .....

Number of respondents = 1662

3.4.2. SURVEY RESULTS

Most respondents either said that the Board meetings took one to two hours (45% of respondents) or more than two hours (39%). This demonstrates that, in most cases, being a voluntary member of a Board requires a substantial commitment given the frequency of meetings attended, the length of meetings, and the materials provided before the meeting.

Table 4: Typical time taken for Board meetings

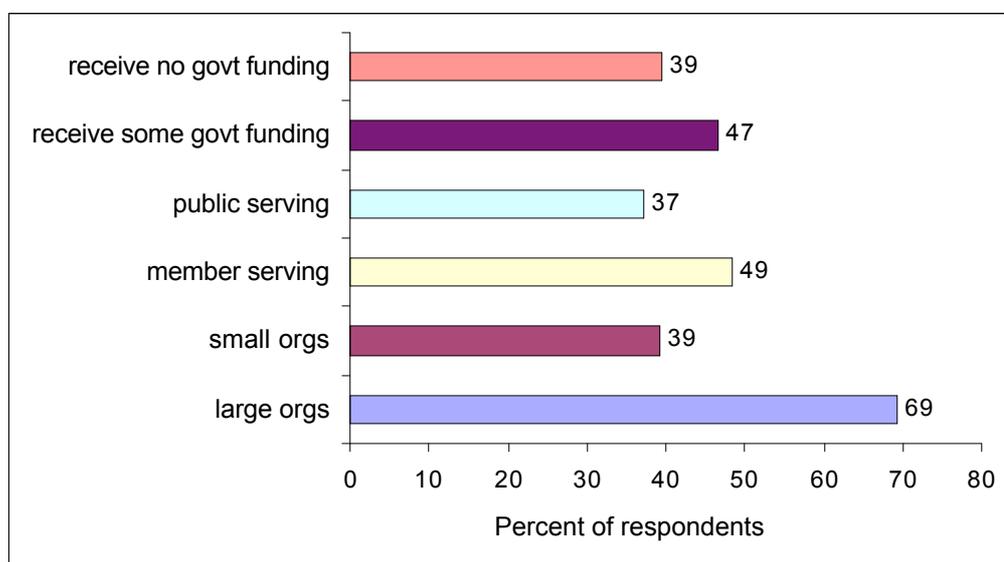
<i>Time for Board meetings</i>	<i>Frequency</i>	<i>Per cent</i>
<1 hr	128	8
1- 2 hrs	754	45
>2hrs	654	39
Other	126	8
no answer given	26	
total	1688	100

3.4.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Figure 3 shows that, in relation to the length of meetings, there was a significant difference between respondents based on size. Boards from large organisations were much more likely to meet for more than two hours than Boards from small organisations. Indeed, over two-thirds of Boards of large organisations (69%) meet for more than two hours, compared with just over a third (39%) of Boards of small organisations. The majority of Boards from small organisations (52%) meet for between 1 to 2 hours. This difference may simply be a result of the amount of time required to oversee the more complex arrangements of a large organisation compared with a smaller one.

Around half (49%) of Boards from member-serving organisations meet for over two hours, compared with only 37% of Boards from public-serving organisations. It is possible to speculate that there is greater factionalism amongst member-serving organisations (leading to the greater likelihood of contested Board elections, as reported in Chapter 5, Board Size, Composition, Remuneration, and Experience) than in public-serving organisations. Alternatively, directors of member-serving organisations may discuss issues that affect them directly, and therefore spend greater time discussing the details of their management, leading to longer meetings. However, without further qualitative study, it is difficult to account for this difference in meeting length.

Figure 3: Board typically meets for more than 2 hours, based on key indicators



### 3.5. Meeting attendance

#### 3.5.1. SURVEY QUESTION

- 10.5 Typically, how many Directors attend Board meetings? (please tick only one box)
- less than \_
  - \_ to less than \_
  - \_ to less than \_
  - \_ or more

*Number of respondents = 1656*

#### 3.5.2. SURVEY RESULTS

In the vast majority of cases (88%) three-quarters or more of the total number of directors attend Board meetings (Table 5).

**Table 5: Typically, how many directors attend Board meetings?**

<b>Number of directors in attendance</b>	<b>Frequency</b>	<b>Per cent</b>
less than a quarter	2	0.1
quarter to less than half	13	0.8
half to less than three-quarters	177	10.7
three-quarters or more	1464	88.4
no answer given	32	
<b>Total</b>	<b>1688</b>	<b>100</b>

#### 3.5.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

There were very few significant differences between respondents. The main difference was based on size. Almost all (98%) of respondents from large organisations said that three-quarters of directors typically attend Board meetings, compared with 87% of small organisations. Philanthropic organisations typically have lower rates of attendance of Board meetings - only 71% (compared to the overall result of 88%).

### 3.6. Formal enough?

#### 3.6.1. SURVEY QUESTION

- 10.9.1 Overall, do you feel your company operates 'formally' enough in terms of its processes?
- yes
  - no
  - not sure

*Number of respondents = 1655*

#### 3.6.2. SURVEY RESULTS

Almost all respondents (92%) were satisfied that the company operates 'formally' enough in terms of its processes. Only Religious organisations were slightly behind the average at 86% vs 92%. Four per cent of all respondents were 'not sure'.

## 4. DECISION-MAKING METHOD

### 4.1. Survey question

10.6 How does the Board decide most issues? (*please tick only one box*)

- consensus
- mix of consensus and voting
- consensus, but as a matter of procedure, vote always taken
- vote

*Number of respondents = 1659*

### 4.2. Survey results

Almost all respondents (91%) reported that some form of consensus was used in the decision making of the Board. This may have involved (a) only consensus decision making, (b) a mix of consensus and voting, or (c) consensus and then, as a matter of procedure, a vote. Breaking this down further: 64% always used consensus (that is, (a) and (c)) and 27% used a mix of consensus and voting. Only 9% of respondents said that they always voted.

**Table 6: Method of decision making**

<i>Method</i>	<i>Frequency</i>	<i>Per cent</i>
Consensus	645	39
mix of consensus	447	27
consensus but vote	413	25
Vote	154	9
no answer given	29	
Total	1688	100

### 4.3. Significant differences between organisations

The significant findings, once data was cross-tabulated, were as follows:

- Seventeen per cent of respondents from Sports and Recreation organisations said they always voted compared with 9% overall.
- Member-serving organisations were 9% less likely to use only consensus than public-serving organisations (35% vs 44%).
- Sixty per cent of respondents from Religious organisations said that decisions were made using only consensus (option (a) Heading 4.2), compared with 39% overall.

## 5. CONFLICTS OF INTEREST

### 5.1. Survey question

10.7.1 Are you aware of any situation in the past five years where an actual or potential conflict of interest has arisen between the interest of a director (or a stakeholder whose interests they represent) and the interests of the company?

- yes
- no

*Number of respondents = 1655*

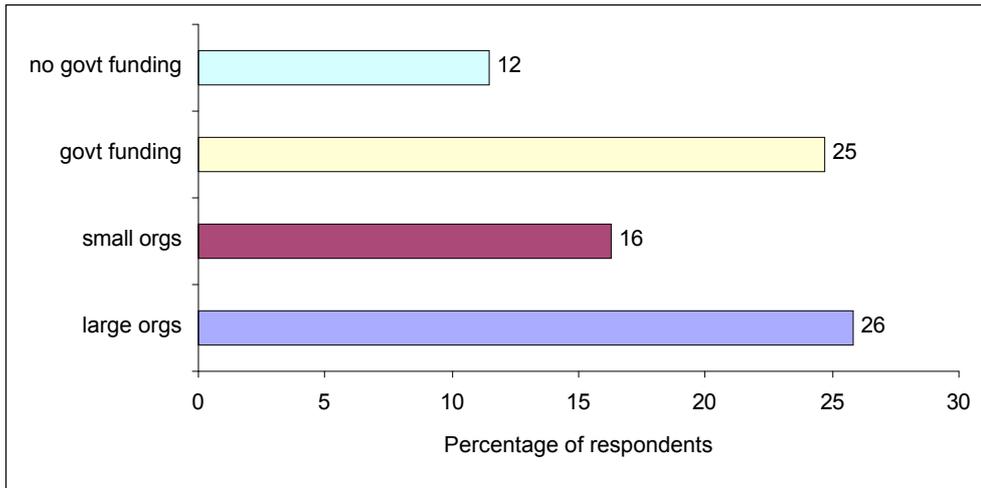
### 5.2. Survey results

Eighty-two per cent of respondents said that there had been no conflict of interests experienced in the last five years, while 18% (n=292) said that some conflict of interest had been experienced.

### 5.3. Significant differences between organisations

Large organisations were significantly more likely to report a conflict of interest in the past five years than small organisations (a difference of 10%), as were those receiving government funding compared with those that do not (a difference of 13%). More than a third (35%) of respondents from Other Human Services organisations also reported some actual or potential conflict of interests in the past five years, which is significantly higher than the overall figure 18%.

Figure 4: Conflict of interests, based on key indicators



### 5.4. Observation

Without results for a 'for-profit' group it is not possible to comment on whether or not the overall figure of 18% who have experience an actual or potential conflict of interest is higher than for other types of companies. However, this overall figure does, indicate that the conflict of interest issue is one that arises as a practical matter for many NFP organisations. Good corporate governance practice would require all NFP organisations to have clear procedures for disclosure of such conflicts or potential conflicts.<sup>13</sup>

## 6. INDUCTION OF NEW DIRECTORS

### 6.1. Survey question

- 10.8 When a new director is appointed, indicate which (if any) of the following occurs:
- receive a copy of the last annual report
    - yes (1240)
    - no (284)
  - receive a copy of the company's constitution
    - yes (1257)
    - no (286)

<sup>13</sup> NFP companies limited by guarantee are public companies and therefore must comply with both ss191- 3 and voting restrictions contained in s195 *Corporations Act 2001* (Cth).

are briefed by senior staff	
<input type="checkbox"/> yes	(1222)
<input type="checkbox"/> no	(292)
receive a copy of strategic and business plans	
<input type="checkbox"/> yes	(938)
<input type="checkbox"/> no	(539)
go on site visits	
<input type="checkbox"/> yes	(502)
<input type="checkbox"/> no	(142)
<input type="checkbox"/> not applicable	
other (please specify).....	

Number of respondents = indicated in brackets next to each option

## 6.2. Survey results

NFP companies generally reported following good practice in inducting new directors. Just over 80% of respondents said that new directors receive a copy of the last annual report, a copy of the constitution and are briefed by senior staff. Sixty-four per cent said that new directors receive strategic and business plans. Seventy-eight per cent of respondents said that new directors, where relevant, go on site visits. Again, we note that the majority of respondents were CEOs and, therefore, there may have been some bias in favour of responding in this way. However, we do not expect any significant bias, given that the survey was confidential.

Table 7: Action taken when new director is appointed

Action	Frequency	Per cent 'Yes'
receive copy of annual report	1240	81
receive copy of constitution	1257	81.5
briefed by senior staff	1222	81
receive strategic and 'business plans'	938	63.5
go on site visits (where relevant)	502	78

### 6.2.1. OBSERVATION

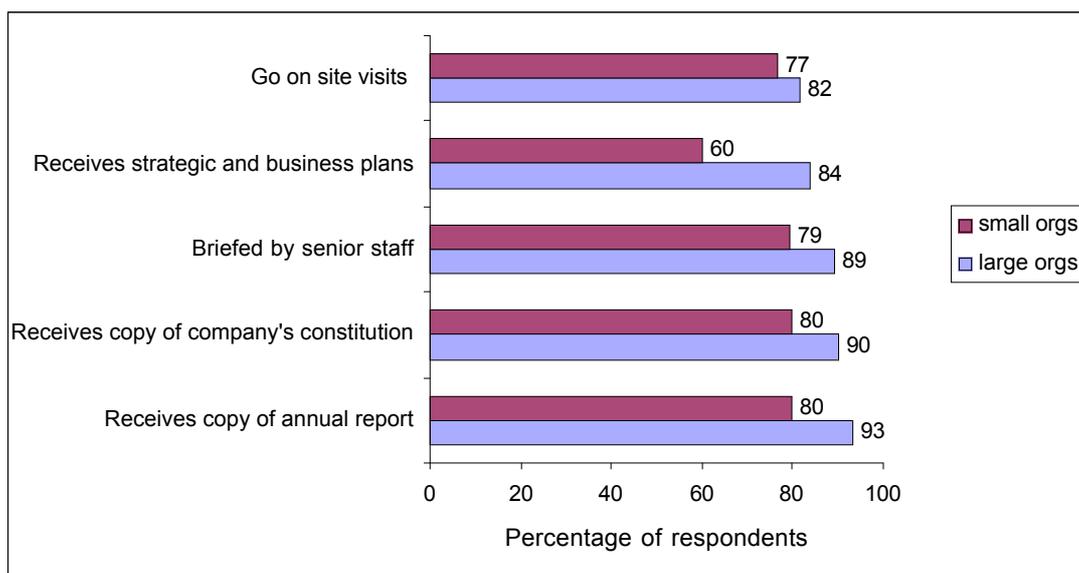
It is cause for concern that 286 respondents said that new directors do not receive copies of the constitution and 284 do not receive a copy of the last annual report, which must be regarded as a basic minimum.

## 6.3. Significant differences between respondents

Once again, the most significant difference between respondents was based on the size of the organisation. Large organisations far more frequently had better practices than small organisations in terms of the induction of new directors. Even assuming fewer resources, there can be little excuse for failing to provide a new director with a copy of the constitution and the most recent annual report, given that both of these have to be prepared regardless of the appointment of a director.

The largest difference between small and large organisations with respect to inducting new directors is the number of respondents that provide the new directors with strategic and 'business' plans - a difference of 24%. If the role of a Board of directors includes overseeing the implementation of the policy of the organisation's mission, then strategic and 'business' plans would seem to be amongst the most crucial material for a new director to have. However, only 60% of small organisations provide new directors with this material. This may be because they have not prepared strategic or 'business' plans, or at least not in any separately articulated written form.

Figure 5: Action taken when new director is appointed, based on size



6.3.1. COMPARISON WITH UK CHARITIES

The Cornforth study had similarly found that the availability of induction and training for new Board members varies between 20% for the smallest charities and increases with size to 77% for the largest charities.<sup>14</sup> The Voluntary Sector UK Almanac 2000 also found that 'around two in five medium to large organisations now offer access to training for their trustees, but only one in five smaller ones do so.'<sup>15</sup>

6.4. Recommendation

**Board training**  
 Support for Board members with training and induction is required. Smaller NFP organisations, in particular, should be targeted as they do not receive the same level of introductory material and training as their larger cousins. Consideration should be given to reaching and assisting the Boards of small NFP organisations. This is an area that would benefit from the advisory and training body recommended in this Report (see Chapter 4, Regulatory Framework).

7. DIRECTORS' AND OFFICERS' INSURANCE

7.1. Survey question - frequency

10.10.1 Does the company pay for directors' and officers' insurance?

- yes
- no

Number of respondents = 1642

10.10.2 If 'no', is directors' and officers' insurance provided by the government?

- yes
- no

Number of respondents = 565

<sup>14</sup> See Cornforth n. 4 at p. 17.

<sup>15</sup> A. Passey, L. Hems, & P. Jas, *UK Voluntary Sector Almanac 2002*, London, National Council for Voluntary Organisations, 2000, p. 105, cited in Cornforth, n. 4, p. 17.

### 7.1.1. SURVEY RESULTS

Although under law a company is not required to provide directors' and officers' liability insurance (D&O insurance), most do. Sixty-eight per cent of respondents said that the company pays for D&O insurance. Of those saying 'no', only 9% said that it was paid for by the government. This means that a substantial number of directors and officers of NFP companies (up to 23%) are not covered by insurance or pay for it themselves.

Consider this sub-group of 23% further. Although practice varies, the company usually pays 90%- 95% of the overall premium and the directors/officers pay between 5%- 10% of the premium.<sup>16</sup> Our survey did not ask respondents to specify the particular proportions that were paid. However, even if the company paid less than the total, one would still have expected the respondent to answer 'yes' to the survey question. Thus, whilst this means that the percentage not covered by D & O insurance could be less than 23%, it would be useful to further investigate the reasons why they had no insurance.

### 7.1.2. PERMISSIBLE PAYMENTS BY THE COMPANY

D&O insurance is intended to protect the personal assets of directors by providing them with an indemnity against any wrongful acts they may have committed. Most policies also reimburse the company for any lawful legal expenses it may have incurred on behalf of the directors and officers. Pursuant to s.199B of the *Corporations Act 2001*(Cth), the D&O insurance policy cannot cover:

- a wilful breach of duty in relation to the company
- an improper use of position
- an improper use of information.<sup>17</sup>

## 7.2. Survey question - actual or threatened legal claims

10.10.3 During the last five years, are you aware of any actual or threatened legal claims against any of the company's directors for a breach of a legal duty?

- yes
- no

Number of respondents = 1656

10.10.4 If 'yes', please specify the general nature of the claim(s)

.....

### 7.2.1. SURVEY RESULTS

Only 52 respondents (3%) said that there had been any actual or threatened legal claims against any of the company's directors for a breach of a legal duty in the last five years.

## 8. ORGANISATIONAL ROLE

### 8.1. NFP governance theory

The widely quoted work of Drucker contends that the role of a Board within a NFP organisation includes the approval of the organisation's mission, its objectives and the measurements it develops to judge its progress towards these objectives. He also contends that it is the Board's role to look critically at the organisation's financial planning and to act as the 'highest court' in relation to organisational problems. Finally, Drucker believes that it is the role of the Board to 'watch the spirit of the organisation' - to make sure that it develops managers, and that its rewards to management strengthen the organisation and direct it towards its objects.<sup>18</sup>

<sup>16</sup> M. Waller, 'Nonprofit Directors' and Officers' Insurance', Program on Nonprofit Corporations, Working Paper Series, Working Paper 12, Queensland University of Technology, 1992, p. 3.

<sup>17</sup> 'Directors' and officers' liability insurance', *Australian Corporate News*, Issue 13, 16 July 2003, CCH, p. 1.

<sup>18</sup> P. Drucker, *The Practice of Management*, Pan Books, London, 1968.

## 8.2. Survey question

11	We are interested in your views on the role of the Board in the company. Please indicate how much you agree or disagree with the following statements about the Board’s main role within your company. <b>(1) strongly disagree, (4) strongly agree, (0) not sure</b>	
(1610)	to act as a general advisory body	1..2..3..4..0
(1624)	to determine strategic directions and monitor performance against plan	1..2..3..4..0
(1625)	to participate in the company’s management and/or its operations	1..2..3..4..0
(1630)	to guide and monitor the company’s financial position	1..2..3..4..0
(1600)	to bring together individuals with sufficient reputation /connections to assist with fundraising & grant applications	1..2..3..4..0
(1604)	to monitor and advise on government policy environment	1..2..3..4..0
(1605)	to represent the interests of particular stakeholders	1..2..3..4..0
(1594)	to appoint the chief executive officer and to review their performance	1..2..3..4..0
	other ( <i>please specify</i> ) .....	

*Number of respondents = numbers shown in brackets for each option*

## 8.3. Survey results

The most strongly agreed upon roles for NFP Boards are:

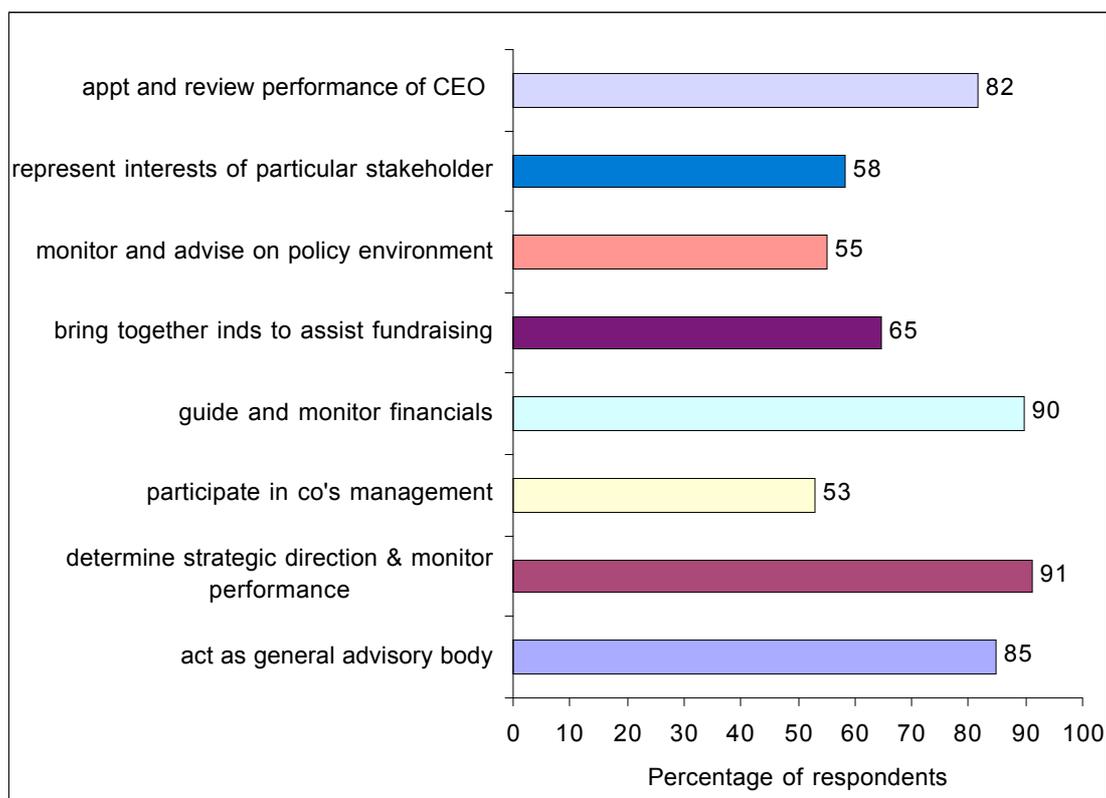
- Determining strategic direction and monitoring performance against the plan (91%: 73% strongly agree, 18% agree).
- Guiding and monitoring the company’s financial position (90%: 68% strongly agree, 22% agree).
- Acting as a general advisory body (85%: 61% strongly agree, 24% agree).
- Appointing and reviewing the performance of the CEO (82%: 62% strongly agree, 12% agree).
- Sixty-five per cent agree (40% strongly agree and 25% agree) that the role of the Board is to fundraise.<sup>19</sup>

In Figure 6, the ‘not sure’ responses have been excluded and the ‘agree’ and ‘strongly agree’ have been combined.<sup>20</sup>

<sup>19</sup> For this option there was a larger number of ‘not sure’ responses than for the other options: 11 % vs less than 2%.

<sup>20</sup> The collapsed chart did not result in any distortion of the refined patterns.

Figure 6: Role of the Board



The majority (53%: 36% strongly agreed and 17% agreed) also agreed that the role the Board included participating in management and/or its operations. Also the majority (53%, again: 36% strongly agreed and 17% agreed) that the role of the Board is to represent the interests of particular stakeholders.<sup>21</sup>

### 8.3.1. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Figure 7 shows that there were significant differences between small organisations and large organisations with respect to whether respondents thought that the role of the Board was to participate in management. Respondents from small organisations and organisations not receiving any government funding were much more likely to think that role the Board included participating in management and/or its operations. Likewise, respondents from member-serving organisations were more likely to have this view of the Board's role.

Respondents from member-serving organisations were more likely to think that the Board's role is to represent the interests of particular stakeholders. This raises issues with respect to the duties of nominee directors, discussed in some detail in the Chapter 7, Stakeholders.

<sup>21</sup> There were 8% of respondents who were 'not sure' about this statement.

Figure 7: Role of Board is to participate in the company’s management, based on key indicators

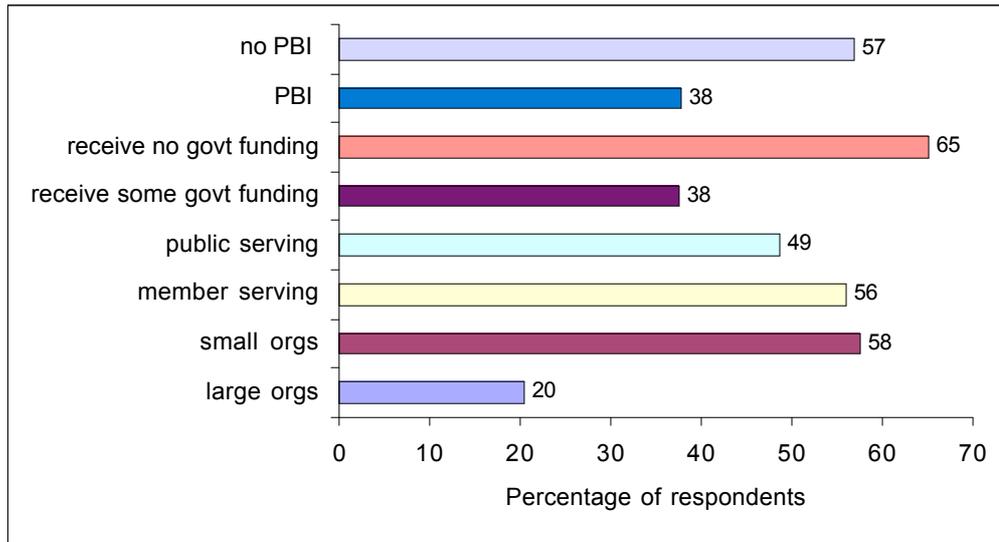
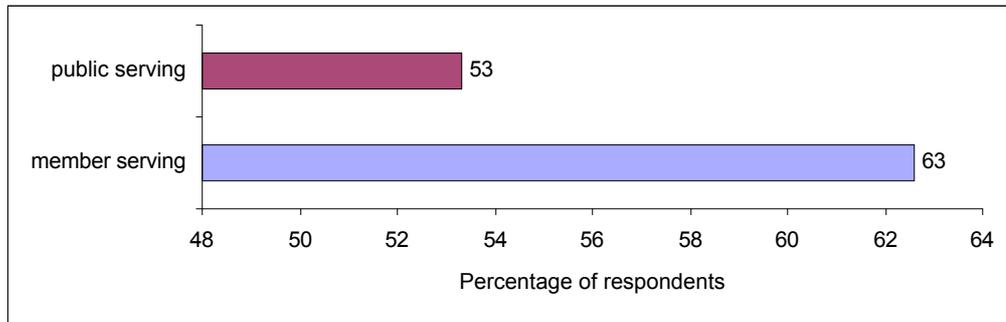


Figure 8: Role of Board is to represent interests of particular stakeholder, based on key indicators



### 8.4. Additional feedback

After the release of the Summary of Preliminary Findings in March 2003, we received the following feedback on the issues of Board selection, accountability and conflicts of interest from an experienced senior employee of a small, national health organisation:

Whatever the legal status of the NFP, most Boards have ‘committee’ mentality, with directors often not having a corporate background and bringing a community organisation mindset to the table. This brings a number of problems:

- A *delegatory* attitude, where their function is perceived as ‘representing’ a certain constituency and influencing the Board in its favour...[this can cause havoc and bad feeling especially, but not exclusively, in member-based organisations]
- An *executive* attitude, where their function is perceived as operational control, with the CEO regarded as an ‘office boy’ who carries them out...
- Difficulty understanding the role of the Board - as the guardian of the NFP’s mission and good name, responsible for ensuring its goals are pursued honestly, prudently and as effectively as possible. This is a subtler, more mature and onerous task than taking the reins away from the CEO.

The difficulty of finding appropriate directors is real, but then so it should be.

This feedback encapsulates some of the key governance issues for NFP Boards and is supported by the data; both the data on the organisational role of the Board and the data on the appointment of directors to represent particular stakeholders (see Chapter 5, Board Size, Composition, Remuneration and Experience).

### 8.5. Observations

It is interesting to note that the majority of respondents (53%) believe that participating 'in the company's management and/or its operations' is one of the Board's roles. This is consistent with the data that 46% of respondents have a smaller management group within the Board<sup>22</sup> which, in some cases, meets as often as daily or weekly (10%). The approach adopted by this significant group of respondents is contrary to that advocated by Drucker,<sup>23</sup> and the generally accepted role of the Board espoused in Australian company law cases.<sup>24</sup> The delineation of Board and staff roles is seemingly complex for many, and it would appear from our data that in some NFP companies (particularly some of the smaller ones), the directors take a very 'hands-on' role, similar to that of directors/controllers of a small, family business.

The role of the Board in bringing together individuals 'with sufficient reputation/connections to assist with fundraising and grant applications' is a role that distinguishes NFP Boards from those of 'for-profits', and which supports the contention that the governance of NFP organisations is more complex.<sup>25</sup>

The need for the development of Australian, NFP governance theory and practices is evident from this Project. In this regard we believe that the data from this Project adds empirical support to comments made by Professor Myles McGregor Lowndes:

Keen insights about the nonprofit sector are required to inform appropriate policy development that will facilitate nonprofit organisations, their transactions and regulation. This research begins with obtaining a notion of the characteristics of nonprofit organisations in Australia and how they differ from nonprofit organisations in other comparable societies and for-profit enterprise...

These insights are necessary not only as to the place of nonprofits in our economy and society, but also how they organize and operate internally. The challenge is to break from the principal and agent paradigm that drives much of the for-profit policy debate in accounting, accountability and governance issues. The nature of most nonprofit organisations with multiple stakeholders, rather than 'owners' does not easily fit into a principal and agent framework. New theories need to be developed taking account of this and other characteristics of nonprofit organizations...Until this theory is developed, tested and applied, regulatory devices may not produce the intended results as they cannot be crafted to suit the attributes of nonprofit behaviour.<sup>26</sup>

## 9. ADVICE RECEIVED

### 9.1. Free legal advice

#### 9.1.1. SURVEY QUESTIONS

- 13.1.1 Has the company received any free legal advice?
- yes
  - no
  - don't know

*Number of respondents = 1657*

<sup>22</sup> See data on smaller management groups reported under Heading 2.1.

<sup>23</sup> See Drucker as outlined briefly under Heading 8.1.

<sup>24</sup> H.A.J. Ford, R.P. Austin & I.M. Ramsay, *Ford's Principles of Corporations Law*, Butterworths, 2003, para [7.060].

<sup>25</sup> For example, D. Lea, 'Voluntary Organizations and Accountability: Theory and Practice' in H.K. Anheier and W/ Seibel (eds), *The Third Sector: Comparative Studies of Nonprofit Organizations*, Walter de Gruyter, New York, 1990. For a summary of the arguments see C. McDonald, 'Board Members' Involvement in Nonprofit Governance' Working Paper No 16, Program on Nonprofit Corporations, Queensland University of Technology, 1993.

<sup>26</sup> See M. McGregor-Lowndes, *Regulatory Infrastructure for Nonprofit Organisations Working Paper PONC97*, August 2000, Queensland University of Technology, pp. 21- 2.

- 13.1.2 If 'yes', was the advice obtained as a result of the actions/connections of a Board member appointed to the Board primarily for their legal expertise?
- yes
  - no
  - don't know

Number of respondents = 967

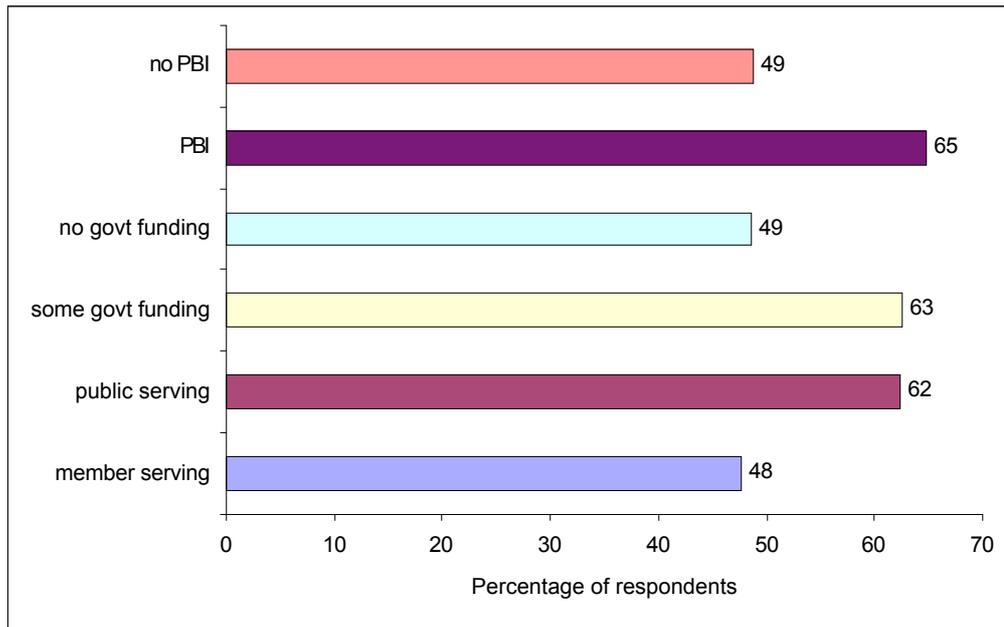
9.1.2. SURVEY RESULTS

Just over half (54%, n=900) of respondents said that the company had received free legal advice. Six per cent said they did not know. Of those that said 'yes', 36% (n=354) received that advice because of the actions/connections of a Board member appointed to the Board primarily for their legal expertise and 5% 'didn't know'. See also data on Board composition reported in Chapter 5, Board Size, Composition, Remuneration and Experience.

9.1.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Interestingly, there were few differences between small and large organisations in relation to whether or not they received free legal advice. Public-serving organisations were more likely to receive free legal advice than member-serving organisations (62% vs 48%) and those receiving government funding were more likely than those that do not to receive free legal advice (63 vs 49%). Philanthropic organisations (71%) and Arts organisations (74%) were the most likely to receive free legal advice.

Figure 9: Free legal advice obtained, based on key indicators



Of those respondents reporting that free legal advice had been received, 36% overall said that it was obtained as a result of the connections of a director. Large organisations were more likely to have received the advice as a result of the connections of a director than small organisations (52% vs 35%), as were public-serving organisations compared with member-serving organisations (43% vs 31%).

Health and Education organisations were also more likely than the overall average to have received the advice as a result of the connections of a director (53% and 49% respectively). Religious (26%), Sports and Recreation (29%) and Interest Group (13%) organisations were the least likely to have received legal advice due to the connections of a director.

### 9.2. Free accounting, financial or investment advice

#### 9.2.1. SURVEY QUESTIONS

13.2.1 Has the company received any free accounting, financial or investment advice?

- yes
- no
- don't know

*Number of respondents = 1653*

13.2.2 If 'yes', was the advice obtained as a result of the actions/connections of a Board member appointed to the Board primarily for that expertise?

- yes
- no
- don't know

*Number of respondents = 821*

#### 9.2.2. SURVEY RESULTS

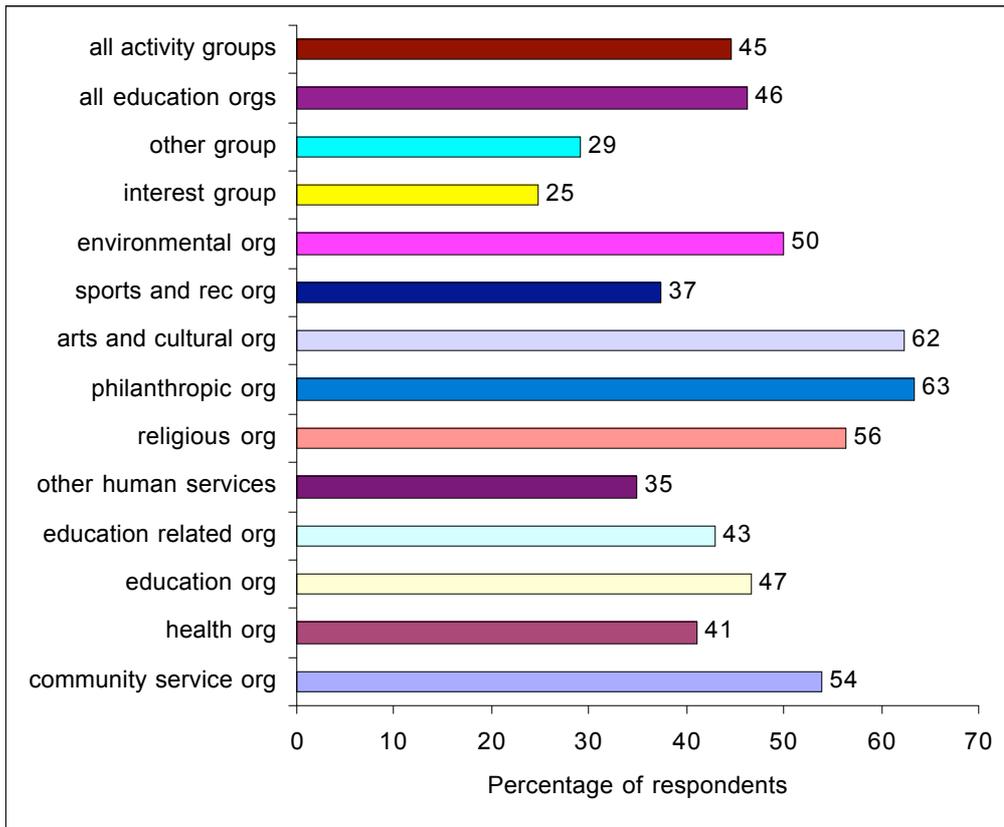
Just under half (45%, n=737) of respondents said that the company had received free accounting, financial or investment advice and 4% said 'didn't know.' Of those that said 'yes', 46% (n=380) said that advice was received as a result of the actions/connections of a Board member and 4% 'didn't know'.

#### 9.2.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Fifty-three per cent of public-serving organisations said they had received free accounting advice compared with 38% of member-serving organisations. This figure was no doubt affected by the fact that only 37% of Sports and Recreation organisations said they had received free accounting advice. In contrast, 63% of Arts and Cultural, 62% of Philanthropic and 63% of Community Services organisations reporting receiving free accounting, financial or investment advice.

The only significant difference with regards to whether that advice was received as a result of a director's connections, was the difference between member-serving and public-serving (41% vs 52%).

Figure 10: Has the company received any free accounting advice, based on principal activity



### 9.3. Auditors' fees

#### 9.3.1. SURVEY QUESTION

- 13.4 Do the company's auditors charge for their services (other than for out-of-pocket expenses)?
- yes
  - no
  - don't know

Number of respondents = 1653

#### 9.3.2. SURVEY RESULTS

Eighty-nine per cent of respondents said that the auditors charged for their services, and 1% said they 'didn't know'.

#### 9.3.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Large organisations were 9% more likely than small organisations to pay auditors fees (97% vs 88%), and member-serving organisations were 7% more likely than public-serving organisations to pay auditors fees (92% vs 85%). Those receiving government funding were also more likely than those that do not receiving government funding to pay auditors fees (91% vs 86%).

Philanthropic organisations were the least likely to pay auditors for their services. Seventy-two per cent of Philanthropic organisations said that auditors charge for their services compared to the overall figure of 89%.

### 9.3.4. OBSERVATION

In 2002, the Office of Small Business estimated the average audit cost for medium-sized companies at \$25,000.<sup>27</sup> There is no reason to think that these figures would be significantly different for NFP companies of a similar size. Given 89% of NFP companies say that auditors charged for their services, this is a considerable cost to the sector. Whilst having accounts audited and maintaining audit independence may be important as a matter of public policy, the cost must be weighed against the benefits.

In Chapter 4, Regulatory Framework, a recommendation is made for setting up a specialist NFP advisory organisation that could provide NFP organisations with audit services at a minimal or at least substantially reduced fee. As the vast majority of respondents pay audit fees (89%), the provision of specialist, low (or no) cost audit services could make a significant difference for many NFP organisations.

## 9.4. Advice received by directors re legal obligations

### 9.4.1. SURVEY QUESTION

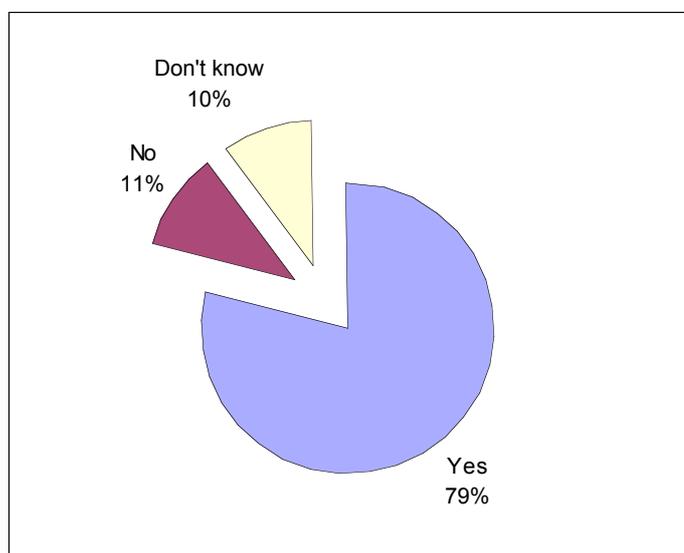
- 13.3 Have directors received any information about their legal obligations as directors?
- yes
  - no
  - don't know

Number of respondents = 1648

### 9.4.2. SURVEY RESULTS

Over three-quarters (79%) of respondents said that directors had received information about their legal obligations as directors, but because 10% said that they 'didn't know' the percentage may be higher than 80%.

Figure 11: Directors received information about legal obligations



<sup>27</sup> Office of Small Business, Department of Employment, Workplace Relations and Small Business, *Submission to the Parliamentary Joint Statutory Committee on Corporations and Securities*, 2001, p. 2. The Motor Trades Association of Australia (MTAA) which represents franchised new motor vehicle dealers, estimated the additional audit cost in excess of \$20,000, Motor Trades Association of Australia, *Submission to the Parliamentary Joint Statutory Committee on Corporations and Securities*, p. 15.

#### 9.4.3. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Ninety per cent of respondents from large organisations said that directors were given information about their legal obligations. That is 13% higher than for small organisations.

Arts and Cultural organisations had the best-informed directors in this respect. Eighty-nine per cent of Arts and Cultural organisations said that directors were given information about their legal obligations, followed by Community Services (84%) and Other Human Service (82%). In contrast, only 67% of Other Groups and 71% of Interest Group directors had received any information about their legal obligations.

## 10. CONCLUSION

The level of commitment of predominately volunteer, non-executive directors is significant - both in terms of what is expected by the organisation and what is given. The majority of Boards meet monthly or more often, and meet for an hour or more.

The written resources made available to directors prior to meetings seem comprehensive, but Boards of smaller organisations maybe at a disadvantage and this is cause for concern. The vast majority of Boards use some form of consensus in their decision making, with 64% always using consensus.<sup>28</sup> The data supports the need for an independent organisation that can assist, particularly smaller organisations, with induction and training of Board members. Our suggested model is for an independent NFP advisory body, see Chapter 4, Regulatory Framework.

In terms of their organisational role, NFP Boards have distinguishing features. A significant group have a smaller sub-group of directors who act as a management team, in some cases meeting daily or weekly. Many view the Board as having additional roles such as assisting with fundraising and representing the interests of particular stakeholders. The delineation of Board and staff roles is seemingly complex for many. Fifty-three per cent of respondents agreed that it is the Board's role to 'participate in the company's management and/or its operation'. The need for the development of Australian, NFP governance theory and practices is evident from this Project.<sup>29</sup>

<sup>28</sup> See Heading 4, 64% always use consensus, although 25% of this group would, as a matter of procedure, take a vote.

<sup>29</sup> In this regard, we would add our support to comments made by Professor Myles McGregor-Lowndes, see n. 26.

## CHAPTER 7: STAKEHOLDERS

### *The more the merrier?*

#### SUMMARY OF KEY FINDINGS IN THIS CHAPTER:

##### Range of stakeholders

- The survey results show that there are a multiplicity of stakeholders in NFP companies.
- Members most frequently cited stakeholder (in the top 2 for 10 out of 11 activity groups and third for the other) even though only 46% of respondents identified their organisations as member-serving.
- Whilst a comparison between principal activities of the organisation and whom they perceive to be their stakeholders reveals some variations, these variations do not provide a clear basis for requiring different levels or types of accountability under the *Corporations Act 2001* (Cth).

##### Tension between stakeholders

- The data bears out the notion that NFP companies are 'object driven'. The most common cause of reported conflict was the tension between NFP objectives and business models.
- Other tension arose from a lack of understanding by some Board members of their role. Namely, to act in the organisation's best interest rather than promoting their own personal profile among members, for example, in a trade association.

##### Complaints to ASIC

- There are proportionately more complaints to ASIC about companies limited by guarantee than other types of companies. Most of these concern 'internal management issues'. These complaints may be the result of conflicts that arise in the course of balancing the different needs of a range of stakeholders.

##### Remedies

- The fact that NFP companies are 'object driven' has not been taken into account by recent corporate law reforms. The mechanisms that members have to initiate proceedings for breaches of the objects clauses are too restrictive and reforms are needed.

#### RECOMMENDATIONS

##### Reform of members' remedies

The special position of members in NFP companies should be further considered in the context of remedies. Members in NFP organisations do not have the same economic power as members of 'for-profit' companies. Nor do they have recourse to a range of shareholder remedies such as selling their shares. Thus members' ability to constrain the actions of Board members and officers of the company, or to ensure that action is taken following a breach of the constitution, is limited. In addition, one of the unique characteristics of NFP organisations is the range of stakeholders with a legitimate interest in the organisation. The public, donors, clients and volunteers all have special stakes in ensuring that the mission of the NFP organisation is pursued and that the organisation's funds are not distributed to members.

The consequences of a breach of NFP objects should be reconsidered, as the mission is what drives an NFP. In this regard we suggest that the following specific reforms be considered:

- All NFP companies should be required to have a 'non-distribution' clause.
- Objects clauses should be compulsory for all NFP companies (not just those holding a licence to omit the word 'limited' from their name).
- Directors should have a specific duty to ensure that the company pursues these objects.
- A breach of the objects clause should be an express ground for bringing an action under s 232 (the oppression remedy) and, possibly, also under s 236 (the statutory derivative action). Modification of s 232 in this way would enable ASIC to initiate action under s 234 on the basis of a complaint by a member or other stakeholder (for example, if in the public interest).

##### Other remedies

It is desirable that NFP organisations and their members have access to expert, low-cost alternative dispute-resolution procedures. This is a valuable role that could be undertaken by the NFP advisory body recommended in this Report (see Chapter 4, Regulatory Framework).

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## 1. INTRODUCTION

The issue of good corporate governance and accountability has always been an important one. Historically, major corporate collapses have often prompted legislative amendments<sup>1</sup> and corporate soul searching - the recent reaction to the collapse of HIH et al is merely the most recent example. As in the 'for-profit' sector,<sup>2</sup> there has also been some soul searching in the NFP sector.<sup>3</sup> The UK *Review of Charities and the Wider Not-For-Profit Sector 2002*, found that charities and NFP organisations should be encouraged to be open and accountable to stakeholders. It stated:

This will both promote public confidence and help them ensure that they are most effectively serving their chosen constituencies, however, defined.<sup>4</sup>

Any examination of accountability necessarily involves a consideration of accountability to whom? In Australia, not much is known about the stakeholders of NFP organisations. We might speculate that the types of institutions, bodies and individuals with an interest in the governance of NFP organisations, and whose interests NFP organisations take into account, differ from those that of 'for-profit' organisations. It would also be reasonable to speculate that the number of stakeholders a NFP organisation must take into account is greater than for 'for-profit' organisations.

The issue of how a NFP organisation can be accountable to a range of different stakeholders is vexed. Interviewed at the *Summit on Non-Profit Leadership*, Professor Mark Lyons said:

One of the difficult questions is just who are constituents or stakeholders. If you are an organisation that deals with, say, youth homelessness, is it just young homeless people? Is it they and their parents, when the parents are often the reason why they're homeless? Is it schools? How do you define constituency and put a border around it to determine who you would seek to invite to membership - and that means voting, as opposed to inviting to be supporters without any democratic responsibility for the maintenance of the organisation.<sup>5</sup>

In terms of company law requirements, the laws governing the question of in whose interests directors must govern are the same for all companies, whether they are companies limited by guarantee or for 'for-profit' companies.

Many of the issues concerning accountability and disclosure are discussed in the Chapter 8, Disclosure. In this Chapter, the main stakeholders of the surveyed NFP organisations are identified and some regulatory issues arising from the list of stakeholders that are identified are discussed.

It may be that the types of accountability to different stakeholders should differ. However, the need to be accountable to a range of stakeholders should be balanced with the requirement that the reporting and decision-making processes of NFP organisations be manageable and not overly complex or burdensome.

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Note: All references in this Report to small and large organisations or companies are based on the definition of "small" and "large" (proprietary companies) as contained in s 45A of the *Corporations Act 2001* (Cth), unless detailed otherwise.

<sup>1</sup> The *Bubble Act* was introduced after many fraudulent promotions of companies to investors. When the 'bubble' burst, the market collapsed and Parliament (over)reacted by introducing the Act. The *Bubble Act* prohibited people claiming corporate status unless incorporated by Act of Parliament or Royal Charter. The Act was repealed in 1825.

<sup>2</sup> For publicly listed companies, this soul searching has resulted in the Australian Stock Exchange's new 'Principles of Good Governance and Best Practice Recommendations', March 2003. Executive general manager and Chair of the Australian Stock Exchange's Corporate Governance Council (CGC), Karen Hamilton, addressed a lunch hosted by the Financial Executives International of Australia, in Sydney on 18 February. She said that company management needed to be 'alive to the concerns of key stakeholders' and to make sure the processes they have in place to monitor such relationships comply with the law: (19/2/2003) Ross Kendall, 'ASX governance guidelines to include CSR', *Ethical Investor* at <<http://www.ethicalinvestor.com.au/>>.

<sup>3</sup> The growing number of Codes of Conduct and Ethical Guidelines that are becoming part of the agreements between funding bodies and NFPs is evidence of this. For a report on Codes of Conduct in the philanthropic sector see the feature titled 'Aspiring to Greater Transparency', *Australian Philanthropy*, Winter 2002, Issue 48.

<sup>4</sup> 'Private Action, Public Benefit: A Review of Charities and the Wider Not-For-Profit Sector', Strategy Unit Report, September 2002, p. 30, 3.9.

<sup>5</sup> T. Wallace, 'Mixed Business', *Australian Financial Review BOSS*, November 2001, p. 50.

## 2. METHODOLOGICAL ISSUES

Two methodological issues warrant brief mention in relation to the survey questions on stakeholders. First, the method of data collection was by survey. While this approach is a useful way to obtain a relatively accurate cross-sectional snapshot of the NFP terrain, it is nonetheless a 'heavy-metal' technique. The stakeholder questions used some open-ended questions to try to unpack the details behind the responses. For instance, to capture the myriad of possibilities of stakeholder types, respondents were asked to name their various stakeholders rather than choosing them from a pre-defined set of broad options. We were simply unable to predict the level of specificity or detail that respondents would need. This open-ended interpretive approach provided high-quality data but at a cost: responses had to be individually coded, which was an extremely time-intensive task. The coding process was further complicated by the fact that often respondents sometimes wrote acronyms that were unknown to us.

Second, respondents were asked only to name their 'three most important stakeholders'. The object, therefore, was not to gain information about the full range of organisations that might be thought of as stakeholders. The decision to choose salience over exhaustive lists was made for pragmatic reasons.

## 3. STAKEHOLDER THEORY OF CORPORATE GOVERNANCE

Within this still emerging literature the concepts stakeholder, stakeholder model, stakeholder management, and stakeholder theory are explained and used by different authors in very different ways. The normative or rights-based construct perceives stakeholders as all those who can affect or be affected by the operations of the organisation. Proponents of this understanding of the stakeholder theory generally accept of the following ideas:

- Stakeholders are people or groups with legitimate interests in procedural and/or substantive aspects of corporate activity. Stakeholders are identified by their interests in the corporation, whether the corporation has any corresponding functional interest in them.
- The interests of all stakeholders are of intrinsic value. That is, each group of stakeholders merits consideration for its own sake and not merely because of its ability to further the interests of some other group, such as the shareowners.<sup>6</sup>

The descriptive or instrumental understanding of stakeholders, which reflects the managerial perspective of the theory, sees stakeholders as those groups and individuals who have a 'legitimate' or 'contractual' interest in the affairs of the organisation. Donaldson & Preston define this understanding as follows:

The stakeholder theory is managerial in the broad sense of that term. It does not simply describe existing situations or predict cause-effect relationships; it also recommends attitudes, structures, and practices that, taken together, constitute stakeholder management. Stakeholder management requires, as its key attribute, simultaneous attention to the legitimate interests of all appropriate stakeholders, both the establishment of organizational structures and general policies and in case-by-case decision making... Stakeholder theory does not necessarily presume that managers are the only rightful locus of corporate control and governance. Nor does the requirement of simultaneous attention to stakeholder interests resolve the longstanding problem of identifying stakeholders and evaluating their legitimate 'stakes' in the corporation. The theory does not imply that all stakeholders (however they may be identified) should be equally involved in all processes and decisions.<sup>7</sup>

The question asked in the survey about the company's stakeholders defines 'stakeholder' as 'those groups of people, other organisations, or even an individual who have a direct and legitimate interest in monitoring the activities and good management of the company'. This explanation of stakeholders reflects the descriptive or instrumental tradition. This may have influenced the responses received.

<sup>6</sup> T. Donaldson & L. Preston, 'The Stakeholder Theory of the Corporation: Concepts, Evidence, and Implications', 1995, 20(1) *Academy of Management Review*, 65 - 91, at 67.

<sup>7</sup> See n. 6.

**4. RANGE OF STAKEHOLDERS**

**4.1. Survey question**

**6. Who are the company's stakeholders?**

By the word 'stakeholder' we mean those groups of people, other organisations, or even an individual who have a direct and legitimate interest in monitoring the activities and good management of the company. By way of example, the company's members, clients to whom the company provides services or, in the case of a church-based company, the church to which it is affiliated.

Bearing this definition in mind, please indicate;

- who you regard as the company's **most important stakeholder(s)** (up to a maximum of three)
- **weight their importance out of 100** (for example, 1 = 40%, 2 = 30%, 3 = 30%—total 100%) and
- **complete the associated questions for each of them**

**6.1.1 Stakeholder A**

(description) .....

% importance .....

*Number of respondents = Stakeholder A 1491, Stakeholder B 967, Stakeholder C 669*

This question was repeated for Stakeholders B and C.

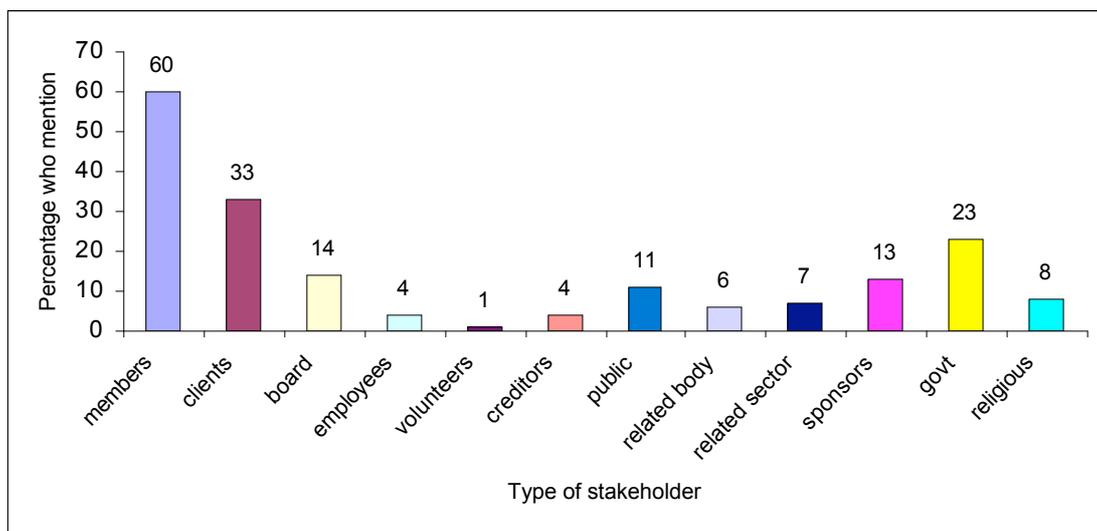
**4.2. Survey results - overall pattern**

As an initial step, all the stakeholder data was combined in order to analyse the overall stakeholder pattern without distinguishing between stakeholder A, B and C, as per the survey question.

As Figure 1 shows, members were the most often cited stakeholder even though 46% of respondents said they were primarily public-serving rather than member-serving. So for the respondent NFP group as a whole, members (60%), clients (33%) and government (this included, local, State and Federal) (23%), were clearly viewed as the most important stakeholders.

Interestingly, volunteers were almost never within the company's most important three stakeholders (1%) although 86% of respondents had at least one volunteer.

**Figure 1: Overall stakeholder profile**



The overall stakeholder data (that is, stakeholders A, B, and C combined) was cross-tabulated with data about respondents' principal activity and other key factors. This was done to examine any further distinctions between NFPs that might be instructive when considering the value of creating categories for legislation. These results follow.

### 4.3. Members

#### 4.3.1. SURVEY RESULTS

'Members' were important stakeholders for all respondent groups, regardless of their principal activity. They were found to be in the top two for 10 of the 11 main activity groups. The remaining activity group, Other Human Services organisations, rated members third. Whilst this might be expected for organisations like Sports and Recreation organisations (shown in Figure 2), which are virtually all member-serving (93% of Sport and Recreation respondents were member-serving), it was a more interesting result for those 46% of all respondents who said they were primarily public-serving. For example, in Health companies (Figure 3) 'members' were the most frequently cited stakeholder, even though 79% of Health companies said they were primarily public-serving bodies.

Figure 2: Stakeholder type, Sports/Recreation (n=281)

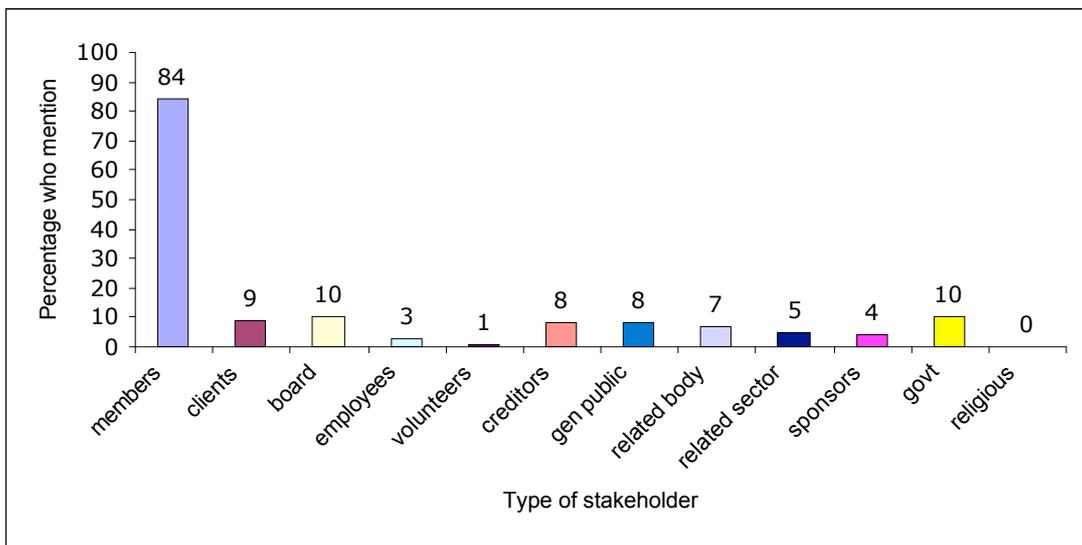
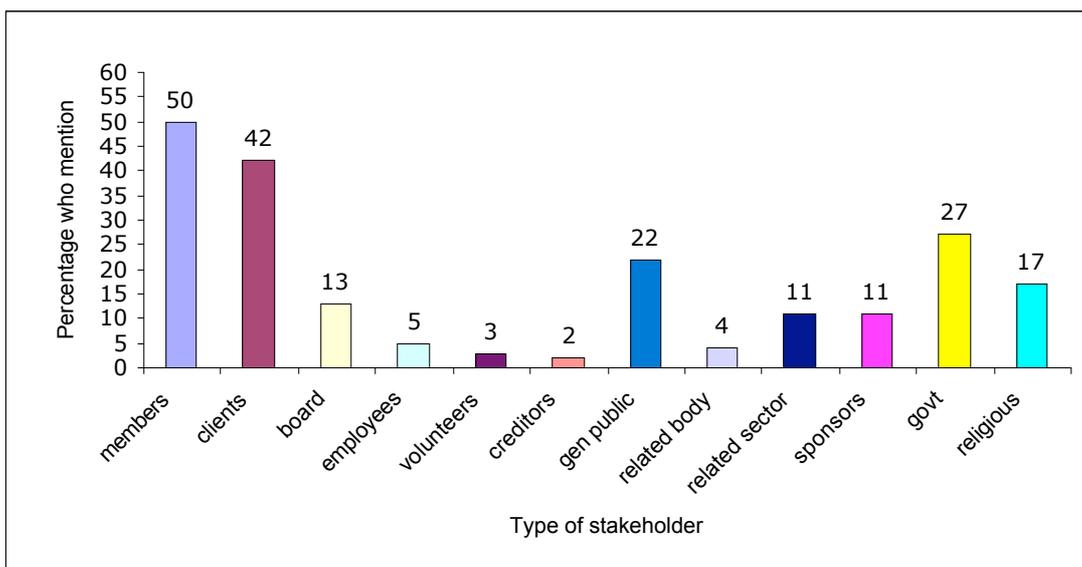


Figure 3: Stakeholder type, Health (n=92)



4.3.2. OBSERVATIONS - ACCOUNTABILITY TO MEMBERS

Members are considered an important stakeholder amongst all types of NFP companies limited by guarantee. As NFP companies do not have shareholders, members have a privileged place within the organisation. Nevertheless, the members' type of accountability and the influence over decision making will differ in different types of organisations. For an Environmental organisation, a large membership will give the organisation greater political sway, and membership subscriptions are a source of funding. However, the organisation is not primarily aimed at serving its members. Rather, its purpose is to conserve the environment. Likewise, a Community Service organisation might say that members are a primary stakeholder, yet they generally do not restrict their services only to members. Other organisations, such as Other Human Services organisations, do not see members as their primary stakeholders. A comment from one respondent was:

Our primary 'stakeholders' are NOT our members. Rather they are 'clients' (missionaries and their spouses/families) and supporters (prayer and financial).

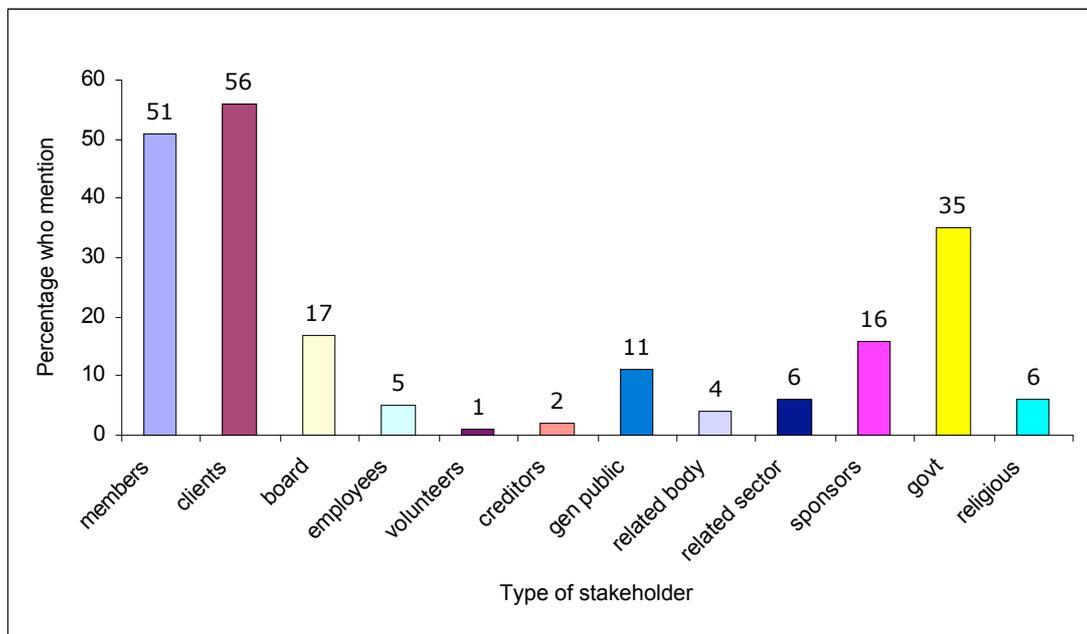
This raises some complex questions that point to problems with the current legal structure of NFP organisations incorporated as companies limited guarantee. Members have privileged legal status. They are able to determine the direction of the organisation,<sup>8</sup> and the Board is primarily accountable to its members. However, the members may not be the primary stakeholder. Rather, the clients may be. As Leat asks, 'if they provide equal rights for members and non-members, why should members pay to join?'<sup>9</sup>

4.4. Clients

4.4.1. SURVEY RESULTS

'Clients' were found to be one of the top three stakeholders for all principal activity groups except Religious, Philanthropic, Sports & Recreational and Environmental respondents. As Figure 4 shows, 'clients' were the most cited stakeholder for Community Services respondents (ahead of 'general public' at 22%). This is an interesting result given that 83% of Community Services respondents said that they were public-serving. It might be concluded, therefore, that this type of organisation believes that they serve the public by serving their specific client group. This finding assists in clarifying the meaning of 'public-serving' for NFP organisations. The notion of 'public' is not some undifferentiated public, but rather, specific, targeted segments of the community.

Figure 4: Stakeholder type, Community Service (n=264)



<sup>8</sup> For example, by determining the objects contained in the company's constitution.

<sup>9</sup> See D. Leat, *Managing Across: Similarities and Differences Between For-Profit and Voluntary Non-profit Organisations*, City Business School, 1993 p. 44.

#### 4.4.2. OBSERVATIONS - ACCOUNTABILITY TO CLIENTS

The importance of clients compared with other stakeholders may be indicative of a recent trend towards 'client-centric' service amongst NFP organisations. This result, as with the results for 'members',<sup>10</sup> demonstrates that NFP organisations may be overcoming the 'paternalistic' brand they have often been charged with in the past. Leat, for example, observed a decade ago that 'many voluntary organisations have been accused of combining a mission of serving consumers with a paternalistic ethos which has effectively ignored service recipients as key constituents'.<sup>11</sup>

This is the result of a few factors:

- market mechanisms have been applied to the NFP sector
- there has been a change of culture
- an organisation's legitimacy and funding is often dependent upon their doing so.<sup>12</sup>

### 4.5. Volunteers

#### 4.5.1. SURVEY RESULTS

Volunteers were almost never included within respondents' most important three stakeholders (1%). This data does not reflect the importance of volunteers to NFP companies. The survey results showed that NFP companies rely heavily on volunteers. Eighty-six per cent of respondent companies had at least one volunteer, 38% have 20 or more, and thirty-one organisations had more than 1,000 volunteers. The results also showed that the vast majority of directors of NFP companies are voluntary - 92% of respondents did not pay their directors.<sup>13</sup>

#### 4.5.2. OBSERVATIONS- ACCOUNTABILITY TO VOLUNTEERS

It is possible that many respondents, particularly member-serving respondents such as Sports and Recreation organisations, do not distinguish between members and volunteers. The volunteers of a Tennis Club, for example, are most likely its members. Yet this will not always be the case. Further inquiry into the way that volunteers' interests and concerns are taken into account by NFP organisations would be interesting in light of these results.

There are some additional legal issues that arise in relation to volunteer work in NFP organisations. Pro Bono Australia, for example, received legal advice revealing that volunteers are often not covered by Workcover.<sup>14</sup>

### 4.6. Government

#### 4.6.1. SURVEY RESULTS

'Government' was cited in the top four for all groups except Philanthropic (9%) and Religious (1%).

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<sup>10</sup> See Heading 4.3.

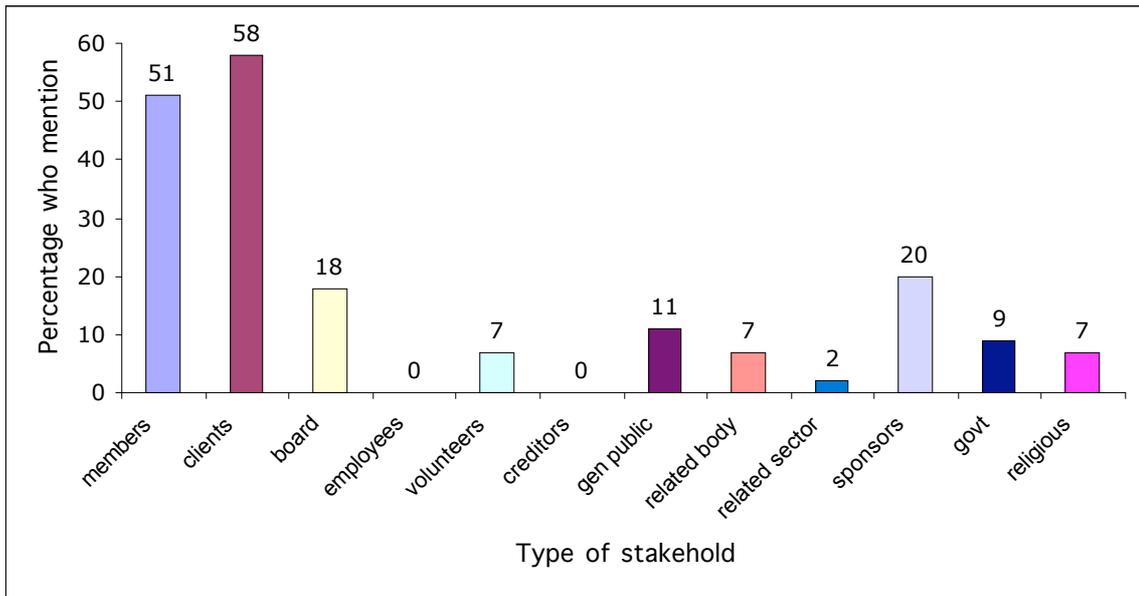
<sup>11</sup> See Leat, n. 9, p. 42.

<sup>12</sup> Leat points out NFP organisations have been used increasingly by local authorities to fulfil legal requirements to 'consult the community'. Having neither the time or resources nor the channels of communication to do so themselves, local authorities have turned to voluntary organisations as an easy and available vehicle for fulfilling their legal responsibilities: Leat, n. 9, p. 46.

<sup>13</sup> See Chapter 1, Profile Data.

<sup>14</sup> 'Volunteers - Covered by 'Workcover'?', Pro Bono Australia Not-for-Profit Newsletter, Volume 6, Edition 7 - 9/23/02 at <<http://www.probonoaustralia.com.au/new/NewsletterPrint.asp>>.

Figure 5: Stakeholder type, Philanthropic (n=45)



4.6.2. OBSERVATIONS - ACCOUNTABILITY TO GOVERNMENT

The result for Philanthropic organisations (shown in Figure 5) is noteworthy (although the small number of respondents to this question, n=45 should be borne in mind). It can be assumed that almost all Philanthropic organisations have charitable status, which enables them to enjoy taxation benefits. It is reasonable to expect that such a taxation concession would give rise to the 'government' or 'general public' having a legitimate interest in their governance and that they would, therefore, cite government more frequently than they have. This is bearing in mind that the definition of stakeholder provided in the survey was 'groups of people, other organisations, or even an individual who have a direct and legitimate interest in monitoring the activities and good management of the company'.

On the other hand, many Philanthropic organisations feel that their independence from government is crucial for them to play a proper role within a liberal pluralist society. Therefore they do not think of government as a primary stakeholder. Further, many philanthropic bodies are established to serve a specific client group in society, and like Community Service organisations, might privilege that relationship over any stakeholder relationship they have with the 'general public' or 'government'. It is nevertheless significant that the 'general public' or the 'government' did not rate within the top four stakeholders for Philanthropic organisations, and this may be an interesting topic for further inquiry.

Further issues concerning accountability to government are discussed in the Chapter 8, Disclosure.

4.7. General public

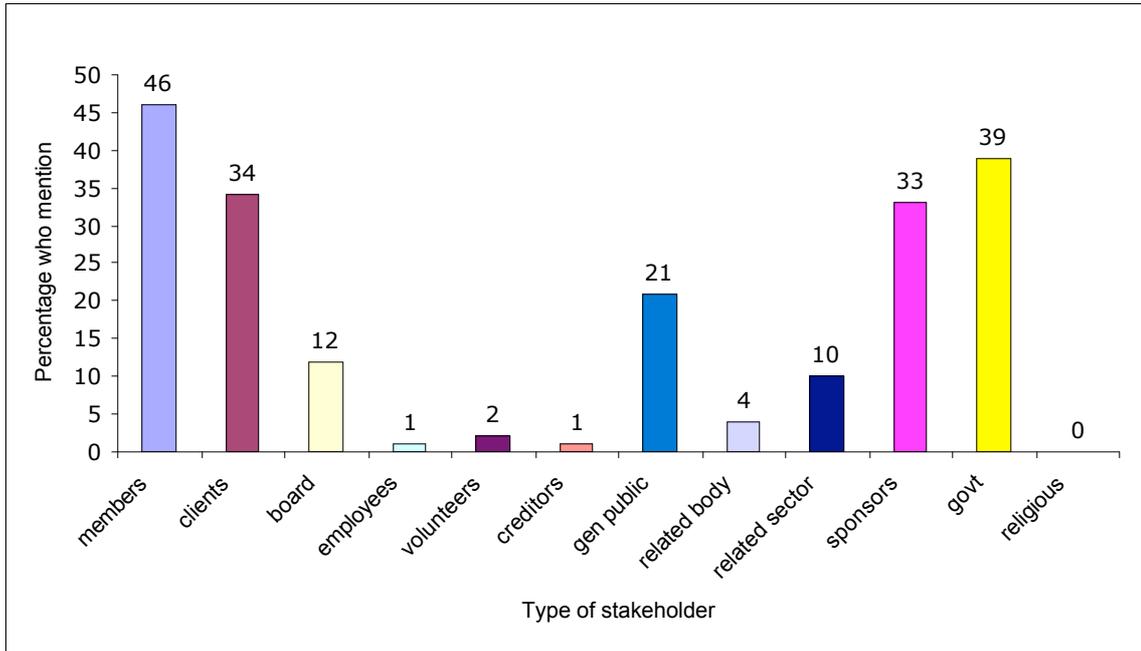
4.7.1. SURVEY RESULTS

The overall frequency with which 'general public' was cited as a stakeholder was 11%. Those groups mentioning 'general public' more frequently were Health organisations (22%, see Figure 3), Arts and Cultural organisations (21%, shown in Figure 6), and Environmental organisations (33%). These organisations are all predominately public-serving, therefore this response might be expected.

The low percentage of respondents citing 'general public' as a stakeholder is particularly interesting for those organisations with PBI status (27% of respondents).

The comments raised under the Heading 4.6.2, are also relevant to 'general public' as a stakeholder.

Figure 6: Stakeholder type, Arts and Cultural (n=95)

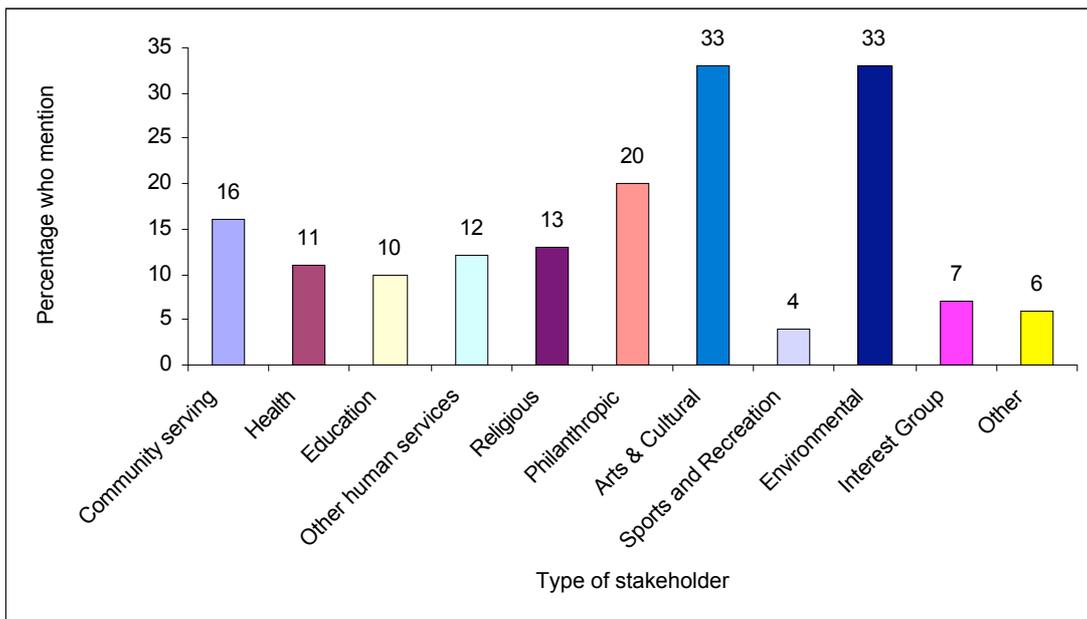


## 4.8. Sponsors

### 4.8.1. SURVEY RESULTS

Overall, only 13% of respondents mentioned 'sponsors' as a stakeholder. (By sponsors, we mean donors and grantees). Arts and Cultural and Environmental organisations mentioned 'sponsors' most frequently as a stakeholder - 33% of both. Sports and Recreation organisations (Figure 7) were least likely to mention sponsors as a stakeholder - only 4%

Figure 7: Percentage mentioning 'sponsors' as a stakeholder



### 4.8.2. OBSERVATIONS - ACCOUNTABILITY TO SPONSORS/FUNDERS

Sponsors or funders of NFP bodies may be made up of a variety of groups with diverse characteristics, demands and expectations. In general, sponsors may include individual donors, corporate donors, trusts and philanthropic bodies, and all levels of government. These broad groups may be further separated into different governmental departments, and different types of corporate and individual donors.<sup>15</sup> (Note: in this Report, 'government' as a donor is included in the category 'government', not 'sponsor'.) Each of these sub-constituencies is likely to have different expectations, values and priorities in funding the organisation.

Those who fund an organisation are clearly in a special position to demand accountability, and it is likely that this will be mandatory and with sanction. The right to require accountability may be contractual, and funders may apply the sanction of withdrawing financial support.

The task of managing the requirements of various funders may increase the complexity of managing an organisation. On the other hand, the greater the number of funders, the less likely it is that any one funder will possess real sanctions in relation to the direction and conduct of the organisation. Indeed, the very variety of funders and their expectations may enable the organisation to claim legitimacy whatever it chooses to do.<sup>16</sup>

A funder's ability to require meaningful accountability will also be limited by their understanding of the operations of the organisation. Indeed, one reason why a government department might fund an organisation is precisely because they lack the capacity to provide the service themselves. While they may be able to require fiscal accountability, they may be unable to require real process or programme accountability. If an organisation does not rely on one funder then it may have the power to insist upon an unrestricted grant.<sup>17</sup>

## 4.9. Related bodies

### 4.9.1. SURVEY RESULTS

The overall frequency with which all respondents to this question mentioned 'related bodies' as a stakeholder was 6%. Interest Group organisations (n=100) mentioned related bodies most frequently - 12%.

The data reported in Chapter 3, Legal Structure shows that while group structures are par for the course in listed public companies and even in medium-size businesses, they were uncommon among our respondent NFP companies. The profile data showed that only 14% were part of a group structure and, even within that 14%, the majority only had one or two related entities. (For example, one proprietary company or one foundation.) Further, 74% of respondents had only individuals as members and not all peak bodies had organisations as members. Philanthropic bodies were most likely to be part of a group structure (29%), with 86% of their 'related bodies' being trusts or foundations. Only 13% of Interest Group organisations had related bodies.

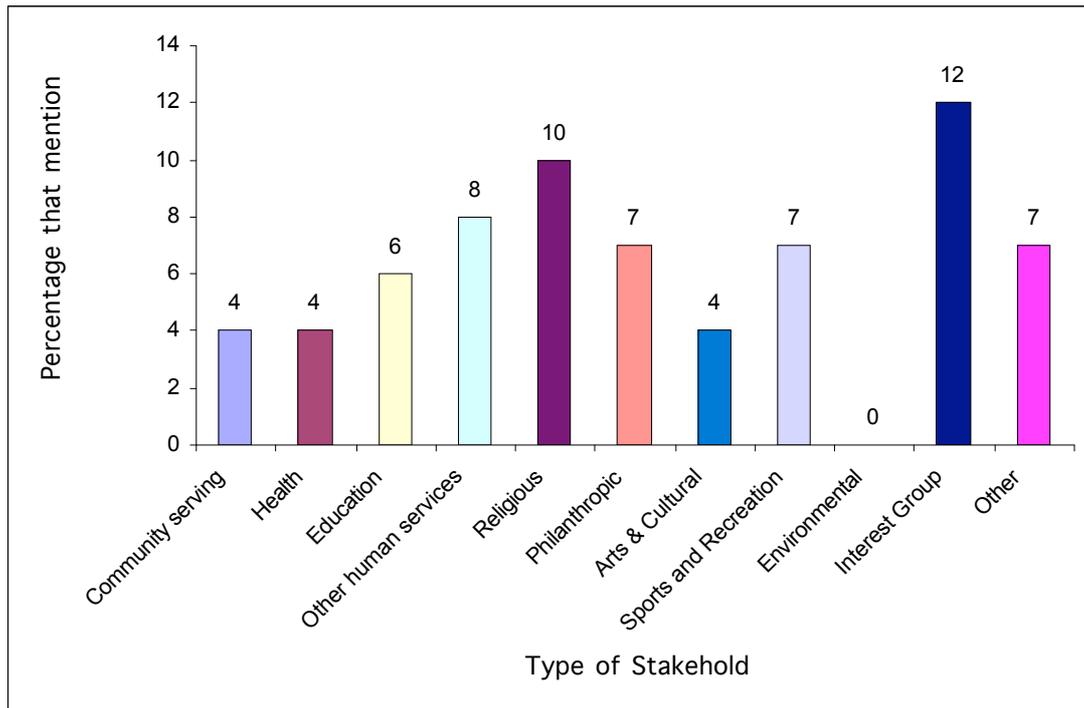
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<sup>15</sup> Leat, n. 9, p. 44.

<sup>16</sup> Leat, n. 9 p. 45.

<sup>17</sup> This is the case for some organisations seeking to maintain independence from funders. For example, a health organisation may accept funding from a pharmaceutical company on the basis that the grant is unrestricted.

Figure 8: Percentage mentioning 'related body' as a stakeholder



4.9.2. OBSERVATIONS - ACCOUNTABILITY TO A RELATED BODY

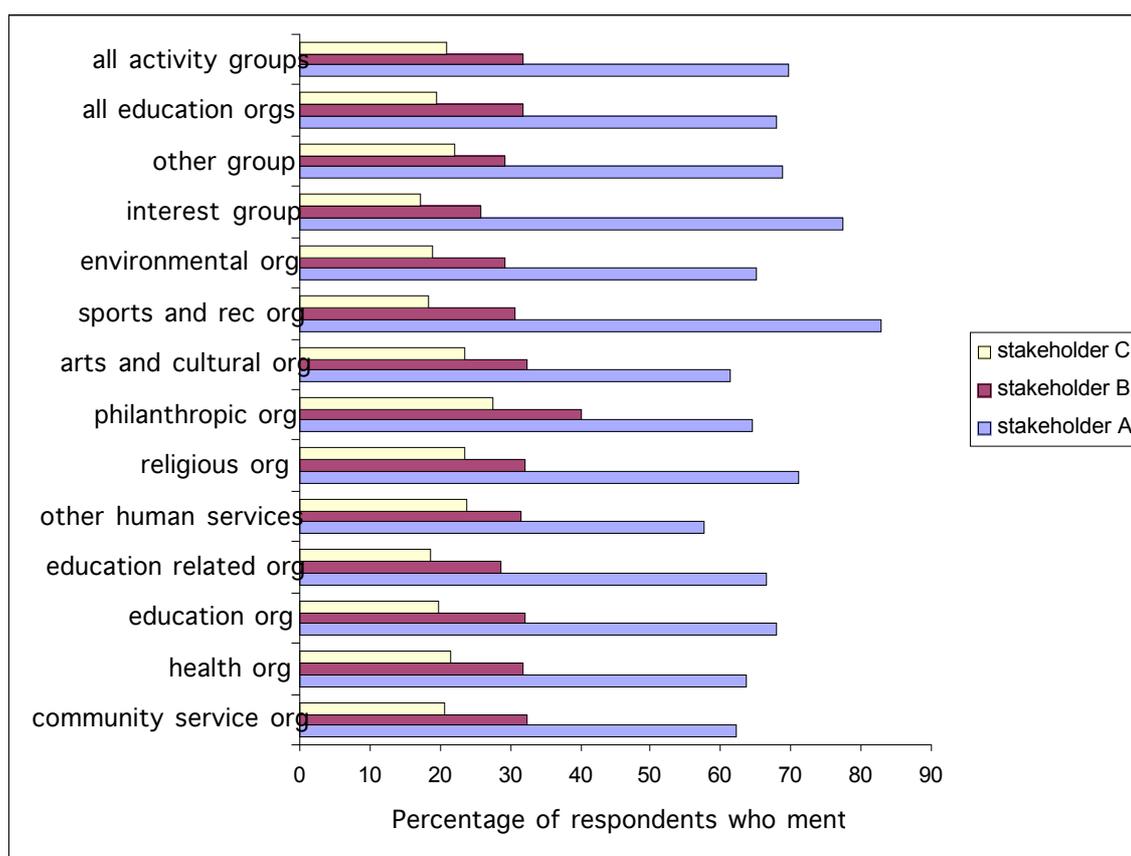
Those respondents who mentioned a related body as a stakeholder are most likely to be peak bodies, with the related bodies being their branches. Another example of a related body is the trading arm of a church body. The existence of related bodies raises problems in reconciling overall standards and accountability with flexibility and a measure of autonomy. Not only do branches have to be accountable to headquarters, but branches may demand accountability from headquarters. Furthermore, a peak body may have some members that are companies and others that are incorporated associations. This means that the laws regulating the member organisations will differ significantly, and make the provision of training and advice complex.

4.10. Importance of stakeholders A, B and C compared

Respondents were asked to rate the importance of each stakeholder they named. Figure 9 shows that for each activity group, Stakeholder A was rated the most important, Stakeholder B was the second most important, and Stakeholder C was the third most important. There were exceptions within each group based on principal activity. Some did not rank their stakeholders from A to C, but overall this pattern prevailed.

While this data is not particularly significant in itself, it is helpful because it confirms that further comparison between respondents based on factors such as public-serving or member-serving is possible.

Figure 9: Importance of stakeholder A, B and C for each activity group



#### 4.11. Significant differences - member-serving or public-serving

The pattern of stakeholders for member-serving organisations was compared with public-serving organisations. As expected, in member-serving organisations, 'members' are very clearly the key stakeholder. The 'government' and the 'general public' are regarded as considerably less important in member-serving organisations, compared with public-serving organisations. In public-serving organisations 'clients' (44%) and 'members' (44%) ranked at a fairly similar level to 'government' (32%). However, the 'government' and 'public' (17%) rank lower than might have been expected for public-serving companies.

Table 1: Member-serving vs public-serving

<b>Member-serving</b> (n = 801)		<b>Public-serving</b> (n = 647)	
members	74%	members	44%
clients	24%	clients	44%
government	17%	government	32%
public	6%	public	17%

#### 4.12. Significant differences - receipt of government income

Respondents who reported receiving government income were compared with those who received none. The results demonstrate that the presence of any government funding seems to create a significant stakeholder relationship. It also meant that the 'general public' became more significant.

This result most likely reflects the effect of government funding contracts, which often have extensive reporting obligations.

Table 2: Government income vs no government income

<b>Government income</b> (n = 634)		<b>No government income</b> (n =816)	
Members	49%	members	70%
Clients	47%	clients	23%
Government	43%	government	8%
Public	14%	public	8%

### 4.13. Conclusions - range of stakeholders

The data reported in this Chapter reveals that there is a very broad range of stakeholders whose legitimate interests in the organisation must be taken into account. The question of stakeholders is directly relevant to the issue of accountability. The issue of how an NFP organisation can be accountable to a range of different stakeholders is vexed.

The results about membership support Lyons’ observation<sup>18</sup> that defining constituencies and determining the basis of membership is a difficult issue for NFP companies. Although members have a privileged legal place within NFP companies, they were not found to be the primary stakeholder for all organisations. This raises important questions about how other important stakeholders influence the decisions of the organisation and demand accountability.

The term accountability has many different meanings. In legal terms, it has implications in terms of in whose interests decisions must be made, and concerning disclosure requirements. That is, who NFP organisations provide reports to, who they ought to report to, and how that disclosure occurs.

Analysis of the results based on distinctions between respondents revealed that the stakeholders NFP organisations consider to be important differs, based according to the principal activity of the organisation. However, our view is that the variations do not provide a clear basis for requiring different levels or types of disclosure under the *Corporations Act 2001* (Cth).

## 5. CLASSIFICATION OF NFP STAKEHOLDERS

As mentioned under Heading 2, the data reported in this Chapter concerns those individuals, groups or bodies that respondents themselves consider to be stakeholders (‘the Survey Stakeholder List’). These may or may not be the same as those with whom they actually have a formal relationship of accountability. Australian researchers Flack & Ryan, also note this ‘decoupling’ of a formal notion of accountability from what is perceived to be ‘their real accountabilities to donors, supporters, service users’ in their recent case study of a hospital foundation.<sup>19</sup> We thought it worthwhile to compare the Survey Stakeholder list with that compiled by Flack & Ryan.

### 5.1. Comparison of survey data with other classification research

A comparison of bodies or people named in the Survey Stakeholder List with Flack & Ryan’s typology is shown in Table 3. The comparison suggests that the survey results reported in this Chapter can add to the existing literature by pointing towards a hierarchy or prioritisation of stakeholders based on the views of NFP respondents.

At first glance, the comparison reveals significant omissions in the Survey Stakeholder List. But upon closer analysis, there are, in fact, few substantive differences.

<sup>18</sup> See Lyons as quoted under Heading 1, see n. 5.

<sup>19</sup> T. Flack, & C. Ryan, ‘Accountability of Charitable Organisations: Meanings and Mechanisms’, Conference presentation at ANZTS, Auckland, November 2002, unpublished, p. 14.

Table 3: Comparison of Flack & Ryan’s typology with the Survey Stakeholder List<sup>20</sup>

Flack & Ryan’s typology	Stakeholder Survey List, % who mention as one of up to 3 stakeholders
<i>Inside stakeholders (providers of resources)</i>	
Board members	Board (14%)
members	members (60%)
employees	employees (4%)
professional staff	
paid workers	
volunteers	volunteers (1%)
purchasers/users of services	clients (33%)
creditors	creditors (4%)
suppliers of goods and services	
donors	sponsors (13%)
private grant makers	
government funders	
<i>Outside stakeholders (parties performing a review or oversight function)</i>	
government regulators (accountability agents for general public)	government (23%)
media (accountability ‘watchdog’ for general public)	
professional bodies	
labour unions	
employer groups or ‘Peak bodies’	related bodies (6%)
analysts and advisors	
special interest groups/minorities	
charity ‘watchdog’ organisations	
community/general public	general public (11%)
	religious body (8%)

## 5.2. Observations on the comparison

In making the comparison between Flack & Ryan’s typology and the Survey Stakeholder List it is important to bear in mind in the methods used in conducting and interpreting the survey data from which the Survey Stakeholder List has been compiled. The survey respondents were limited to naming three stakeholders and thus did not have an opportunity to list all the stakeholders who might have a legitimate interest in their organisation, or to whom they have a duty to report. In presenting the results, the aim was to reduce the survey responses to (approximately) the ten most common, rather than presenting an exhaustive list. Flack & Ryan’s typology does not prioritise stakeholders, as was the task for the respondents in the survey, it merely lists them.

Bearing in mind these methodological differences, a comparison of the two lists is instructive. Flack & Ryan divide stakeholders into ‘inside stakeholders’ (providers of resources) and ‘outside stakeholders’ (parties providing a review or oversight function). They acknowledge that this distinction may be problematic for the NFP sector because their stakeholder list has been drawn largely from literature in the ‘for-profit’ and government sectors.<sup>21</sup> Seven out of 12 of the stakeholders listed in the Survey Stakeholder List are ‘inside stakeholders’ according to Flack &

<sup>20</sup> Adapted from T. Flack. & C. Ryan, 2002, n. 19, p. 5. Flack & Ryan’s typology represents a literature survey. The original table includes a column for authors.

<sup>21</sup> Flack & Ryan, n. 19, p. 5.

Ryan's typology. The 'inside stakeholders' mentioned by our survey respondents were members (60%), clients (33%), the Board (14%), employees (4%), creditors (4%), sponsors/donors (13%) and volunteers (1%). Other 'inside stakeholders' listed by Flack & Ryan were mentioned by survey respondents. It is necessary to take into account that our coding used slightly different terminology:

- The term 'sponsors' used in the survey stakeholder list includes donors, private grant makers and government funders. Flack & Ryan distinguish between government regulators and government funders, a distinction that would have been useful for our survey.
- The term 'clients' in the Survey Stakeholder List correlates with purchasers/users of services.
- The Survey Stakeholder List makes no distinction between types of employees, whether they are employees, professional staff or paid workers.

The 'outside stakeholders' mentioned by the respondents to the survey include:

- government, which in turn included State, Federal and Local government, as well as ASIC and funding departments (23%)
- public, which includes local community groups or subsections of the general public (11%) and peak bodies (included under the category 'related bodies' (6%) in the Survey Stakeholder List)

Religious body (8%) is not included on Flack & Ryan's typology, but is included on the Survey Stakeholder List.

The respondents to the survey did not mention the media, professional bodies, labour unions, employer groups, analysts and advisors, charity watchdogs or special interest group/minorities. (If charity watchdogs were government based, they were included under the 'government' category in the survey.) Labour unions and employer groups may be less relevant to many NFP organisations because of the high level of reliance upon volunteers, rather than employees. Nevertheless, some of these bodies, particularly labour unions and employer groups, have a legitimate (often legal) interest in NFP companies, and any consideration of reporting requirements should take them into account.

Flack & Ryan have carried out a comprehensive synthesis of the academic literature on the topic, and, despite differences between the survey and their typology, there is significant overlap.

## 6. TENSION BETWEEN STAKEHOLDERS

### 6.1. Survey question

- 6.2.4 Has there been any significant tension between this stakeholder (or any individual within the group) and the company OR between this stakeholder and any other stakeholder in the company?
- yes
- no

*Number of respondents = Stakeholder A 1533, Stakeholder B 988, Stakeholder C 672*

- 6.2.5 If 'yes', please explain the nature of the tension and, if it has been resolved, how it was resolved.

*Number of respondents = 123 in total*

### 6.2. Survey results

#### 6.2.1. QUANTITATIVE DATA

For Stakeholder A, 12% reported some tension between Stakeholder A and the company or between Stakeholder A and any other stakeholder in the company. This rate was similar for Stakeholders B and C - Stakeholder B 14% and Stakeholder C 13%.

### 6.2.2. QUALITATIVE DATA

One hundred and twenty-three respondents wrote a comment giving some detail about the nature of the tensions between the company and the stakeholder, or the tension between stakeholders. Analysis of these comments revealed two broad categories of tension. They were 'organisational mission vs business model' and 'stakeholder self interest vs organisational interest'.

Of those respondents commenting, the predominant group (49 out of 123) could be classified in the first group. Namely, tension between the requirement to take on business strategies in order to remain viable, while still meeting the organisation's NFP objects or mission. By way of illustration, one respondent wrote that there had been this type of conflict between the company and volunteers:

In order to remain a viable company, we have had to employ normal business models. This new attitude has conflicted with stakeholders' perceptions of what the company should stand for. Only partially resolved.

In relation to the way this type of conflict had arisen with funding bodies, one respondent wrote:

The company straddles two worlds: social justice and commercial reality. Funding bodies have seen that by aligning with one, we damage the other. Mainly resolved now, by explaining we do no different to them.

In relation to this type of conflict with sector affiliates, the comment was:

These stakeholders think the company has abandoned its original aims in pursuit of money. Partially resolved by explaining that without money we will not be able to continue in business. (Amazingly, this really does require explanation!)

It needs to be noted that the respondents to the questionnaire were mainly 'managers' or CEOs, people who are charged with the responsibility of sound financial management, and not volunteers, who might have different views on this issue.

## 6.3. Tension between NFP mission vs business model

### 6.3.1. OBSERVATIONS

Anecdotal evidence suggests that there is a growing tension within many NFP organisations between:

- the requirement to take on business strategies in order to remain viable
- meeting the organisation's NFP objects or mission.

By way of a recent example, an article in *The Age* in January 2003<sup>22</sup> reported a conflict that arose between volunteers in Shepparton and the head office of St Vincent de Paul. The conflict led to the dismissal of the Sandhurst branch by the Board of St Vincent's via a fax, a move that volunteers found 'more fitting a boardroom than one of Australia's biggest and best-loved charities'. Peter Ellingsen, the reporter, described the nature of the crisis as follows:

...Vinnies...is just one of many non-profit groups caught in an identity crisis. Government cuts, compassion fatigue and corporatisation of welfare, have left charities unsure of whether they are businesses or benevolent collectives.<sup>23</sup>

This tension increases as organisations grow and take on more traditional 'for-profit' 'management strategies. The tension may also be exacerbated by the requirements of funding bodies - whether private or government-based - that have a legitimate interest in the financial soundness of management strategies. In an environment of intense competition between NFP bodies for funding, closer attention is being paid to efficiency and effectiveness, and there is an increasingly professional and analytical approach to what is done, why and at what cost.<sup>24</sup>

Leat argues that this pressure for more 'management' also stems from the sector's changing relationship with government and its role in relation to public policy and service provision. Like the conservative governments in the UK, which Leat examines, the Coalition Government in Australia has emphasised 'partnership' with both the NFP and 'for-profit' sectors in a wide range of service provision areas. There has been a large scale contracting-out of services, notably in employment services, which has increased the size of the sector in terms of income and the number of bodies.

A survey carried out by the Australian Management Corporation in 2002 found that there was clear evidence of a move toward government funding. The survey also identified that the

<sup>22</sup> P. Ellingsen, 'Charity gives itself heartache', *The Age*, Perspective, 9 January 2003, p. 9.

<sup>23</sup> *The Age*, n. 22.

<sup>24</sup> D. Leat, above, n. 9, p. 5.

competition between organisations for public support was intense and continuing to increase.<sup>25</sup> This increased competition for funds is likely to lead to less co-operation between charities.<sup>26</sup>

There is no consensus within the sector regarding how to deal with the tensions, or whether indeed, the tensions are real, as Ellingsen's article, and the many subsequent letters to the editor that it generated, identified:

As government and public money has dried up, they have been forced to turn to business or to accept government contracts, and that has meant adopting corporate manners. For some...the shift towards 'partnerships' with business and government is positive. Social entrepreneurs, as the new charity chiefs are now called, are the future, says McClure, who chaired a Federal Government welfare inquiry.

But there are others, like former Brotherhood of St Laurence director, David Scott, who see the move as further marginalisation of the poor, and a way of limiting the advocacy role charities have traditionally played.<sup>27</sup>

Many of the respondents' comments in this section reported a similar source of tension.

### 6.3.2. IS THERE REAL TENSION BETWEEN NFP MISSION AND BUSINESS MODELS?

This issue is relevant to any question of whether NFP organisations should be treated differently under company law than 'for-profit' companies.

Some would argue that differences between NFP objects and 'for-profit' management strategies are exaggerated. This was certainly the view of some respondents (see, Heading 6.2.2). Leat questions the 'not concerned with profit' vs 'driven by profit' distinction between NFPs and for-profit organisations. She argues that:<sup>28</sup>

- in both sectors 'profit' is an unclear concept - its meaning and measurement vary
- some NFPs and parts of others generate profit/surplus - even if they cannot distribute that profit
- the timescale over which 'for-profit' organisations attempt to maximise profit varies
- it is debatable whether profit maximisation is the primary goal for all types of 'for-profit' organisations in all types of markets. Maximising sales and/or growth may be equally, if not more, important.

Further, she points out that 'the financial liability of for-profit entrepreneurs is likely to be hedged by financial institutions, whereas in non-profits risk may be less well insured'.<sup>29</sup> When this risk is taken into account, it makes sense that NFP organisations may need to be particularly careful to ensure that the long-term financial surety of the organisation is firmed up.

Despite these caveats, it remains the case that profit and financial measures alone are an inadequate and inappropriate basis for measuring performance in NFP organisations. Moss Kanter & Summers<sup>30</sup> point out that the real difference between 'for-profit' and NFP organisations in establishing performance indicators lies not so much in the lack of profit, but rather the intangible nature of what is typically provided by NFP organisations.

Whilst the measurement of performance is not easy in any organisation, profit, as a marker, can be measured easily. Because it is seen by 'for-profits' as a good test of market satisfaction and of the capacity of an organisation to run itself efficiently, profits are generally the main measure of performance. NFP organisations, in contrast, define themselves not by their financial returns but by the services they offer. These services are often intangible and difficult to measure and clients, employees, managers, volunteers and donor/funders may make different judgments with regard to their quality. This has led Moss Kanter & Summers to argue that it is not lack of profit per se, but rather the centrality of (intangible) social values over (objective) financial values that complicates management for NFP organisations.<sup>31</sup>

<sup>25</sup> 'Your guide to Victoria's Not-for-Profit Organisations', advertising feature in *The Age*, Monday, 3 June 2002. See Heading 3.2.3 in Chapter 6, Disclosure, for further information about the survey.

<sup>26</sup> For example see comments by Commissioner Doug Davis (Salvation Army, Melbourne): 'We were always competitive, but now it's absolutely the case, it's crystal clear it's the case. 'Australia - Salvation Inc - Inside the Salvation Army', *The Australian*, Dossier, 23 June 2001.

<sup>27</sup> *The Age*, n. 22.

<sup>28</sup> D. Leat, n. 9, p. 1.

<sup>29</sup> D. Leat, as above, n. 9.

<sup>30</sup> R. Moss Kanter & D.V. Summers, 'Doing Well While Doing Good: Dilemmas of Performance Measurement in Non-profit Organisations and the Need for a Multiple-Constituency Approach', in W.W. Powell (ed.), *The Nonprofit Sector; A Research Handbook*, Yale University Press, New Haven, CT, 1987.

<sup>31</sup> Kanter & Summers, n. 30.

Within the current contract culture, NFP organisations may have to learn to juggle the intangible goals of public benefit/service with the more tangible objectives of acquiring contracts and satisfying a variety of paying and non-paying customers within the constraints of the real cost of financial survival. If profit is nothing more than the real cost of staying in business, then profit is likely to be of increasing concern to NFP organisations.<sup>32</sup>

#### 6.4. Tension between self interest vs company's interests

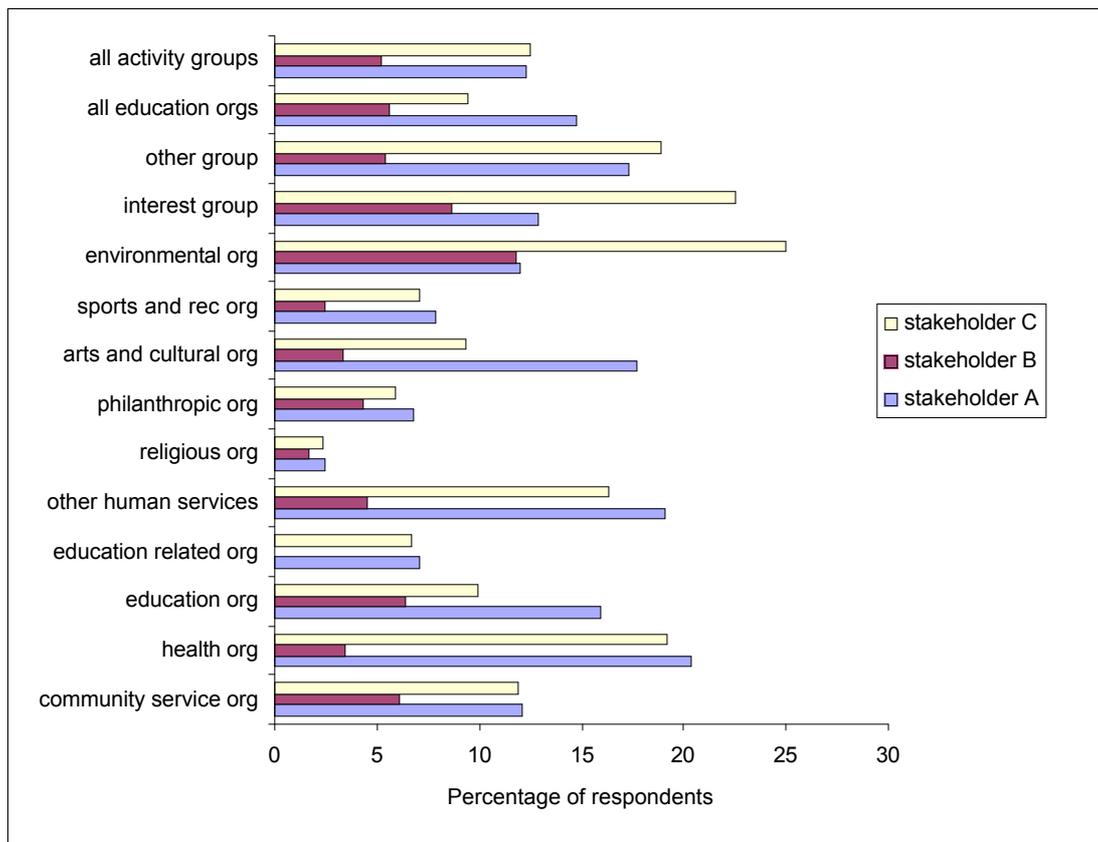
Another cause of tension some respondents reported was a lack of understanding of the role/duties of a Board of directors. These respondents reported some conflict between the self-interest of the director (for example, wanting to promote their personal profile among members in a trade association) and the company's interest.

#### 6.5. Significant differences - principal activity

It was assumed that the issues raised in the discussion under Heading 6.3 would not be as contentious for all types of organisations. We might assume, for example, that most Sport and Recreation organisations would not feel the same pressure to balance business objectives and NFP objectives, because the two are not in conflict in the context of an organisation that operates primarily to provide a service to its members. This assumption was borne out by the statistics, as seen in Figure 10.

Perhaps predictably, Health organisations, Other Human Services and Environmental organisations experience the highest level of tension with stakeholders, or between stakeholders. Religious organisations reported the lowest level of tension with stakeholders or between stakeholders, followed by Education, Sports and Recreation organisations. It might be assumed that for a Religious organisation (as opposed to a Community Service or Other Human Services organisation that has religious underpinnings) the aims are consistent amongst stakeholders, reducing the likelihood of conflict.

**Figure 10: Significant tension between this stakeholder and company or between this stakeholder and any other stakeholder in the company, based on principal activity**

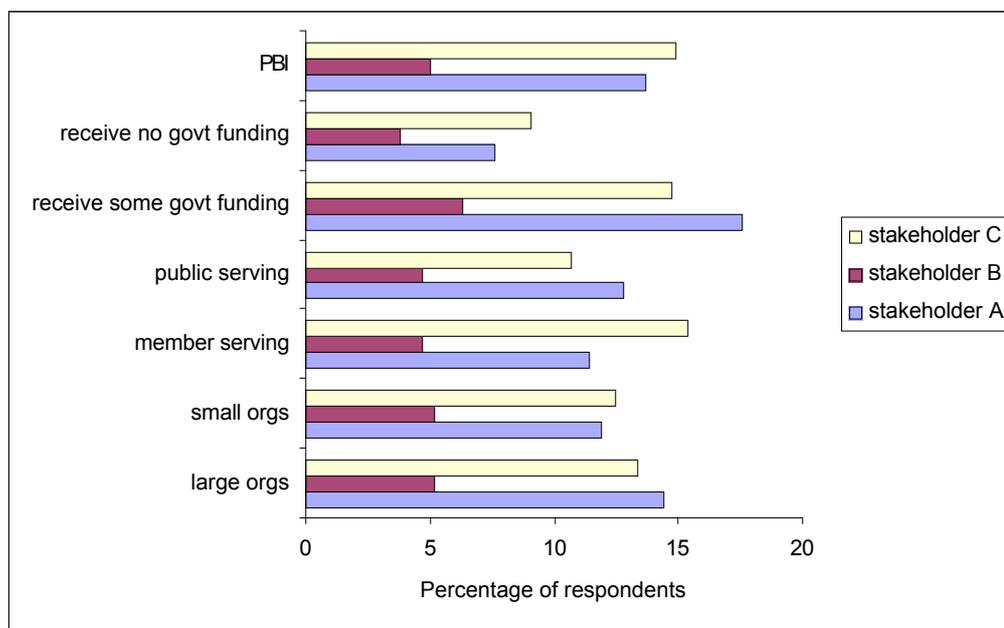


<sup>32</sup> P. Drucker, *The Practice of Management*, Pan Books, London, 1968.

### 6.6. Significant differences - other key indicators

The results (Figure 11) show that the presence of government funding increases the incidence of tension or conflict significantly.<sup>33</sup> Overall, the incidence of tension was greater for member-serving organisations than public-serving organisations.<sup>34</sup> However, in the case of Stakeholder A, the tension was greater for public-serving organisations.

Figure 11: Significant tension between this stakeholder and company or between this stakeholder and any other stakeholder in the company, based on key indicators



## 7. COMPLAINTS TO ASIC

### 7.1. Data

To complement the survey results, statistics on complaints were obtained from ASIC so as to examine the nature and extent of conflicts that result in complaints. Between July 1998 and August 2002, 4.4% of complaints to ASIC were about companies limited by guarantee, compared with 0.7 % of all other companies (that is, companies other than companies limited by guarantee).<sup>35</sup> In other words, a disproportionately high number of complaints are received about companies limited by guarantee.

According to ASIC, most of the complaints it receives about companies limited by guarantee ‘concerned internal management issues’. Most complainants raised specific concerns about the structure and conduct of meetings, or issues related to the company’s financial records.<sup>36</sup> On the basis of the information provided by ASIC, it is difficult to assess what reasons might lie behind complaints about financial records etc. It is not possible to say whether or not the data from ASIC supports conclusions drawn from the survey data that the company’s mission/purpose is the main cause of stakeholder tension. If a member of an NFP reports to ASIC regarding the manner in which their company is raising or spending funds, this is not, of itself, likely to result in any action by ASIC as the company/its directors will not have acted in breach of the *Corporations Act 2001* (Cth). Alternatively, making a complaint about improper financial reporting is likely to attract more attention from ASIC.

<sup>33</sup> The differences between the incidence of tension in organisations receiving government funding compared with those that don’t were: 16% (n= 112/63) for Stakeholder A, 11% (n= 78/47) for Stakeholder B and 5.6% (n= 59/22) for Stakeholder C.

<sup>34</sup> The differences between member-serving and public-serving organisations were: Stakeholder A, -1.4% (n= 92/84); Stakeholder B, 6.3% (n= 74/53); Stakeholder C, 4.7% (n= 45/37).

<sup>35</sup> This data was provided by ASIC. Of these complaints, 5% were investigated, 14% resulted in surveillance, and 30% were resolved by information provided/negotiation. Forty-nine per cent were analysed, assessed and recorded.

<sup>36</sup> See, n. 35.

## 7.2. Observation

The survey data bears out the notion that NFP companies are 'object driven' rather than 'profit driven'. It is not surprising, then, that tension might arise about the nature of the company's mission and whether or not the directors are fulfilling it, rather than whether there has been an adequate return on investment. The success of an 'object driven' organisation is inherently harder to measure. The survey data and the information received from ASIC support the thesis that, because NFP companies have a greater number of stakeholders than 'for-profit' companies, balancing the different needs of these stakeholders gives rise to additional and different tensions.

# 8. REMEDIES FOR MEMBERS OF NFP COMPANIES

## 8.1. Implications of previous reforms

The fact that companies limited by guarantee are largely object-driven, rather than profit-driven has been ignored in the Australian company law reform process. Changes to the *Corporations Act 2001* (Cth) in July 1998 had the effect of 'downgrading' the consequences for directors who breach the company's object clause.<sup>37</sup> Prior to the amendments, a contravention of an objects clause could be relied upon in s 162(7):

- the prosecution of a person for an offence under the former Corporations Law (s 162(7)(c))
- an application to the court for a management banning under s 230 (former s 162(7)(d))
- an application for an oppression order (now s 246(AA) (former s 162(7)(e))
- an application for a statutory injunction under s1324 (former s 162(7)(f))
- proceedings by the company or a member against the present or former officers of the company (former s 162(7)(g))
- an application by ASIC or a member to wind up the company (former 162(7)(h).

Since these amendments, breaching an objects clause does not constitute a breach of the *Corporations Act 2001*(Cth). It can no longer be relied upon to form the basis of these actions, for example, to obtain a statutory injunction to prevent the execution of a contract that is in breach of an express object. A breach of the objects clause is now treated in the same way as any other breach of the company's constitution.

The argument underlying the amending Act was that a member could still enforce objects by bringing an action against a director for breach of the company's constitution or a breach of directors' duties. However, the legislation does not make this clear. In any case, the options open to members are procedurally quite difficult.

Consider the position of a member of a NFP organisation. Before action can be taken in the company's name, the member would need to obtain the requisite majority at a general meeting to remove the existing directors - this can itself be a difficult task. Otherwise, the member would need to bring a statutory derivative action (s 236), which requires the action to be carried out in the company's name. Even if a member succeeds in obtaining leave to bring such an action,<sup>38</sup> the court is not bound to require the company to bear the costs of the proceeding.<sup>39</sup> Alternatively, if a member were to commence a personal action in his or her own name there would be considerable personal expense and it is unclear whether a personal right arises simply from a breach of an objects clause. What member of a NFP organisation is likely to have the incentive, determination or funds to be able to take such action or to rally a sufficient number of fellow members to do so?

It is more likely that an action in the name of the company will only be taken when matters have deteriorated to the point where a liquidator or administrator is appointed. Indeed, if the member does not take action when a breach occurs, there may be other undesirable consequences for the member – for example, tax exempt status (under taxation or stamp duty laws) may be lost, or ASIC may revoke the company's licence to omit the word 'limited' from its name.<sup>40</sup>

<sup>37</sup> See S. Woodward, 'Not-for-profit companies - some implications of recent corporate law reforms', *Company and Securities Law Journal*, Vol. 17, September 1999.

<sup>38</sup> See s 237 of the *Corporations Act 2001* (Cth).

<sup>39</sup> See s 242 of the *Corporations Act 2001* (Cth).

<sup>40</sup> See S. Woodward 'Ultra Vires' over simplified - changes to company powers under the Second Simplification Bill', 1997, 15 *CSLJ* 162 at pp. 170 - 1.

## 8.2. Oppression remedy

If a member of a NFP organisation that has (at least arguably) breached its express objects or acted in breach of an express limitation on its powers, it is not clear from the wording of s 232 of the *Corporations Act 2001* (Cth) that this will be sufficient to establish an action for oppression under that provision. Certainly the possible orders the court can make are wide enough to cover any possible remedy a member of an NFP company could want.<sup>41</sup> However, we suggest that neither the criteria of 'contrary to the interests of members as a whole' (s 232(d)) nor 'oppressive to, or unfairly prejudicial to, or unfairly discriminatory against, a member' (s 232(e)) would cover the NFP objects situation. We are not aware of any relevant case law on this issue. In any event, costs are again at the court's discretion and thus, it will only be a passionate or foolhardy, but necessarily well-resourced member(s) who would bring an action on the current wording.<sup>42</sup>

## 8.3. Vexatious members

It is important to consider the other side of the coin - the vexatious member. Often members in NFP organisations feel passionately about the organisation's cause. In a member-serving organisation they may have a personal interest in an issue such as how teams are selected or which fundraising activities are carried out. The limited resources of an NFP company could be depleted quickly by the need to defend a vexatious claim.

## 8.4. Importance of members' remedies

It is necessary to provide remedies for members in an NFP organisation as an accountability mechanism so that they can ensure that the organisation continues to pursue its mission. However, a fine balance needs to be achieved. The range of accountability mechanisms are more limited in an NFP organisations than in 'for-profit' companies, particularly in large listed companies where additional mechanisms are in force.<sup>43</sup> In contrast, the financial resources of an NFP company are often limited. It is not in the public good for these limited resources to be expended defending vexatious legal actions by members. An early 'filter', based on the merits of the claim is desirable, such as the need to apply for leave under s 237 *Corporations Act 2001* (Cth)

## 8.5. Recommendations - remedies

### Reform of members' remedies

The special position of members in NFP companies should be considered further in the context of remedies. Members of NFP organisations do not have the same economic power as members of 'for-profit' companies. Nor do they have recourse to a range of shareholder remedies such as selling their shares. Thus members' ability to constrain the actions of Board members and officers of the company, or to ensure that action is taken following a breach of the constitution, is limited. In addition, one of the unique characteristics of NFP organisations is the range of stakeholders with a legitimate interest in the organisation. The public, donors, clients and volunteers all have special stakes in ensuring that the mission of the NFP organisation is pursued and that the organisation's funds are not distributed to members.

The consequences of a breach of NFP objects should be reconsidered, as their mission is what drives NFP organisations. In this regard we suggest that the following specific reforms be considered:

- All NFP companies should be required to have a 'non-distribution' clause.
- Objects clauses should be compulsory for all NFP companies (not just those holding a licence to omit the word 'limited' from their name).
- The directors should have a specific duty to ensure that the company pursues these objects.
- A breach of the objects clause should be an express ground for bringing an action under s 232 of the *Corporations Act 2001* (Cth) (the oppression remedy) and, possibly, also under s 236 (the statutory derivative action). Modification of s 232 in this way would also enable ASIC to initiate action under s 234 on the basis of a complaint by a member or other stakeholder, for example, if it were considered to be in the public interest.

<sup>41</sup> See s 233 of the *Corporations Act 2001* (Cth).

<sup>42</sup> We would like to thank Professor Elizabeth Boros, Monash University, for her insightful comments on this aspect of the Report.

<sup>43</sup> Other accountability mechanisms include stock exchange regulation, dividends/returns to members and the influence of institutional investors.

### 8.5.1. REQUIREMENT FOR OBJECTS CLAUSES AND DUTY TO PURSUE THEM

In relation to the requirement in our recommendation for including objects clauses, it is worth noting that the UK Report 'Private Action, Public Benefit' includes such a requirement for the recommended 'Community Interest Company'. It also states 'directors would be under a duty to pursue them'.<sup>44</sup>

### 8.5.2. OPPRESSIONS REMEDY

If a breach of an objects clause was an express ground for an action for oppression under s 232, this would also enable ASIC to initiate an application based on its investigations into the company's affairs (see s 234(e)). This is an important point. If the objects of an NFP company, its mission, are not being followed by the directors, and the members (who may be the same people as the directors) are for whatever reason not opposed to this course, with this new provision, it would be possible for ASIC to take action. For example, if it had received a serious complaint from a client, donor or member of the public about the organisation's operations, ASIC would act as the necessary 'filter' against vexatious or minor complaints. Bearing in mind that the organisation may continue to benefit from taxation exemptions (on income, stamp duty etc) while acting contrary to its NFP objects, there is a public policy reason for giving this enforcement option to ASIC.<sup>45</sup>

Actions under either s 232 (oppression) or s 236 (statutory derivative action) give the court power to dismiss quickly any vexatious claim and wide discretion in relation to ordering the payment of costs. While costs will always be a barrier, particularly in the NFP context (a member is not protecting an investment), the contribution of organisations such as PILCH<sup>46</sup> and community legal centres, do help in this regard.

### 8.5.3. NON-DISTRIBUTION CLAUSES

We are aware of Australian Taxation Office administrative practices that require certain types NFP organisations to have clauses in their constitution or rules that prohibit distribution to members of profits or any surplus on a winding up. Some, but not all, of the State and Territory incorporated associations' Acts have such restrictions, see Appendix 5, Comparative Table. At best there is considerable inconsistency. These clauses need to be entrenched in some way so that a majority of members cannot amend the clause. We recommend that all NFP organisations<sup>47</sup>, or at least those enjoying preferential taxation treatment, be required to have such clauses. In this regard, we note a practical example cited by Professor McGregor-Lowndes:

Another example is the distribution of nonprofit clubs and societies that have enjoyed tax exemption over the years and received government grants to establish their facilities. Clubs such as lawn bowling clubs are being disbanded. Some are able to alter their constitution to permit the remaining members on dissolution to receive any surplus funds. This has occurred in several lawn bowling clubs and appears to be entirely within the law. However, the question has to be asked, What benefit should the community investment in the way of taxation exemptions, rates rebates, concessional leases of land and government grants also receive from the surplus assets. As our population's interest changes even more rapidly, this will be a pressing issue.<sup>48</sup>

### Feedback from sector

Further, the indications we have received suggest that this recommendation will be supported the sector. Ms Woodward and Ms Marshall were invited to present a seminar about the Project on behalf of Freehills, solicitors, as part of their pro bono services. This seminar was held in Sydney on 17 June 2003 and was attended by approximately 70 people from a variety of NFP organisations, as well as some advisors to NFP organisations. After a presentation about the

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<sup>44</sup> UK Strategic Unit Report, 'Private Action, Public Benefit', n. 4, para. 5.28 and recently released draft *Companies (Audit, Investigations and Community Enterprise) Bill*, see <[http://www.dti.gov.uk/cld/companies\\_audit\\_etc\\_bill/](http://www.dti.gov.uk/cld/companies_audit_etc_bill/)>

<sup>45</sup> The authors would like to thank Professor Elizabeth Boros, Monash University, for her helpful comments on members' remedies.

<sup>46</sup> Public Law Interest Clearing House, a Victorian NFP organisation that arranges pro bono legal advice for many other NFP organisations, at <[www.pilch.org.au](http://www.pilch.org.au)>. There are similar organisations in Queensland and New South Wales.

<sup>47</sup> Consideration would have to be given to the treatment of trading organisations, for example, those operating on the cooperative model even though they are companies limited by guarantee.

<sup>48</sup> See Professor Myles McGregor-Lowndes, 'Regulatory Infrastructure for Nonprofit Organisations', Working Paper PONC97, August 2000, Queensland University of Technology, p. 19.

Project, people were divided into groups to discuss some of the preliminary recommendations. There was clear agreement from participants that the rules of a NFP organisation should include a compulsory non-distribution clause as this 'defines a not-for-profit body'.

## 8.6. Recommendation - access to dispute resolution services

### Other remedies

It is desirable that NFP organisations and their members have access to expert, low-cost alternative dispute-resolution procedures. This is a valuable role that could be undertaken by the independent NFP advisory body recommended in this Report (see Chapter 4, Regulatory Framework).

Given that the nature of tension and disputes between stakeholders in NFP organisations is often different to those experienced in 'for-profits' (see, for example, Heading 7), the need for access to low-cost alternative dispute resolution procedures such as mediation is important. It is also a practical way of increasing access and preventing limited resources being used to resolve disputes with stakeholders such as members.

## 9. CONCLUSION

The survey questions reported in this Chapter have provided new insights into the nature of this important NFP group and their stakeholders. It is hoped that this data will contribute to the ongoing debate about transparency and accountability.

Whilst some of the findings were expected, such as findings about the multiplicity of NFP stakeholders, others were less expected. More surprising findings included those where:

- Volunteers were frequently not considered to be important stakeholders by the respondents (1%), despite the fact that 86% of organisations had volunteers.
- The distinction between public-serving and member-serving organisations did not translate into a significant difference between stakeholders. Clients and members ranked at a fairly similar level to government as stakeholders for public-serving organisations.

Our findings bring into contrast significant differences in profile between Australian NFP companies limited by guarantee and 'for-profits'. NFP companies have a large range of stakeholders whose interests and needs they take into account. This can render the current Australian regulatory scheme unwieldy because it serves as a less relevant but additional layer on top of the reporting that NFP organisations make to stakeholders. One respondent's comments encapsulate these tensions:

The [Corporations] Act is written and administered in such a way as to attempt to protect the shareholder and to a limited extent creditors. The concept of stakeholders seems alien.

If the concept of stakeholders being alien to the reporting requirements under the *Corporations Act* there are wider implications than simply the *Corporations Act 2001* (Cth) failing to take into account the range of bodies to whom NFP companies report. It also points to a fundamental difference between NFP companies and 'for-profit' companies. The primary reason that NFP stakeholders and 'for-profit' stakeholders differ is because the objects or mission of the organisation differ. NFP companies are generally established with the object or mission of serving the interests of certain stakeholders, whether they are the members of a club or the clients of a welfare organisation. Any consideration of NFP accountability must take include an assessment of the extent to which the NFP objects or mission have been met. Only then will stakeholders' legitimate interests in NFP companies have been taken into account.

Recommendations to amend the *Corporations Act* have been made to reflect the special position of members and stakeholders in NFP companies in the context of remedies. Members of NFP organisations do not have the economic power of members of 'for-profit' companies, nor recourse to the range of shareholder remedies, such as selling their shares. The ability of members to constrain the actions of Board members and officers of the company, or to ensure that action is taken following a breach of the constitution, is limited. It is recommended that the consequence of a breach of NFP objects needs to be reconsidered so as to reflect the importance of the mission to the NFP organisation, and make recourse to remedies more accessible to NFP members and stakeholders.

## CHAPTER 8: DISCLOSURE

### *Is what you see, what you get?*

#### SUMMARY OF KEY FINDINGS IN THIS CHAPTER

- Public disclosure requirements are linked to an organisation's legal structure. The myriad of structures under which NFP organisations operate has resulted in inconsistencies and significantly disparate disclosure obligations, not based on any sound, overall public policy agenda.
- Accountability relies on relevant, accurate and up-to-date disclosure. If the NFP sector is not seen as accountable, public confidence will be jeopardised and donations put at risk.

#### Reporting to stakeholders

- Lines of accountability in the NFP sector are complex. While the overall pattern of reporting to stakeholders was split fairly equal between voluntary and mandatory reporting obligations, it did vary significantly depending on factors such as organisational size, receipt of any government funding and principal activity.
- Ninety-six per cent of respondents said that reports to at least one of their main stakeholders was made on a regular basis. However, this rate was much lower for other stakeholders, even though they were identified by the organisations themselves as important.
- The regularity of reporting also varied considerably, based on the nature of the stakeholder receiving the report. Reports to members were made by 95% of respondents, but regular reports to the general public were only made by 62% of respondents.

#### What should be disclosed?

The survey data shows a disparity between the level of disclosure the majority of respondents believe should be available to the public (namely, summary financial information) and the level of disclosure that they are required by the *Corporations Act 2001* (Cth) to make (namely, fully audited accounts):

- Only 9% thought that no information should be made available by them to the public.
- Only 39% agreed that fully audited accounts should be available to the public.
- The majority (56%) were of the opinion that summary financial information was sufficient.

In relation to public disclosure of specific items that are likely to be of interest to NFP stakeholders:

- Only 36% of respondents thought all sources of public funding should be disclosed if the total public funding exceeds \$100,000.
- Only 25% were in favour of disclosing specific financial information regarding the remuneration of directors and senior management.
- Only 25% favoured disclosure of marketing expenditure compared with fundraising receipts.

Again, there were significant differences between respondents on this issue based on factors such as the nature of their principal activity, size and whether they received any government funding.

#### RECOMMENDATIONS

##### Reform of disclosure requirements

The current disclosure obligations required by the *Corporations Act* (in particular the requirement for audited accounts by all NFP companies limited by guarantee) do not achieve the appropriate balance between legitimate public and stakeholder interest in disclosure, on the one hand, and the relative cost based on the size of the organisation, on the other. A sliding scale of disclosure requirements based on size should be developed for NFP organisations, and be tailored specifically to the needs of stakeholders. There should be a minimum disclosure standard required by all NFP organisations, regardless of size, and this should include:

- Summary or concise financial statement, based on an NFP specific accounting standard.
- A description of activities carried out, and how they meet the objects of the organisation.
- Disclosure of whether or not directors have received remuneration.

For larger organisations, further information should be supplied. This could include:

- audited accounts
- disclosure of the amount (and possibly sources) of public funding.

Small organisations might be defined as organisations whose annual income or total annual expenditure is less than \$100,000. However, more consideration needs to be given to the criteria for determining size. ASIC, or a certain percentage of members, should have the residual power to require any organisation to be audited.

### Introduce a NFP-specific Accounting Standard

The 1995 Industry Commission's recommendation that the Australian Accounting Standards Board and Public Sector Accounting Standards Board develop suitable accounting standards for NFP organisations, should be implemented. Consideration should be given to elements from which it would be appropriate to exempt small organisations.

### Review overall NFP disclosure obligations

The survey data demonstrates that a review of the overall reporting obligations for NFP organisations is required. The data shows that current disclosure requirements:

- are not well tailored to the needs of the NFP sector and its stakeholders
- entail considerable duplication
- have an overall load that is too onerous for most small NFP organisations.

The current reporting requirements for fundraising are State-based, irregular and often duplicate the taxation and corporations law requirements. This duplication places an unnecessary administrative burden on NFP organisations, which often rely on volunteer labour. The reporting obligations under various Acts- including the *Corporations Act* and various State Fundraising and Collection Acts - should be unified. Multiple filings should be avoided and low-cost, online searching facilities should be available so as to maximise transparency. It is desirable that the reporting obligations should, as much as possible, constitute a 'one-stop' report that would satisfy the needs of various bodies.

A review of NFP disclosure requirements should include consultation with the NFP sector and their stakeholders. The review will also need to have regard to the sometimes competing concerns of a range of organisations such as funding bodies, the Australian Taxation Office, State departments administering the Fundraising/Collection Acts and peak accountant bodies, with a view to minimising the current duplication of disclosure obligations.

## ISSUES FOR FURTHER DELIBERATION

### Standard Information Return

- Consideration should be given to the desirability of developing a Standard Information Return, similar to the Annual Return proposed by the NZ Working Party on Registration, Reporting and Monitoring of Charities (see Appendix 4).
- Consideration should be given to whether organisations should be asked to disclose their main purposes and activities. Matters for disclosure might include the number of years the activity has been carried out, in what geographical areas, and the way those activities furthered the objects of the organisation. The Return might also include questions about how accountability to stakeholders is achieved.

### Disclosure of payments to directors

Where directors, trustees or committee members or related parties (that is, relations or associates) receive benefits of any kind (including salaries, fees, honoraria, and in-kind compensation), these should be publicly disclosed. Consideration should be given to the application of Chapter 2E of the *Corporations Act 2001* (Cth) (related party transactions), or possibly new conflict of interest type-provisions, to all NFP companies. That is, removing the existing exemption for companies limited by guarantee that hold a licence to omit the word 'limited' from their name. This would be in addition to finding the most effective way of ensuring that all NFP organisations disclose remuneration of directors and officers.

### Fundraising accounting standards

Further consideration should be given to the way revenue from fundraising, gifts, memberships, dues and association fees, and the sale of goods and services, is disclosed. This is in addition to disclosure of moneys spent on administration, advertising, promotion and the like. This matter requires further consideration by the Australian Accounting Standards Board, as comparability between organisations is a vexed issue. Consideration should be given to including an estimate of the number of volunteer hours donated to the organisation, because the donation of time and labour is an important and unique aspect of the NFP sector.

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## 1. INTRODUCTION

This Chapter is concerned with the way NFP organisations can be transparent and accountable to their stakeholders and to the public in general. It is a premise of this Chapter that transparency and accountability should underpin the disclosure obligations required by the *Corporations Act 2001* (Cth) and ideally for all NFP organisations, no matter what their legal structure. The availability of more transparent and consistent information about the NFP sector would benefit the community in a number of ways which are explored in this Chapter. It can assist donors in making informed decisions about who to support. It can also provide assistance in the development of policy. The 1995 Industry Commission Report on *Charitable Organisations in Australia* noted:

Accountability relies upon provision of up-to-date, accurate and relevant information relating to the operations and finances of organisations. Even when potential donors do not themselves seek information on individual organisations, the media may well do so. Better informed media coverage of the sector has the potential to improve community awareness and decisions.<sup>1</sup>

The Industry Commission identified the following problems with the current system of accountability by NFP organisations:

- lack of consistent data collection processes
- lack of public access to information
- lack of standardisation of financial reporting and other information.<sup>2</sup>

These are still key issues almost a decade later.

The myriad of legal structures for NFP organisations contributes significantly to these problems. This Chapter focuses on companies limited by guarantee, as the object of the survey, but also touches on incorporated associations. Aboriginal corporations and NFP organisations incorporated under Acts of Parliament are not discussed in any depth, but should also be kept in mind whilst reading the recommendations. The Industry Commission noted that many of the larger and long-established NFPs in Australia are incorporated under their own Acts of Parliament.<sup>3</sup> Indeed, at the date of publication of the Commission's report, fifteen of the 50 largest NFPs were incorporated under their own Acts of Parliament. The Industry Commission estimated that the combined income of these fifteen NFPs was more than \$542 million in 1992–93, including more than \$90 million in fundraising and donations. This is likely to be considerably higher today, following the outsourcing of service provision previously carried out by government bodies. The extent to which these organisations provide information on their finances and operations depends on the requirements of their particular Act. However, we believe that the public interest is such that there is no sensible basis for excluding those NFPs that have been, for unique historical reasons, created by Acts of Parliament, from the reporting standards recommended in this Chapter.

This Chapter reports on the survey data collected on:

- the nature of the reports, if any, given to stakeholders
- the levels of information that respondents believe should be publicly disclosed.

## 2. DIFFERENT MEANINGS OF ACCOUNTABILITY

It is important to note that there are many possible meanings for the term 'accountability'. It means different things to different people and will be interpreted differently in differing environments. One way to understand accountability is in terms of 'answerability'. Another is provided by the Canadian Auditor General who speaks of accountability 'as a process demonstrating in a transparent and proactive way how performance was attained'.<sup>4</sup>

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Note: All references in this Report to small and large organisations or companies are based on the definition of "small" and "large" (proprietary companies) as contained in s 45A of the *Corporations Act 2001* (Cth), unless detailed otherwise.

<sup>1</sup> *Charitable Organisations in Australia*, Industry Commission Report No. 45, AGPS, June 1995, p. 201.

<sup>2</sup> Industry Commission Report n. 1, p. 205.

<sup>3</sup> Industry Commission Report n. 1 p. 204, para. 8.2.4.

<sup>4</sup> Referred to in T. Flack & C. Ryan, 'Accountability of Charitable Organisations: Meanings and Mechanisms', unpublished conference paper, p. 4. 2002

Leat observes that distinguishing between different meanings of accountability highlights the way in which organisations may be accountable to different groups in different ways.<sup>5</sup> Some groups may be offered an account or explanation and others may be merely ‘taken into account’. Other groups may, however, have the right to impose sanctions on the organisation if it fails to provide an account and/or fails to comply with their expectations and demands.

Leat also calls attention to the fact that accountability not only has different meanings, it also operates at different levels or in different areas. She suggests it is worth distinguishing between:

- a. fiscal accountability - which is about good housekeeping, presenting financial accounts
- b. process accountability - which is about how things have been done
- c. programme accountability - which is about what has been achieved.

Different groups may demand or be owed accountability at different levels or in different areas. For example, the *Corporations Act 2001* (Cth) requires fiscal accountability from NFP organisations incorporated as companies limited by guarantee, but very little by way of process and program accountability.

### 3. IS DISCLOSURE IMPORTANT?

#### 3.1. Policy arguments

We should not assume that disclosure is the panacea to all problems. It will not, of itself, protect members and society from abuses by those involved in NFP organisations. Before discussing the issue of disclosure by NFP organisations further, we have outlined in Table 1 some of the policy arguments that can be made about legally mandated disclosure obligations. These arguments are then discussed in greater detail.

**Table 1: Policy considerations - disclosure by NFP organisations**

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

#### 3.2. Arguments for public disclosure

##### 3.2.1. ‘PUBLIC’ ARE A STAKEHOLDER, EVEN IN MEMBER-SERVING ORGANISATIONS

Almost all NFP organisations receive some taxation benefit, whether in the form of charitable status and tax deductibility for gifts, or income tax exemption. Ninety-one per cent of respondents stated that their income was exempt from income tax, donations to were tax deductible to 48% and 41% received some income from government sources. The receipt of taxation benefits increases the necessity to act in a transparent and responsible manner towards the public.

<sup>5</sup> D. Leat, *Managing Across Sectors: Similarities and Differences Between For-Profit and Voluntary Non-profit Organisations*, City University Business School, 1993, p. 42.

This feedback on our Summary of Preliminary Findings<sup>6</sup> from an senior employee with considerable experience in the sector, summarises the argument well:

NFP's are very privileged to enjoy tax-free status and other advantages, and have an indisputable responsibility to provide an honest, public account of this, to demonstrate that the privilege is not being abused. Whether they feel they 'need' to do this is less important than the fact that they have a duty to do so.

### 3.2.2. DONOR CONFIDENCE RELIES ON A HIGH DEGREE OF ACCOUNTABILITY

The provision of relevant and accessible information by NFP organisations to stakeholders and regulators is a significant factor in ensuring stakeholder confidence and attracting donations. There has been some controversy in recent years over the balance between the cost of administration compared with the money used in direct services. This sentiment was encapsulated in a series *The Australian* ran on the Salvation Army:

Donors deserve to know more about the finances of their preferred charities, more about how their money is spent and more about the quality of service it provides. They also need to know more about what they get for their dollar when government services are put out to tender. After all, charities gain tax breaks because they add humanity, empathy and compassion to the raw philanthropic dollar. No one begrudges the Salvos or any other charity the right to be efficient or big. But openness and assurances about the charitable nature of their mission would provide peace of mind to donors, and ensure more give willingly.<sup>7</sup>

It is particularly difficult to find credible information about performance and, in particular, anything which enables meaningful comparison between similar organisations.<sup>8</sup> This lack of information means that donors often have little more than individual reputations and self-supported claims on which to base their decision to donate. Volunteers also must have confidence in the organisation in order to donate their time. As evidence of this, the UK Strategy Unit Report reported a poll in which 73% of people said they would be more likely to give to charity if they had independent information about its performance, and 67% said there should be charity league tables.<sup>9</sup>

Any discussion of 'performance' should proceed with caution. Comparative performance information is only meaningful or useful to the extent that it is based on appropriate indicators of performance that can be applied to all organisations in the comparison. The appropriate indicators and effective methods of evaluation for NFP organisations are underdeveloped. However, this is an area of growing interest for NFP organisations and, perhaps more so, funders.<sup>10</sup> A number of funding organisations are currently working on ways of carrying out long-term evaluations of performance by organisations they have funded over past years.<sup>11</sup>

### 3.2.3. 'FOR-PROFIT'S CHARGING FOR INFORMATION ABOUT NFP'S

Society's demand for best value is rising steadily, and no exception is made for NFP organisations. Heightened expectations, not only from government, but from members, service beneficiaries and users, from donors and corporate sponsors or partners mean that easily accessible information about organisations is demanded. Currently, this demand is being met by private agencies.

Two Australian examples of such agencies include:

- a. Australian Management Corporation, whose advertising supplement in *The Age* on 3 June 2002 invited NFP organisations to register for the company's survey. They were to provide details of their financial position and income levels to the company to ensure they were 'open and transparent to the public that supports them'. Of the 1000 organisations approached in Victoria, 130 had 'already accepted' (including several well-known organisations).

<sup>6</sup> Distributed in March 2003, at <<http://cclsr.law.unimelb.edu.au/activities/not-for-profit/>>.

<sup>7</sup> 'Australia: The business of being charitable - Inside the Salvation Army', *The Australian*, Dossier, 23 June 2001.

<sup>8</sup> The same was found of the NFP sector in the UK: 'Private Action, Public Benefit: A Review of Charities and the Wider Not-For-Profit Sector', UK Strategy Unit Report, September 2002, p. 61, 6.3.

<sup>9</sup> Media Trust, Charity Performance Survey, UK Strategy Unit Report, 2001, n. 8, p. 61. See also discussion of problems with comparative tables, Headings 5.9.3 and 5.12.3.

<sup>10</sup> The way to measure the performance of donees was one of the main themes at the 2003 Philanthropy Australia Conference, 'Nothing Ventured, Nothing Gained: Venture Philanthropy for the Common Good', Sydney, March 2003.

<sup>11</sup> For example, the Victorian Women's Trust is currently developing new long-term evaluation methods, at <<http://www.vwt.org.au/>>.

- b. Walsh Consultants Pty Limited operate under the business name of 'Givewell'. Their website at <<http://www.givewell.com.au>> states: 'Givewell was formed in 1997 to play a key role in fostering a better culture of giving in Australia. We do this by conducting research on charities and generating ideas on better ways to give. We also believe that more informed and generous giving will lead to a more accountable, efficient and effective charitable sector.' NFP organisations are encouraged to register with them (free) and subscribers (for example, grant makers) pay to subscribe to their service.

There are also numerous examples of similar international initiatives. *ACCESS Reporting*, for example, is an initiative of the Aga Khan Foundation, together with other non-government organisations, that aims to be the world's first global reporting standard for NFP, public-benefit organisations seeking social investment. Another well-known leader in the area is the *Global Reporting Initiative*,<sup>12</sup> which promotes guidelines for sustainability reporting by corporations.

### 3.2.4. STANDARDISATION OF DISCLOSURE

NFPs are currently required to report to their members, and our data shows that the majority also provide reports to a range of other stakeholders. In addition, NFPs must lodge annual returns with the relevant regulator (ASIC for companies limited by guarantee, State and Territory registrars for incorporated associations) and comply with the disclosure requirements under fundraising, collection and taxation legislation.

However, there is no standardisation of reports or accounting standards that allows potential or recurrent donors, members or other stakeholders to easily compare similar NFP organisations. Subject to the important cautions given under Headings 5.9.3 and 5.12.3, this information would also be useful to the NFP organisations themselves, as they examine their management practices and benchmark against other NFPs. Standardised reports would assist policy makers to examine where money has been spent and what kinds of programs have been run. This would help them track the kinds of overall effects these programs have had. It would be a useful addition to the current data that is available to (and from) the Australian Bureau of Statistics. It would be an important first step in any longitudinal study of the effectiveness of the programs of NFP's.

### Industry Commission Report 1995

The Industry Commission on Charitable Organisations recommended the development of sector-specific accounting standards for Community Social Welfare Organisations (CSWOs).<sup>13</sup> In addition to the reasons just discussed, the Commission proposed this standardisation with the express purpose of reducing the costs to CSWOs of preparing reports for different funding bodies in different ways. Government bodies would then be in a position to rely on this standard for general financial reporting purposes rather than the ad hoc approach which dominates financial accountability requirements today.<sup>14</sup> The Charity Definition Enquiry likewise recommended 'a clear and consistent accountability framework...of reporting requirements that would meet the needs of all relevant government agencies.'<sup>15</sup>

### Recent studies

More recently, Chartered Accountants of Australia released a *Review of Not-for-Profit Financial and Annual Reporting* that concluded that NFPs would benefit from the development of a financial reporting framework that meets their specific requirements.<sup>16</sup>

We applaud the work being undertaken by researchers in the 'Nonprofit Accounts Project' at the Centre of Philanthropy and Nonprofit Studies, Queensland University of Technology.<sup>17</sup> The purpose of this project is to develop a common approach to the capture and external reporting of

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<sup>12</sup> At <[www.globalreporting.org](http://www.globalreporting.org)>.

<sup>13</sup> CSWO is the term the Industry Commission chose to call the vast array of organisations in the sector. This was in preference to the term 'Charitable Organisation' which, while relevant to tax law, has little applicability outside this area. As many of the organisations themselves pointed out, it has outdated connotations, see Industry Commission Report, n. 1.

<sup>14</sup> Industry Commission Report, n. 1 Recommendation 8.2, p. 214.

<sup>15</sup> *Report of the Inquiry into the Definition of Charities and Related Organisations*, 2001, Charity Definition Inquiry, at <<http://www.cdi.gov.au>>, p. 293.

<sup>16</sup> *Review of Not-for-Profit Financial and Annual Reporting*, Chartered Accountants, May 2003, at <<http://www.icaa.org.au/services/index.cfm?id=A105977944>>, p. 20.

<sup>17</sup> This project is being conducted by a team of researchers headed by Emeritus Professor Lew Edwards. See <<http://cpns.bus.qut.edu.au>>.

accounting information by NFP organisations. A recent report about the project highlights the extent of the problem in Queensland, and, quite probably, throughout Australia:

The first step in the project was to create a ‘map’ of the various financial reporting accountabilities faced by Queensland nonprofit organisations...the findings confirm the anecdotal evidence of multiple and irreconcilable differences in the reporting requirements. For example, there are:

- 113 different line descriptions that related to direct labour costs;
- 129 different revenue line items; and
- 836 different expense line items.<sup>18</sup>

### 3.3. Arguments against public disclosure

#### 3.3.1. ‘FREEDOM OF ASSOCIATION’

It is a fundamental principle of a pluralist, democratic society that individuals should be free to join together in pursuit of lawful purposes with minimal interference from the state. In practical terms, this means that care should be taken to avoid introducing measures which increase bureaucracy and discourage people from forming associations.<sup>19</sup>

NFP bodies are independently governed. This enables them to respond directly to the needs of a particular local community or interest group. They can choose to work with government or not, and to advocate changes in policy. Not all NFP organisations are public in nature and many are set up exclusively to serve members. It is important that this independence is respected. It is particularly important that public benefit is not defined according to political interests.<sup>20</sup>

#### 3.3.2. TIME AND EXPENSE

The need to provide information should be balanced against the costs to organisations. An excessive regulatory burden can draw important resources away from the primary objects of organisations. The enforcement costs for government should be also not be too onerous.

Eighty-eight per cent of respondents could be said to be within the s 45A *Corporations Act 2001* (Cth) definition of small.<sup>21</sup> As a result the resources that they have to call on are not great and their income, expenditure and receipt of taxation benefits may not be high enough to warrant elevated standards of disclosure.

The sector is characterised by high levels of reliance on volunteers and low numbers of employees. The survey results showed that 86% of respondent companies had at least one volunteer and 38% had 20 or more volunteers providing assistance to the company. In contrast, only 28% of all respondents reported having more than 20 employees. Volunteers are generally not in a position to spend hours filling out forms. In fact, the requirement to do so may act as a deterrent. In addition, disclosure obligations often require specialist skills that a volunteer may not possess.

Most organisations already provide reports to grant makers and donors. Grant makers and sponsors are unlikely to reduce their reporting obligations because the NFP is making public reports, as they require information specific to their funding programs. Therefore, increasing the amount of public-reporting obligations of NFP organisations will only increase the amount of time and resources spent on filling-in forms, rather than getting on with the stated business of the NFP.

#### 3.3.3. ALWAYS SOME ‘BAD APPLES’

In balancing these competing policy arguments, it is worth noting the UK Cabinet Report comments in favour of a ‘risk-based’ approach to regulation:

Regulation should have clear objectives. It should be carefully targeted and proportionate to risk - both to the risk of abuse and also to the risk of damage to public confidence. In general, this means that regulation of small organisations, where the sums of money involved are modest, should be lighter than regulation of large organisations, which handle large sums and may also have a disproportionate impact on public confidence.<sup>22</sup>

<sup>18</sup> See *Philanthropy and Nonprofit Matters*, Edition 24, September 2003 p. 2 at <<http://cpns.bus.qut.edu.au>>.

<sup>19</sup> UK Strategy Unit Report, n. 8, p. 30, para 3.5.

<sup>20</sup> UK Strategy Unit Report, n. 1, p. 30, para 3.6.

<sup>21</sup> See Chapter 2, Profile Data, for discussion of data on organisational size.

<sup>22</sup> UK Strategy Unit Report, n. 8, p. 30, para 3.10.

### 3.3.4. BETTER TO RELY ON GRANT MAKERS

The often unquantifiable nature of NFP objectives makes standardised reporting difficult. Grant makers and sponsors may be in a better position to require reports and monitor NFP bodies because they can check the progress of the target body against the set objectives of the funding program. Relying on grant makers and sponsors to monitor NFP operations is consistent with the principal of pluralism and freedom from excessive government interference that underpins liberal democracy.

Given that the majority of NFP organisations surveyed (56%) say that their primary role is to serve their members, it should be left to individuals to decide which organisations they will be members of, volunteer for, and sponsor. It follows that it should be up to the same stakeholders to determine what level of transparency they require. It may be that the stakeholders believe that their influence over the organisation via other means (Board membership, etc.) is a more important method of accountability than the ability to examine public reports.

### 3.4. Conclusion

Disclosure is the first step in accountability. Without information, members and other stakeholders are unable, when necessary, to consider action to constrain the Board or influence the direction of the organisation generally. The range of stakeholders, and the different reasons they might have for demanding accountability were discussed in the Chapter 7, Stakeholders. One particularly important reason is that many NFP organisations are public bodies that rely on fundraising to run their programs. Insufficient disclosure can jeopardise public confidence.

We believe there is an overwhelming case in favour of some disclosure by all incorporated NFP organisations, even those that are entirely member-serving and those incorporated by special Acts of Parliament. However, the nature of the disclosure, and to whom it should be made, are more vexed issues. In this regard, the issues of time and expense relative to organisational size and the extent of concessional taxation treatment need to be weighed carefully.

At present there is no clear or logical link between an organisation's size and taxation treatment on one hand, and the level of public disclosure (if any) on the other. As a stark highlight of this point, we note a recent statement by the Australian Taxation Office:

There are 700,000 non-profit organisations, but only 170,000 of them are in the tax system - 94% of these are companies, and the remainder trusts. Combined annual turnover of non-profit organisations in Australia exceeds \$27 billion. The 30,000 largest nonprofit organisations employ 8% of Australia's workforce. So while these organisations pay less than \$1 billion in tax, their role is significant because they collect around \$5 billion of tax paid by their employees, representing around 5% of total PAYG withholding.<sup>23</sup>

## 4. REPORTS TO STAKEHOLDERS

### 4.1. Survey question

6.1.2 Does the company provide any regular report to this stakeholder?

- yes
- no

*Number of respondents = Stakeholder A – 1543; Stakeholder B – 1000; Stakeholder C - 690*

6.1.3 If 'yes', is it as a result of a mandatory obligation or does the company provide it voluntarily?

- voluntary
- mandatory

*Number of respondents = Stakeholder A - 1429; Stakeholder B - 804; Stakeholder C - 519*

These questions were repeated for each stakeholder (A, B and C).

<sup>23</sup> See ATO Compliance Program 2003 - 4 available at <<http://www.ato.gov.au/>>.

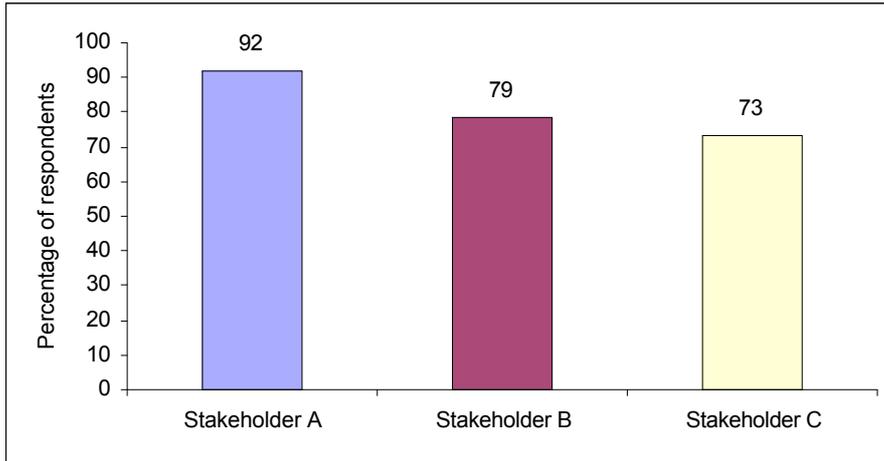
## 4.2. Is the report made on a regular basis?

### 4.2.1. SURVEY RESULTS

Figure 1 shows that reporting by NFP companies to stakeholders is regular, with 92% of respondents making a regular report to Stakeholder A, 79% of respondents making a regular report to Stakeholder B, and 73% of respondents making a regular report to Stakeholder C.

In order to establish how regularly the reports were made overall, the proportion of respondents who said that at least one stakeholder received a report was generated. Ninety-six per cent of respondents said that at least one stakeholder received a report on a regular basis.

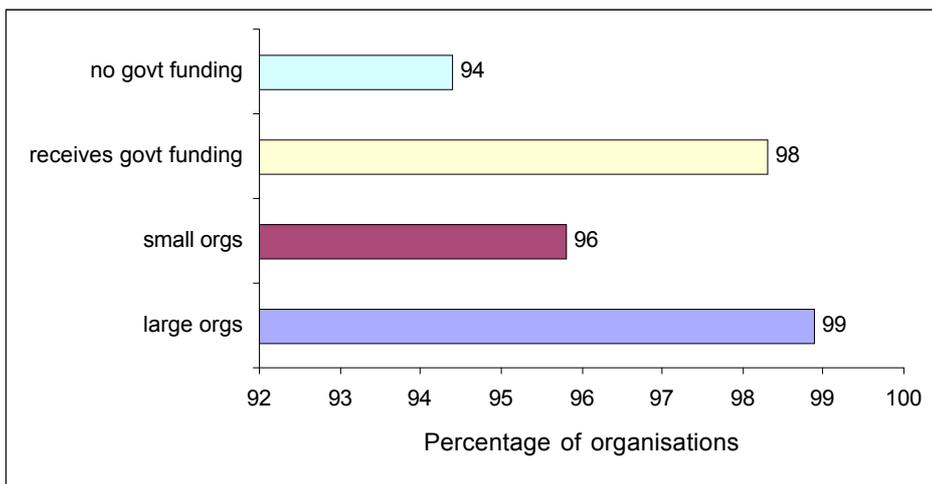
**Figure 1: Percentage of respondents making a regular report to each stakeholder**



### 4.2.2. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

There were very few significant differences between respondents based on principal activity. Figure 2 shows that large organisations made reports more regularly than small ones (99% vs 96%).

**Figure 2: At least one stakeholder received a report, based on key indicators**



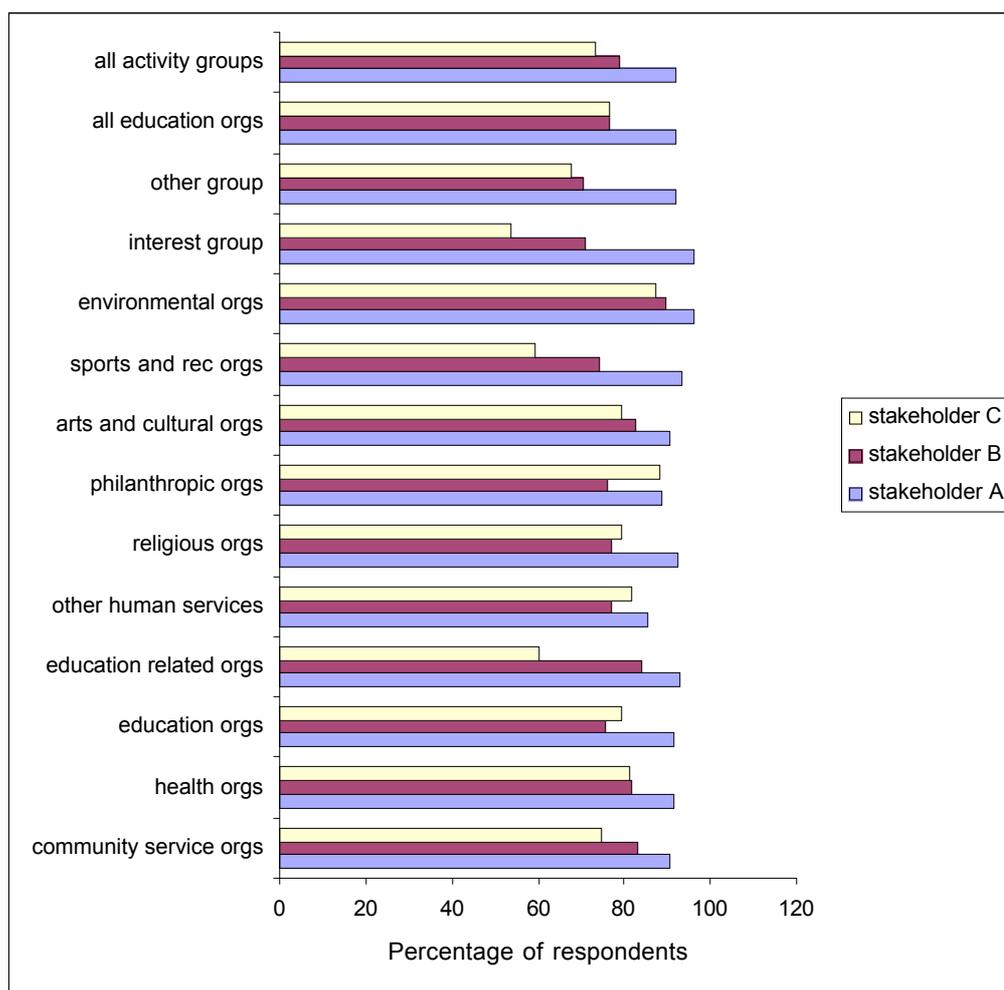
An interesting difference between respondents was that between organisations with a 'large Board' (9 directors or more) and those with a 'small Board' (8 directors or less). Those with 'large' Boards were more likely to provide a regular report to at least one stakeholder - 98% vs 95%.

4.2.3. DIFFERENCES IN REPORTS TO STAKEHOLDER A, B AND C

Figure 3 shows the breakdown in regular reports provided to stakeholders A, B, and C based on principal activity. It shows that reports are almost always provided to the most important stakeholder (typically Stakeholder A was ranked as the most important stakeholder). This contrasts with the provision of reports on a mandatory basis (reported under Heading 4.3).

The data also shows some interesting variations with regards to reports to the second and third most important stakeholders (stakeholders B and C). Whilst some organisations provide regular reports to all their stakeholders, other organisations are much less likely to provide regular reports to their second and third most important stakeholders. For example, 96% of Interest Group organisations provide regular reports to their most important stakeholder, but only 53% said that they provide regular reports to Stakeholder C. In contrast, Environmental organisations are far more consistent in their provision of reports – 96% percent provide regular reports to stakeholder A; 90% provide regular reports to stakeholder B; and 88% provide regular reports to stakeholder C.

Figure 3: Regular reporting to stakeholder A, B, and C, based on principal activity

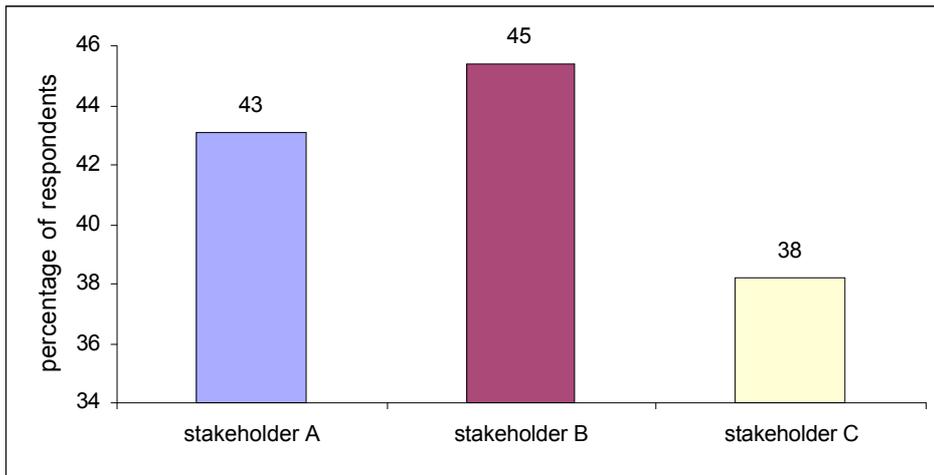


4.3. Is the report made on a mandatory or voluntary basis?

4.3.1. SURVEY RESULTS

Figure 4 shows that fewer than half of reports by NFP companies to stakeholders A, B and C are made due to a mandatory obligation.

Figure 4: Report to stakeholders on mandatory basis



To establish what proportion of the reports were made on a mandatory basis overall, the proportion of respondents who said that at least one stakeholder received a report was generated. Fifty-eight per cent of respondents said that at least one stakeholder received a report due to a mandatory obligation.

4.3.2. SIGNIFICANT DIFFERENCES BETWEEN RESPONDENTS

Figure 5 shows that large organisations are more likely than small organisations to have a mandatory obligation to provide a report. There was a 15% difference between large organisations and small organisations that provided at least one stakeholder with a mandatory report.

Interestingly, the difference between public-serving and member-serving organisations is not particularly significant (62% vs 56%). However, there is also a strong correlation between the receipt of government funding and the likelihood of a mandatory obligation to provide a report. Seventy per cent of organisations receiving government funding have a mandatory obligation to provide a report to at least one stakeholder compared with the overall figure of 58%.

Figure 5: At least one stakeholder receives a report as result of a mandatory obligation, based on key indicators

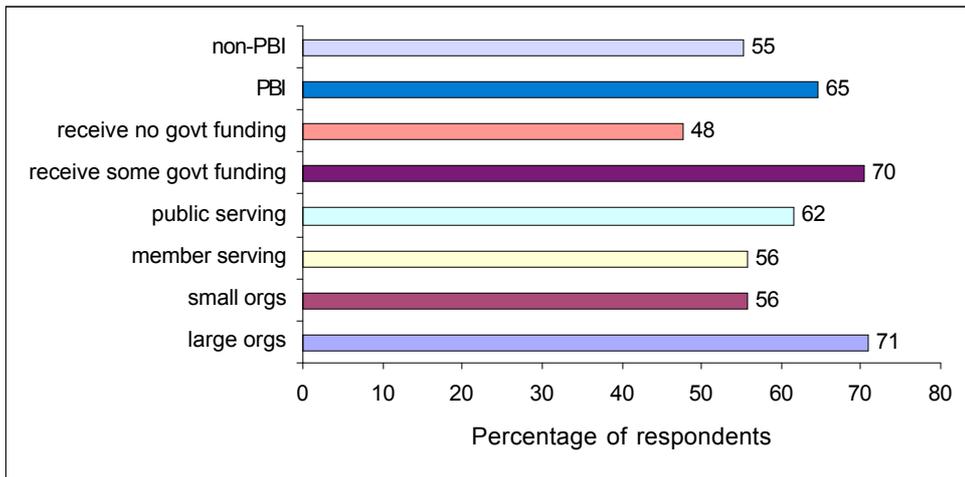
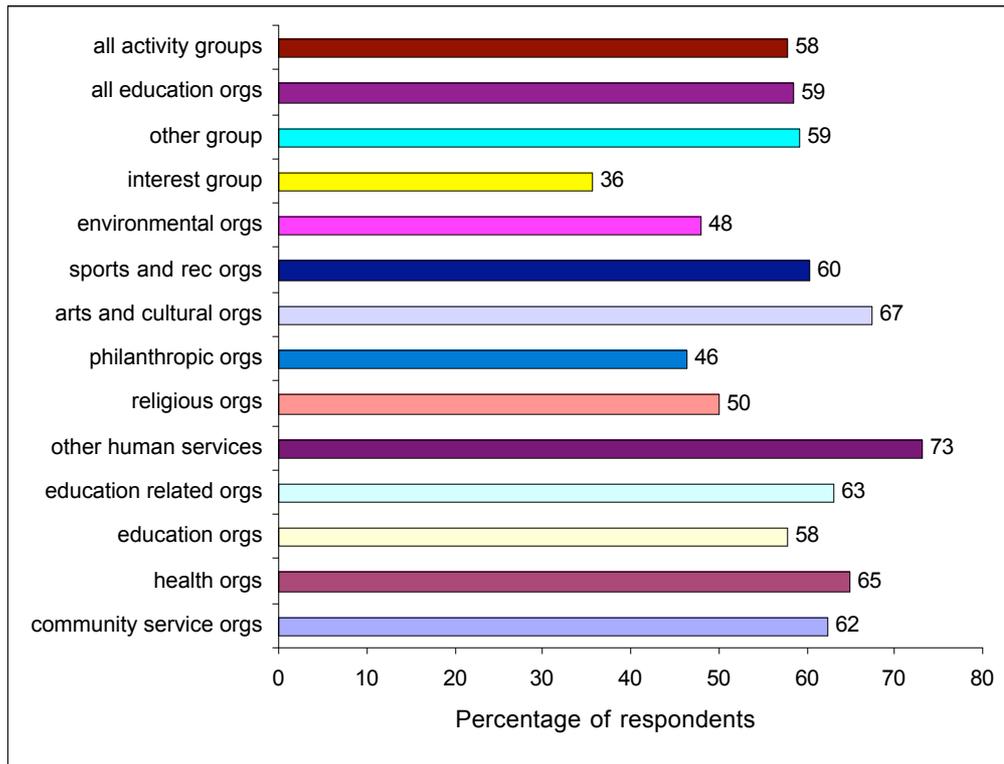


Figure 6 shows that Other Human Services organisations have the highest level of mandatory reporting (73% have a mandatory obligation to provide a report to at least one stakeholder), followed by Arts and Cultural organisations (67%). This may be linked to the strong correlation between the receipt of government funding and the likelihood of a mandatory obligation to provide a report. (Other Human Services organisations receive around 48% of their income from government sources on average, and Arts and Cultural Organisations receive around 30% of their income on average from government sources.) Interest Group organisations are the least likely to have a mandatory obligation to provide a report (36% vs 50% overall).

Figure 6: At least one stakeholder receives a report as result of a mandatory obligation, based on principal activity



#### 4.3.3. MANDATORY OR REGULAR REPORTS - DIFFERENT TYPES OF STAKEHOLDERS

To examine the nature of the reporting to different types of stakeholders, the data on reporting was cross-tabulated with the main categories of stakeholders (as coded under question 6.1.1, see Chapter 7, Stakeholders). For those respondents who named that type of stakeholder as one of their three main stakeholders, Table 2 shows those providing that stakeholder with a regular report, and whether the report was made on a mandatory, voluntary or 'mixed' basis (that is, they ticked both voluntary and mandatory options). For example, a respondent might have said that 'members' were one of their three main stakeholders, and then answered 'yes' to the question 'does the company provide a regular report to this stakeholder?' and 'yes' to it being provided on a 'voluntary' basis.

The results show a considerable variation in the regularity of reports, depending on the nature of the stakeholder. Members were most often named as a stakeholder, and receive reports most regularly (from 95% of respondent companies), but not normally in response to what the respondent<sup>24</sup> regarded as a mandatory obligation (49%). Where volunteers are considered to be a stakeholder, reports are made regularly by 91% of respondents, but this is rarely on a mandatory basis (5%).

<sup>24</sup> Even though respondents may have regarded the sending of reports to their members as 'voluntary', all public companies have a mandatory (legal) obligation to send to members a copy of company's financial report, the directors' report and the auditors report, or, alternatively, 'a concise report' - ss 314(1) -(2) *Corporations Act 2001* (Cth).

Table 2: Regular reports to specific stakeholders

Type of stakeholder	FREQUENCY OF REPORT	BASIS FOR REPORT		
	Regular report % Yes	Voluntary % Yes	Mandatory % Yes	Mandatory & voluntary % Yes
members	95	42	49	9
clients	70	76	18	6
Board	87	57	37	6
employees	77	85	11	4
volunteers	91	95	5	0
general public	62	79	18	3
related body	90	48	49	3
related sector	78	75	21	4
sponsors	92	49	48	3
government	89	16	80	4
religious	89	52	46	2

#### 4.3.4. OTHER RESEARCH

This data tells us whether respondents report to particular types of stakeholders regularly, and if such reports are provided entirely on a voluntary basis or not. The data does not tell us anything about the content or nature of the report. For example, maintaining a website may be one way of providing a regular report. In relation to the nature of the reporting, we note the findings of the recent *Review of Not-for-Profit Financial and Annual Reporting* conducted by Chartered Accountants of Australia. This study reviewed the Annual Reports and Financial Reports of 22 NFP organisations from a variety of sectors. The organisations were comparatively large by NFP standards; the revenue received by the selected organisations in 2001 ranged from \$286,000 to \$165,275,000. That review found that 19 of the 22 financial reports examined were prepared as 'general purpose financial reports'.<sup>25</sup> The remaining 3 were 'special purpose financial reports'.<sup>26</sup> Of the 14 NFP organisations reviewed that were companies limited by guarantee, only 3 companies

<sup>25</sup> According to the Report, a 'general purpose financial report' is a financial report intended to meet the information needs common to users who are unable to command the preparation of reports tailored so as to satisfy, specifically, all of their information needs (as above, n. 16, p.17).

<sup>26</sup> Only 'non-reporting entities' have the option of preparing 'special purposes financial reports' in compliance with the Accounting Standards and Urgent Issues Group Consensus Views. The Statement of Accounting Concepts SAC1, provides guidance as to classification as a 'reporting entity' or 'non-reporting entity'. The Chartered Accountants of Australia Report found that the 'special purpose financial report' was not a useful form for NFP organisations (n. 16 p.18).

prepared concise financial statements for their members and other stakeholders.<sup>27</sup> In summary, the report found that the annual reports and financial statements prepared by the organisations reviewed were, although in compliance with the law, not adequate to the specific needs of their stakeholders. The report concluded that for the purposes of reporting to stakeholders:

NFP organisations would benefit from the development of a financial reporting framework that meets their specific requirements. This framework could be based on the requirements of the Concise Financial Reporting provisions of the Corporations Law and Accounting Standard AASB 1039, Concise Financial Reports.<sup>28</sup>

#### 4.3.5. OBSERVATION

In light of the limited resources available to NFP organisations, it is unlikely that a large proportion would be in a position to prepare significantly different reports for different users. Therefore, the disclosure requirements of the *Corporations Act 2001* (Cth), together with the accounting standards that support that law, should facilitate accountability tailored to stakeholder needs. With the aim of facilitating further consideration by NFP organisations of the ways in which they involve and are accountable to stakeholders, it may be desirable to ask NFP organisations to disclose:

- who they see as their main stakeholders
- how they ensure accountability to them
- how they listen to and act on their views.<sup>29</sup>

## 5. WHAT INFORMATION SHOULD BE PUBLICLY DISCLOSED?

### 5.1. Survey question

14.1 What information (if any) do you believe should be available to the public about your organisation?

- no information

OR (tick one or more box)

- name and registered office
- summary financial information
- fully audited accounts
- if total public funding is over \$100,000, disclosure of all sources of public funding
- copy of constitution
- description of activities
- specific financial information regarding remuneration of directors and senior management
- attendance of directors at Board meetings
- marketing expenditure compared with fundraising receipts
- other (please specify).....

*Number of respondents = 1491, with varying numbers of respondents selecting the different options*

<sup>27</sup> Under part 2M, s 314(1) - (2) of the *Corporations Act 2001* (Cth) public companies may provide 'concise financial statements' to members.

<sup>28</sup> As above n. 16, p. 20.

<sup>29</sup> This proposal is taken from the 'Example of a Standard Information Return, UK Strategy Unit Report, n. 8, p. 63 and a copy is contained in Appendix 4 to this Report.

## 5.2. Overall survey results

Table 3: Respondents' view on what information should be available to the public

<i>Type of Information</i>	<i>% of respondents who selected (in descending order of prevalence)</i>
name and registered office	98
description of activities	89
copy of company constitution	60
summary financial information	56
fully audited accounts	39
attendance of directors at Board meetings	37
if total public funding over \$100,000 disclosure of all sources of public funding	36
specific financial information on remuneration of directors and senior management	25
marketing expenditure compared with fundraising receipts	24
no information	9
other	8

The survey data shows a disparity between the level of disclosure that the majority of respondents believe should be available to the public (namely, summary financial information) and the level of disclosure that they are required by the *Corporations Act* to make (namely, fully audited accounts):

- Nine per cent of respondents thought that no information should be made available by them to the public.
- Only 39% agreed that fully audited accounts should be available to the public.
- The majority (56%) were of the opinion that summary financial information was sufficient.

In relation to public disclosure of specific items that are likely to be of interested to NFP stakeholders:

- Only 36% of respondents thought all sources of public funding should be disclosed if the total public funding exceeds \$100,000.
- Only 25% were in favour of disclosing specific financial information regarding the remuneration of directors and senior management.
- Only 25% favoured disclosing marketing expenditure compared with fundraising receipts.

### 5.2.1. FEEDBACK ON THESE FINDINGS

We received the following feedback on these findings after the release of our Summary of Preliminary Findings in March 2003. Generally, there was concern at a seemingly low degree of commitment from those working in the sector to disclosure.

From the CEO of an aged care NFP organisation with income of \$25 million:

...I am dismayed that only 39% agreed that fully audited accounts should be available. It may well be your sample, e.g., it seems to be small to medium, member-serving with no government funding.

From the Chair of a small religious NFP:

Our reporting covers mandatory requirements. Equally importantly, it seems to honour our moral & ethical obligations to our 'clients'...

Another (an experienced senior officer in the sector) put it very strongly:

[the data in Table 3] ..reveals some scandalously arrogant attitudes to disclosure, with barely half agreeing that summary financial information should be publicly available.

A NFP may not 'like' accounts being made available, but there can be no argument that they have an obligation to lodge certain information and make it available to members and to members of the public who wish to see it.

The following sections provide additional breakdowns of the results for each of the options given in survey question 14.1. In some instances, there were significant differences between the views of respondents on this issue based on such factors as the nature of their principal activity, size and whether they received any government funding. Under each of the options, observations are made about the merits of requiring such information (if any) to be disclosed. Our recommendations for reform and issues that we believe warrant further deliberation are identified at the end of this topic under Heading 9.

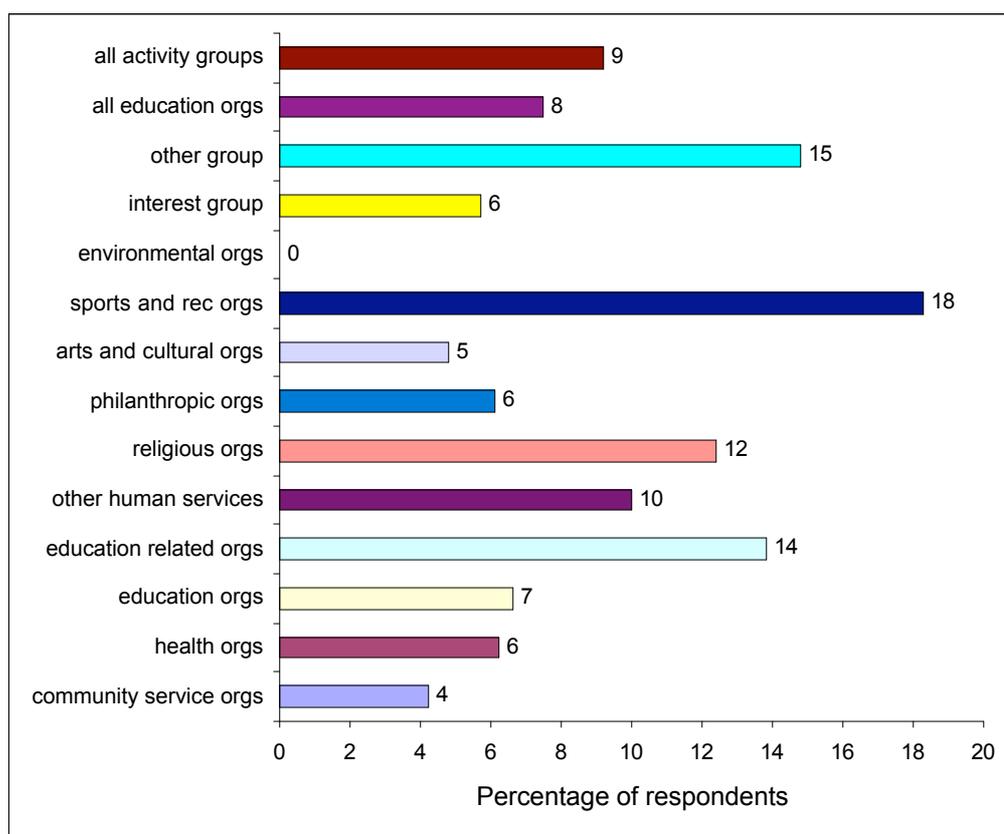
### 5.3. No information

#### 5.3.1. SURVEY RESULTS

There were a surprisingly high number of respondents who said that 'no information' should be available to the public (9.2%, n=155 organisations). There were some differences in the percentage of respondents who selected the 'no information' option based on the nature of their principal activity. No Environmental organisations said that 'no information' should be made to the public (Figure 7). This confirms the earlier observation made about the strong culture of disclosure in this activity group. Sports and Recreation organisations were most often of the opinion that no report should be made available to the public. This may be because they fall so clearly into the member-serving category.

There were also some differences between respondents based on other key factors. There was a 7% difference in opinions between member-serving organisations and public-serving organisations on this point. There was also a difference of 7% between organisations receiving some government funding and organisations receiving none. Organisations with PBI status were 7% less likely to say that 'no information' should be made available to the public than organisations with PBI status. These differences are not particularly significant.

Figure 7: No information should be available to the public, based on principal activity



### 5.3.2. OBSERVATION

Public disclosure of certain information about the identity and operation of an organisation has for centuries been an accepted legal condition of being incorporated. That is, an obligation imposed in order to gain separate legal entity status with the privileges and protections that entails for the individuals that form the organisation. The public disclosure of 'no information' is therefore not a real option, despite its selection by some of respondents.

## 5.4. Name and registered office

Currently, NFP organisations registered as companies limited by guarantee, and those registered under the various incorporated associations acts in each State and Territory, are required to provide details of their name and registered office, and these are publicly available.

### 5.4.1. SURVEY DATA

Not surprisingly, close to all respondents (98%) agreed that name and registered office should be disclosed. There was very little difference between types of organisations based on principal activity. The size of the organisation, whether public-serving or member-serving, and whether in receipt of any government funding made very little difference to the response.

## 5.5. Summary financial information

### 5.5.1. FINANCIAL INFORMATION COMPANIES CURRENTLY HAVE TO LODGE

The requirements under Part 2M.3 of the *Corporations Act 2001* (Cth) require an NFP company limited by guarantee to lodge audited financial statements (s 295, Part 2M.3 - Division 3) and a directors' report confirming that the financial statements give a 'true and fair view' and that the company is able to pay its debts when they become due and payable.<sup>30</sup> Meeting these requirements may be a considerable expense for a truly small NFP company. It is important to keep in mind if 88% of the respondents had chosen to be a proprietary limited company rather than a company limited by guarantee they would have had minimal mandated reporting obligations, as they would, on the basis of the size data they provided, have been defined as small (s 45A).<sup>31</sup> Small proprietary companies are not required to lodge financial reports unless requested by ASIC or more than 5% of members (s 298(3)).

### 5.5.2. WHAT DO OTHER TYPES OF NFP ORGANISATIONS LODGE?

A comparison of incorporated associations with companies limited by guarantee is interesting. The required information to be disclosed when lodging an application for the incorporation of an association vary greatly in different jurisdictions. So too do the annual returns to be filed by incorporated associations.<sup>32</sup> Annual returns must be lodged in all States except Western Australia. The information required as part of the annual return varies from State to State. In some States, organisations can be exempted from the requirement. For further detail, see the comparative table, Appendix 5). Audited financial reports are only required in some States and Territories, and then, only from 'prescribed associations'.

The disclosure requirements (if any) for other NFP organisations will depend on the terms of the Act that they are established under.

### 5.5.3. SURVEY DATA

The majority (56%) of all respondents were of the opinion that only 'summary financial information' about their organisation should be available to the public. Environmental organisations, Health organisations and Arts and Cultural organisations were most likely to be of the opinion that 'summary financial information' should be made available to the public (75%, 74% and 70% respectively). Interest Group organisations were the least likely (42%).

<sup>30</sup> Annual Returns were abolished for all companies as at 1 July 2003.

See <[http://www.asc.gov.au/asic/asic\\_infoco.nsf/byheadline/Corporate+Law+Economic+Reform+Program+7?openDocument#public](http://www.asc.gov.au/asic/asic_infoco.nsf/byheadline/Corporate+Law+Economic+Reform+Program+7?openDocument#public)>.

<sup>31</sup> See Chapter 2, Profile Data.

<sup>32</sup> A.S. Sievers, *Associations and Clubs Law in Australia and New Zealand*, The Federation Press, 1996.

Following the general trend throughout this Chapter, large organisations were more likely than small organisations (66% vs 54%); those with PBI status (64%) were more likely than those without; public serving were more likely than member serving (62% vs 50%), and those receiving government funding were more likely than those not receiving government funding (64% vs 49%), to think that 'summary financial information' should be available to the public.

### 5.5.4. OBSERVATION

In light of the current lodgement requirements for public companies, providing only summary financial information would be a considerable downgrading of the financial disclosure obligations for NFP organisations which are incorporated as companies limited by guarantee. Careful consideration needs to be given to the financial information that should be included or excluded, and whether smaller organisations could be exempted from completing certain sections. If the financial reports required of NFP organisations were tailored to meet the needs of NFP organisations, their members, donors and other stakeholders, then a requirement to lodge them under the *Corporations Act* ought not be too onerous. The burden on organisations would be justified by the public benefit. To this end, the proposed development of sector-specific accounting standards for Community Social Welfare Organisations (CSWOs) by the Industry Commission should be supported.<sup>33</sup> A recent report by the Chartered Accountants also similarly concluded that NFP organisations would benefit from the development of financial reporting frameworks based on the requirements of the Concise Financial Reporting provisions of the *Corporations Act* and Accounting Standard AASB 1039, Concise Financial Reports.<sup>34</sup> The Charities Commission of England and Wales recently commissioned out a similar exercise, resulting in the 'Accounting and Reporting of Charities: Statement of Recommended Practice' which was co-authored by the Accounting Standards Board.<sup>35</sup>

Feedback from an accountant who regularly advises a range of NFP organisations highlights the issue:

Should NFP's be treated as any other Public Company from a reporting point of view, or can these NFP hide behind the "Special Purpose Reporting" regime which seems to have found a place in this sector? Can NFP afford (from a \$\$ point of view) to comply with the financial reporting requirements of a normal reporting entity, or can they afford (from a governance point of view) not to?

We have made a recommendation that a NFP accounting standard be introduced, see Heading 9.

## 5.6. Fully audited accounts

### 5.6.1. CURRENT REQUIREMENTS

NFP organisations incorporated as limited guarantee companies must have their financial reports audited. In accordance with s 301 of the *Corporations Act 2001* (Cth) all companies (except small proprietary companies), 'registered schemes' and 'disclosing entities' must have the financial report for a financial year audited in accordance with Division 3 and obtain an auditor's report. The auditor's report must be sent to the members as part of the annual financial report to members (s 314).

### 5.6.2. SURVEY DATA

The overall support for this proposal was not particularly high, with only 39% believing that fully audited accounts should be available to the public. Figure 8 shows that the majority of Other Human Services organisations were supportive (55%), whereas only 22% of Interest Group organisations believed that fully audited accounts should be available to the public.

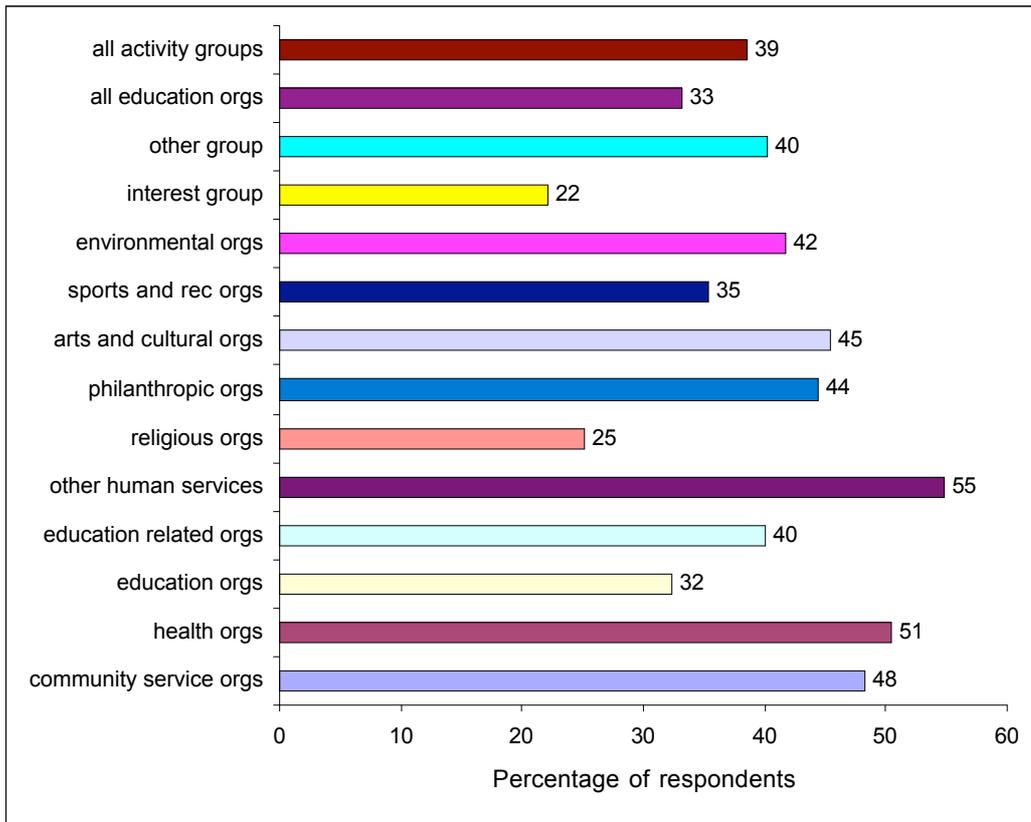
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<sup>33</sup> Industry Commission Report, n. 1, Recommendation 8.1, p. 216.

<sup>34</sup> *Review of Not-for-Profit Financial and Annual Reporting*, Chartered Accountants, May 2003, at <<http://www.icaa.org.au/services/index.cfm?id=A105977944>>, p. 20.

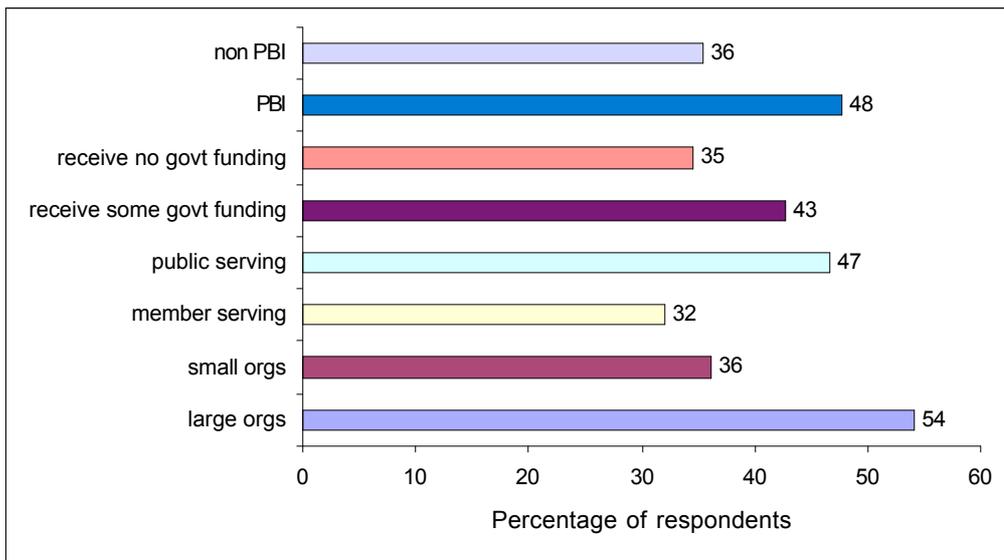
<sup>35</sup> *Accounting and Reporting by Charities: Statement of Recommended Practice*, revised 2000, UK Charities Commission, October 2000.

Figure 8: Fully audited accounts should be available to the public, based on principal activity



Further analysis (Figure 9) also showed that respondents whose companies were primarily member-serving were less likely to believe that fully audited accounts should be available to the public, than those whose company primarily serve the public (32% vs 47%). Large organisations were 18% more likely to believe that fully audited accounts should be available to the public than small organisations.

Figure 9: Fully audited accounts should be available to the public, based on key indicators



### 5.6.3. OBSERVATION

The Industry Commission recognised that smaller NFPs may face higher costs as a result of the form of incorporation and the standard accounting procedures that it proposed. It recommended requiring CSWOs to be subject to a limited scope audit or audit by an independent examiner. However, the Industry Commission was of the opinion that by creating standardised reporting requirements, the number of reports organisations are obliged to complete would be reduced. Further, the Industry Commission said that given that the costs of an audit depends on the time it takes, the cost of an audit for a smaller organisation would be lower than for a larger organisation.<sup>36</sup>

The Industry Commission recommendations for standardisation have not been implemented and comments written by respondents concerning survey question 4.2 suggest that many organisations are suffering as a result. The comments indicate that the cost of auditing is high as a proportion of the administrative costs. As quoted in Chapter 3, Legal Structure, a Sports and Recreation organisation with income of less than \$100,000 said that the audit fees were \$9300 in their last financial year. A museum with income of less than \$10,000 said that their audit fees had been over \$1200. That is, more than 10% of the museum's overall income. In 2002, the Office of Small Business estimated the average audit cost for medium-sized companies at \$25,000. There is no reason to think that these figures would be significantly different for NFP companies.<sup>37</sup>

We have made two recommendations relevant to this data:

- a. The possibility of truly small NFP organisations being exempted from the auditing requirement unless requested by ASIC or a certain percentage of members – see Heading 7.1
- b. The establishment of a NFP advisory body which could provide auditing services at a minimal or reduced cost, particularly for smaller organisations, see Chapter 4, Regulatory Framework.

## 5.7. If total public funding is over \$100,000, disclosure of all sources of public funding

### 5.7.1. SURVEY DATA

Overall, 36% of respondents thought that all sources of public funding should be disclosed if total public funding exceeds \$100,000.

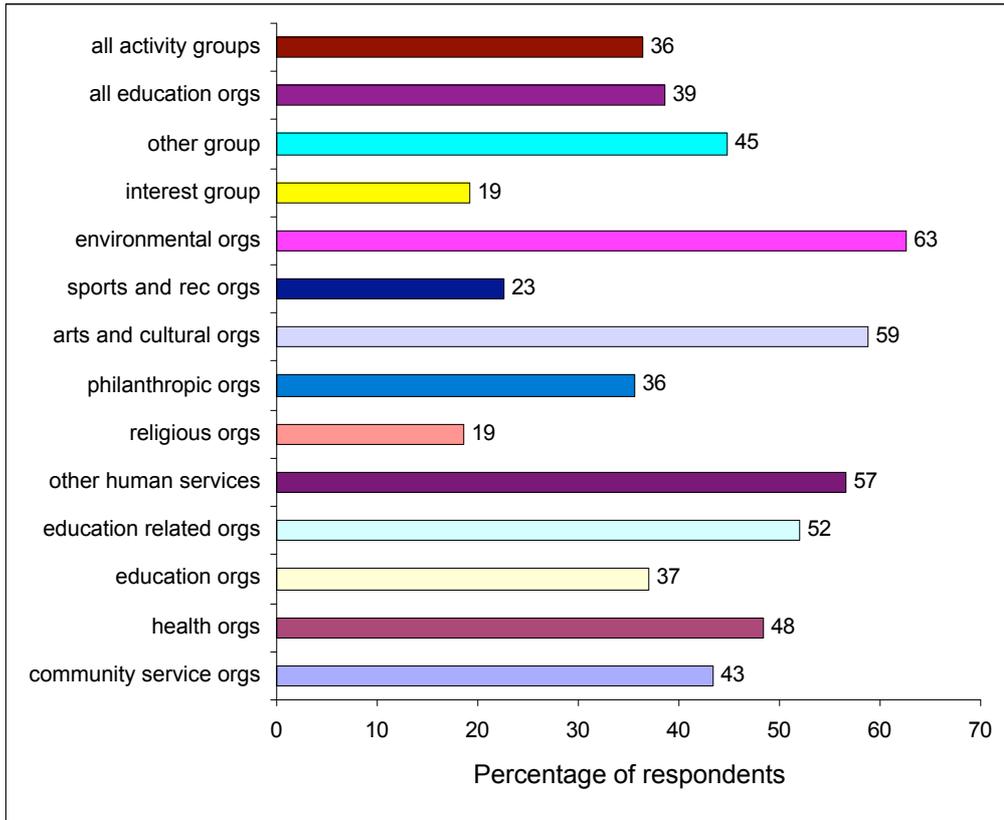
There was a large divergence of views about this point between organisations based along the lines of principal activity, see Figure 10. Only 19% of Religious organisations, 22% of Sport and Recreation organisations and 19% of Interest Group organisations said that there should be disclosure of all sources of public funding if total public funding is over \$100,000. In contrast, Environmental organisations were again most frequently in support of disclosing sources of public funding (63%), followed by Arts and Cultural (60%) and Other Human Services organisations (57%) compared with the overall rate of 36%.

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<sup>36</sup> *Charitable Organisations in Australia*, Industry Commission Report No. 45, AGPS, June 1995, p. 219.

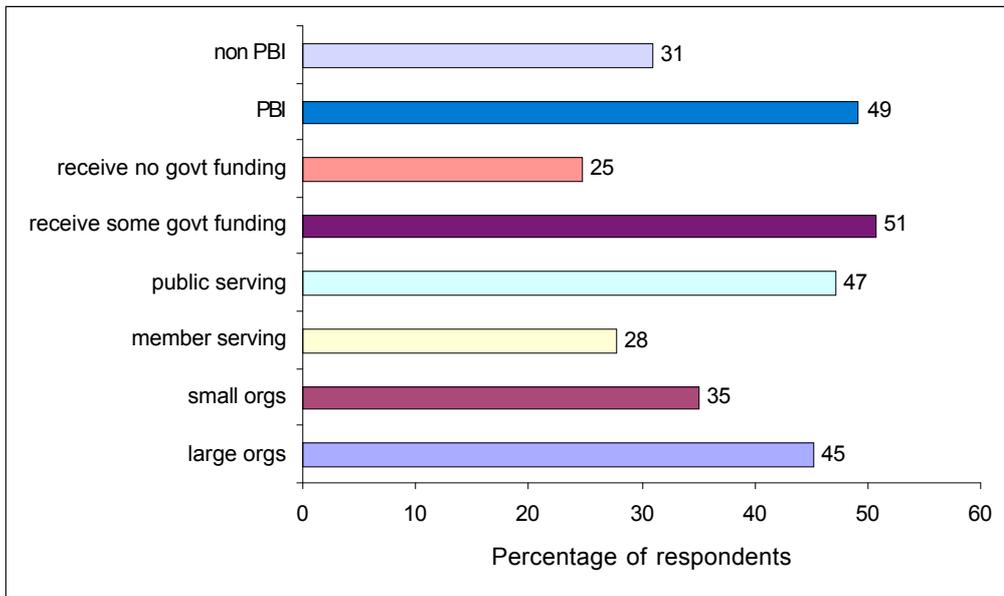
<sup>37</sup> Office of 'Small' Business, Department of Employment, Workplace Relations and 'Small' Business, *Submission to the Parliamentary Joint Statutory Committee on Corporations and Securities*, 2001, p.2. The Motor Trades Association of Australia (MTAA) which represents franchised new motor vehicle dealers, estimated the additional audit cost in excess of \$20,000: Motor Trades Association of Australia, *Submission to the Parliamentary Joint Statutory Committee on Corporations and Securities*, p. 15.

**Figure 10: All sources of public funding should be disclosed to the public if total public funding is over \$100,000, based on principal activity**



As Figure 11 demonstrates, there is a significant difference of opinion on this point between those that receive government funding and those that do not - 26%. This shows that organisations receiving government funding appreciate the considerable responsibility that government funding carries with it. There was a 10% difference between small and large organisations on this point. Organisations with PBI status were likewise more likely to support the proposed disclosure than those without: 49% vs 31%.

**Figure 11: All sources of public funding should be disclosed to the public if total public funding is over \$100,000, based on key indicators**



### 5.7.2. OBSERVATION

Companies limited by guarantee are not specifically required to disclose their sources of public funding, although, sources of funding may be covered in the financial statements as lines of income. There is no standardised method of accounting for sources of public funding. This is a good example of the fact that the *Corporations Act* (Cth) disclosure requirements were not designed with NFP organisations in mind, and do not touch on matters that donors and other stakeholders might consider to be of importance.

The requirement to disclose all sources of public funding over \$100,000 may serve the objective of reducing the regulatory burden on organisations that are too small to warrant it, but ensure that those receiving the benefits of public funding impart suitable levels of relevant information about sources of funding.

We do not have any figures on the proportion of NFP organisations receiving less than \$100,000 in 'public funding', as we did not ask respondents for a breakdown of their sources of funding. However, we do know that 30% of respondents to the survey were from organisations whose income is less than \$100,000 per annum. (We can assume that a proportion of this income came from public funding, but a proportion would also be raised from investments and trading activities.) Using this distinction, around a third of organisations would be excluded from such disclosures, whilst the greater majority of organisations (70% have income over \$100,000) would be required to disclose all sources of public funding. It may be that the cut-off figure should be higher (or lower), say, \$500,000, but nevertheless, the principle seems to be a good one.

Just how, or in what detail, organisations would disclose their sources of funding, is another question. Organisations might be asked to provide the full details of grants from government sources and registered charities. However, in order to protect the privacy of corporate and individual donors, NFP's might be asked only to provide an overall figure for these categories.

### NZ propsoals

The New Zealand Working Party on Registration, Reporting and Monitoring of Charities<sup>38</sup> recommends that organisations disclose amounts raised under the following categories:

- a. investments
- b. [New Zealand] company dividends
- c. all other investments (excluding [New Zealand] company dividends)
- d. donations from the public
- e. trading activities
- f. grants from other registered charities
- g. government contracts or grants
- h. income from members (including subscriptions)
- i. other

See Appendix 4 of this report for a copy of the sample NZ disclosure form. It would be useful to obtain the views of the sector on this disclosure form.

In Australia there is great inconsistency between the States and Territories about the disclosure of fundraising activities. A recommendation concerning fundraising is made under Heading 10.

## 5.8. Copy of constitution

### 5.8.1. SURVEY RESULTS

Overall support for the public disclosure of the constitution was 60%, with highest support from Arts and Cultural organisations (77%) and Environmental organisations (75%). The lowest support was from Religious organisations (47%) and Sport and Recreation organisations (48%). These were the only activity groups from which support for disclosure of the constitution was below 50%. The differences between other organisations were not particularly significant. Likewise, the receipt of government funding, PBI status, and the size of organisations made very little difference to respondent's views on this point.

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<sup>38</sup> Report of the Working Party on Registration, Reporting and Monitoring of Charities, 28 February 2002, Appendix 6.

5.8.2. OBSERVATION

As a general principal, it seems logical that the constitution of a NFP organisation should be publicly available. In particular, the constitution can provide:

- a potential member with information about the rights of members, and whether there are different classes of members
- a potential or current donor with information about the whether directors are paid or not paid
- enable a potential donor to determine whether its funding objectives match the NFP’s objects.

It is of particular relevance to NFP companies because:

- Those holding a licence to omit the word ‘Limited’ from their name (s.150) must have a constitution which requires the company to pursue charitable purposes only, that prohibits the company making distributions to its members and paying fees to its directors.
- Even NFP companies not holding such a name licence typically have objects clauses in their constitution. By their very nature, a NFP company should have a clause prohibiting distributions to members and stating objects and certain restrictions on powers.<sup>39</sup>

5.9. Description of activities

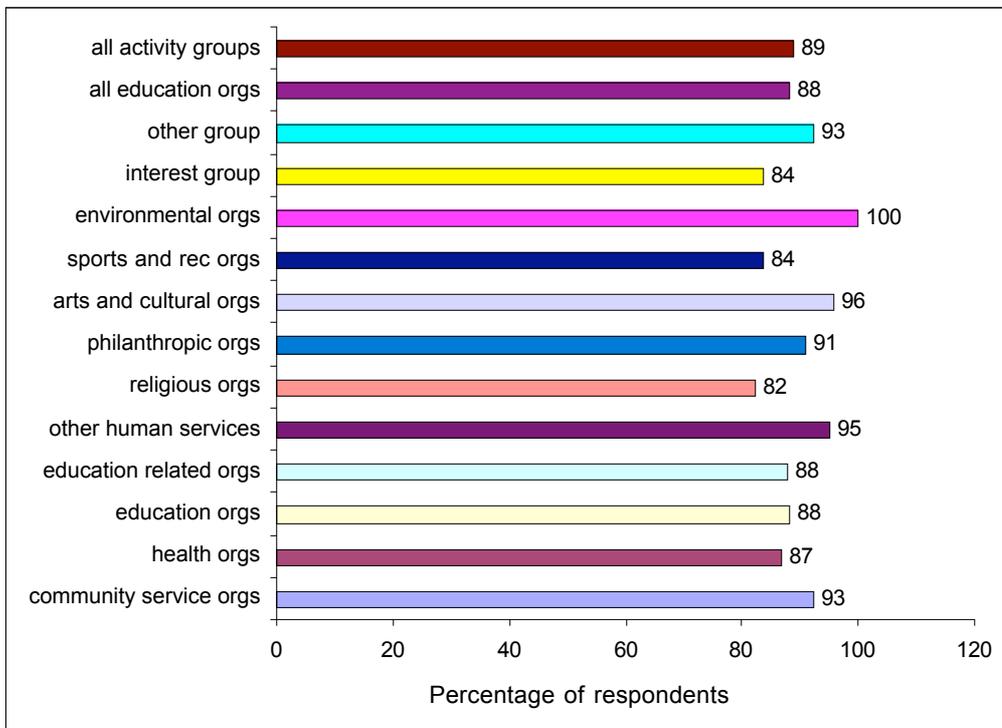
5.9.1. CURRENT LEGAL REQUIREMENTS

Companies limited by guarantee (as public companies) must lodge a description of activities with their annual Directors’ Report. Under s 299(1)(c) of the *Corporations Act 2001* (Cth) the annual Directors’ Report must include general information about the operations and activities of the company. This should include a statement about the entity’s principal activities during the year and any significant changes in the nature of those activities. Only small proprietary companies (as defined in s 45A) are excluded from providing annual Directors’ Reports (s 292), unless they are directed to do so by a vote of at least 5% of the shareholders (s 293) or by ASIC (s 294).

5.9.2. SURVEY RESULTS

Figure 12 shows very consistent support for the disclosure of a description of activities to the public amongst all activity groups, with 89% indicating support for the proposal. From these consistent results it would seem that this is not regarded as an onerous or costly obligation.

Figure 12: Description of activities should be disclosed to the public, based on principal activity



<sup>39</sup> See the recommendation on non-distribution clauses and objects clauses in constitutions of NFP companies discussed in Chapter 3, Legal Structure.

### 5.9.3. OBSERVATION

Respondents were overwhelmingly in favour of providing an account of activities in their reports. This reflects the fact that NFP organisations are largely object driven, and are therefore of the view that a report of the activities carried out - what Leat might call process and programme accountability - would be the fullest representation of the achievements of the organisation.

### UK Proposals

The 2002 UK Strategy Unit Report, *Private Action, Public Benefit* recommended that those charities with income of £1 million or more provide audited accounts detailing a range of qualitative and quantitative information about the charity.<sup>40</sup> The information would focus on the charity's impact, how it measures its performance in achieving its aims, and how it intends to improve.<sup>41</sup> The Report also recommended that as part of their report and accounts, the largest charities should complete an annual 'Standard Information Return' that would highlight how the charity sets its objectives and measures its outcomes against these, see Appendix 4 for a copy of the recommended UK 'Standard Information Return'. During the subsequent widespread consultation about the Strategy Unit's recommendations, 77% of respondents expressed clear support for the aim behind the recommendation, namely to improve the relevance and accessibility of information about charities. However, many supporters had reservations about the recommendation itself.<sup>42</sup> The main reservations were that:

- compiling the 'Standard Information Return' could be a bureaucratic burden and lead to increased administration costs
- the 'Standard Information Return' could prove a trojan horse for charity league tables, which most charities would deplore
- the diversity of charities meant that comparisons between charities, based on the information extracted from 'Standard Information Returns', could be misleading and perhaps harmful
- auditing the 'Standard Information Return' could prove difficult because of the mix of quantitative and qualitative information.

Despite the reservations voiced by some respondents to the review, the UK Government accepted the recommendation and intends to develop the format of the 'Standard Information Return', using the sample form in Appendix 4. However, the UK Government says it will work towards 'finding a means to ensuring that the information can be compiled without placing undue administrative burdens on charities.'<sup>43</sup> In 1995 the Industry Commission also expressed reservations about comparison of fundraising expenditure, see Heading 5.12.3.

### NZ proposals

The 'Annual Return' proposed by the NZ Working Party on Registration, Reporting and Monitoring of Charities includes a section for providing 'the main activities that will be carried out in order to further the objects of the entity's governing document'. The 'Annual Return' sample form provides space for four objects, and an extra space for adding any information about any additional objects and activities. All the information provided in the 'Annual Return' is then to be made publicly available.<sup>44</sup> (See Appendix 4 for a copy of the sample NZ Annual Return.)

It would be useful to obtain the views of the sector on the new NZ model.

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<sup>40</sup> UK Strategy Unit Report, n. 8, p. 79, para. 7.44. The recommendation reads: 'That all charities with income of £1m or more in any financial year should be required to have their accounts for that year professionally audited. The independent examination requirement should apply to charities with income between £10,000 and £1m. The latter threshold should be re-examined if the audit threshold for non-charitable 'small' companies changes.'

<sup>41</sup> 'Private Action, Public Benefit: A Review of Charities and the Wider Not-For-Profit Sector', UK Strategy Unit Report, September 2002, p. 62, 6.10.

<sup>42</sup> *Charities and Not-for-Profits: A Modern Legal Framework. The Government's response to 'Private Action, Public Benefit'*, Home Office, July 2003, p. 18.

<sup>43</sup> See NZ Report, n. 29, p.18.

<sup>44</sup> See NZ Report n. 29, Appendix 6.

## 5.10. Specific financial information regarding remuneration of directors and senior management

### 5.10.1. REMUNERATION - CURRENT LEGAL REQUIREMENTS

As a general rule, companies limited by guarantee are not currently required to publicly disclose the amount of any remuneration paid to (executive or non-executive) directors and senior management - s 300(11) only applies to listed companies. It should be noted, however, that:

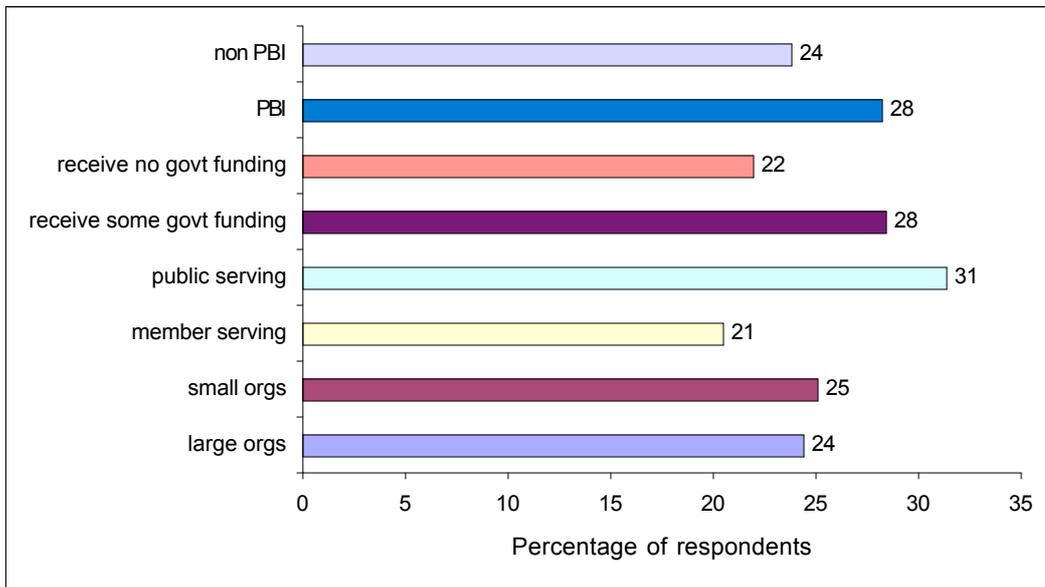
- a. s 300(1)(d) requires share options granted to directors as part of their remuneration to be disclosed in the annual Directors' Report
- b. there is a general requirement for all companies (s 202B(1)) that directors' remuneration must be disclosed if those members with 5% or more of the votes, or 100 or more members, pass a resolution requiring the disclosure
- c. companies limited by guarantee that hold a licence to omit the word 'Limited' from their name (s 150) must have a constitution that 'prohibits the company...paying fees to its directors' and that 'requires the directors to approve all other payments the company makes to directors' (for example, this later requirement means that the directors must approve the salary paid to any executive directors)<sup>45</sup>.

### 5.10.2. SURVEY DATA

The support for the proposal that 'specific financial information regarding remuneration of directors and senior management be disclosed' was not very high - only 25%.

Interestingly, as Figure 13 shows, there is very little difference between respondents based on size. There was an 11% difference between member serving and public serving organisations, and a 6.4% difference between organisations receiving government funding and those that do not.

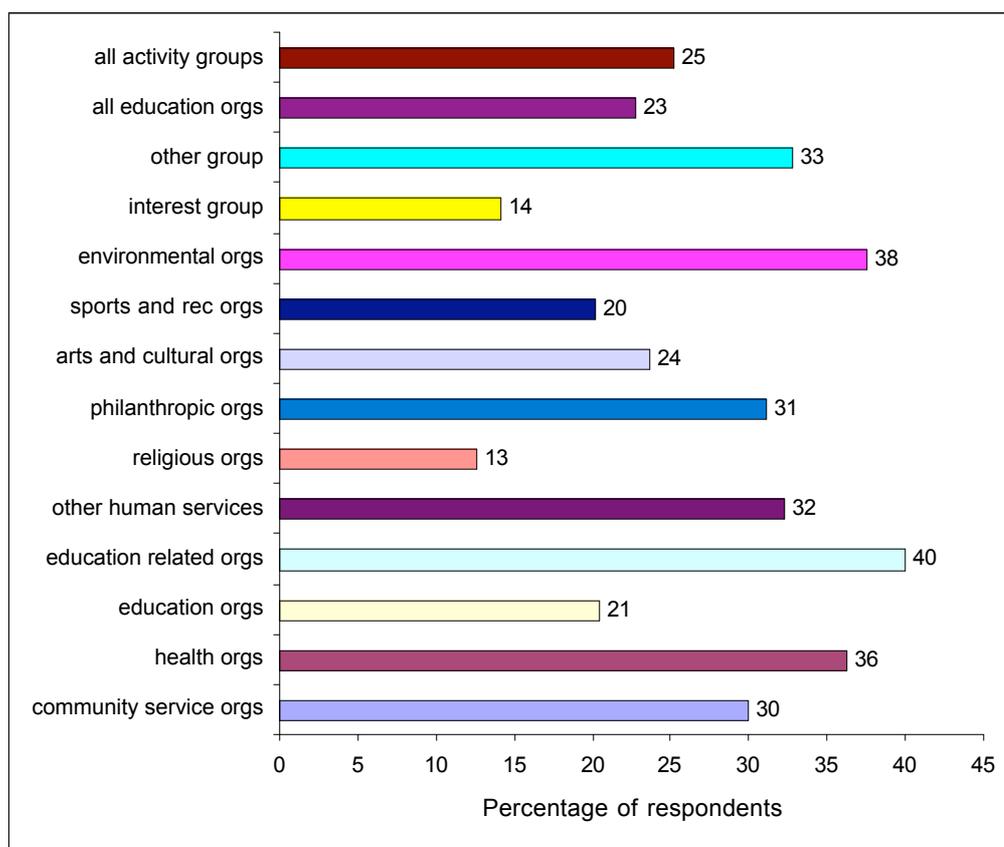
**Figure 13: Specific financial information regarding remuneration of directors and senior management should be disclosed, based on key indicators**



As Figure 14 shows, support for the proposal amongst activity groups followed the standard pattern that has emerged from the disclosure data – with the lowest support coming from Religious (13%), Sports and Recreation (20%) and Interest Group organisations (14%).

<sup>45</sup> See ss 150(1)(b) - (c) of the *Corporations Act 2001* (Cth).

Figure 14: Specific financial information regarding remuneration of directors and senior management should be disclosed to the public, based on principal activity



### 5.10.3. OBSERVATIONS

Interestingly only a quarter of respondents were in favour of the disclosure of this information even though 92% said that they did not pay their non-executive directors. It would seem, therefore, that executive directors (such as the CEOs who completed the survey) are reluctant for stakeholders (including the general public) to have information about their salary levels.

Unlike in the case of the directors of 'for-profit' companies, it is not common practice for non-executive directors of NFP organisations to receive remuneration, or other benefits. Only 8% of respondents said that directors were remunerated.<sup>46</sup> Disclosure in the case that directors are remunerated is, in our opinion, important. Stakeholders (members, donors and creditors, in particular) have obvious interests in knowing if non-executive directors are paid, and if senior management are paid higher than the normal market amount for managers of NFP organisations.<sup>47</sup>

Information about the remuneration of senior management may also be desirable. Payment of NFP CEOs in Australia and abroad has made the headlines in recent years. For example, the disclosure of Wesley Mission's \$160,000 payment of CEO Mr Langley, which he inherited largely from his predecessor, the Reverend Kevin Green, 'scandalised' the Wesley community, sparking feelings of 'anger and betrayal'.<sup>48</sup> If this information had been disclosed earlier, stakeholders would have been in a position to act earlier if they felt this was inappropriately high.

<sup>46</sup> See Chapter 5, Board Size, Composition, Remuneration and Experience.

<sup>47</sup> This question was included in the survey upon the suggestion of Ms Lesley Alway and we thank her for her helpful comments on the draft survey form.

<sup>48</sup> 'Heavy loss adds to charity's woes', *The Age*, 22 November 2000, p. 3.

### Canadian position

By way of an example of what could be required, we note the Canadian ‘Registered Charity Information Return’ (copy contained in Appendix 4). The Return asks detailed questions concerning compensation of employees and directors. For example, ‘For the five highest compensated positions indicate the number of positions in each of the following annual compensation categories. Include only those positions that are permanent, full-time positions.’ It does not ask the amount that directors are compensated, but merely whether or not they were compensated during the fiscal period.

### Related Party Transactions

The rules regarding disclosure of related party transactions (as contained in Chapter 2E of the *Corporations Act 2001* (Cth)) are applied differently to companies limited by guarantee depending upon whether they hold a name licence or not. Those that hold a licence to omit the word ‘limited’ from their name (a name licence)<sup>49</sup> are not bound to comply with the related party transaction provisions.<sup>50</sup> Those that do not hold a name licence must pay regard to related party transactions. For all companies (name licence, no name licence, limited by guarantee or proprietary), excessive remuneration may constitute oppressive or unfair conduct under Part 2F.1 of the *Corporations Act 2001* and/or a breach of directors’ duties.

Inconsistency in the application of the related party provisions does not seem desirable. We are unaware of any sound policy reason for why a sub-group of NFP companies should be exempt from reporting, and gaining member approval, for example when a relative of a director is going to receive a payment that is in excess of what can be regarded as ‘reasonable remuneration’.<sup>51</sup> It also seems desirable that organisations should report payments to trustees or Board members of NFPs by related parties. This is particularly an issue for, for example, the charitable arm of a large corporation.<sup>52</sup>

## 5.11. Attendance of directors at Board meetings

### 5.11.1. CURRENT LEGAL REQUIREMENTS

NFP organisations that are incorporated as companies limited by guarantee are required to disclose the attendance of directors at Board meetings in their annual directors’ report to ASIC (s 300(10) *Corporations Act 2001* (Cth)). The information required includes the directors’ qualifications, experience and special responsibilities, number of meetings attended during the year for each director, and the number of meetings of each Board committee held during the year, and each director’s attendance at those meetings.

### 5.11.2. SURVEY DATA

The overall support for this proposition was 37%, which is not high: especially given that disclosure to ASIC is already a legal requirement.

The data concerning activity groups followed the standard pattern that has emerged from the disclosure data, with the lowest support coming from Religious (19%) and Interest Group organisations (23%) and the highest coming from Other Human Services (55%) and Environmental organisations (54%). However, as Figure 13 shows, large organisations showed far greater support for disclosure of Board attendance than small organisations - with 19% difference between these categories.

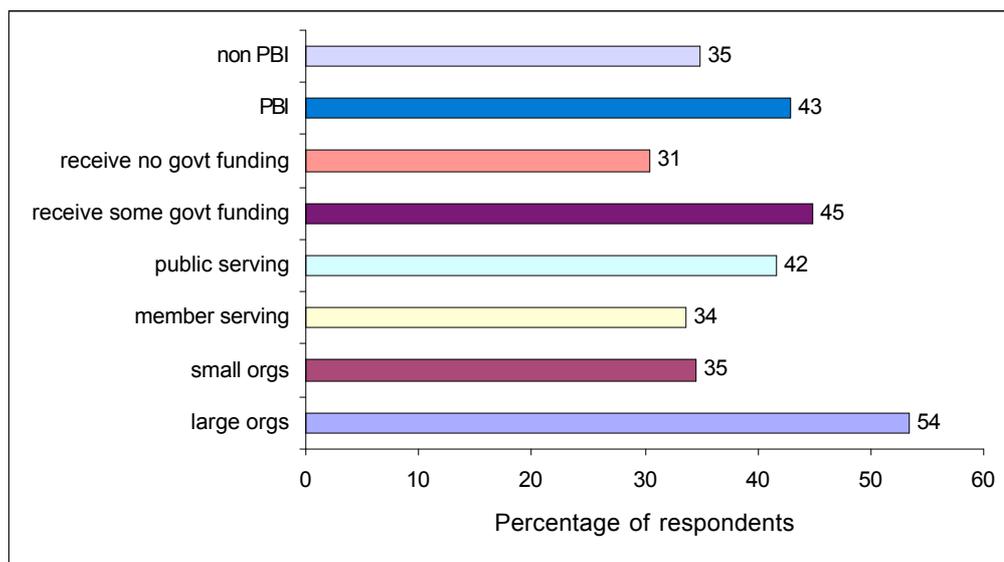
<sup>49</sup> See *Corporations Act 2001* (Cth), ss 150–1.

<sup>50</sup> This follows from para. (b) of the definition of ‘public company’ contained in the *Corporations Act 2001* (Cth), s 9.

<sup>51</sup> There are certain exceptions, where member approval would not be required. For example, where the financial benefit represents ‘reasonable remuneration’ under s 211(1) *Corporations Act 2001*.

<sup>52</sup> Accounting and Reporting by Charities: Statement of Recommended Practice, revised 2000, UK Charities Commission, October 2000, para. 166.

Figure 13: Attendance at Board meetings should be disclosed, based on key indicators



### 5.11.3. OBSERVATION

The attendance of directors at Board meetings is one of the key indicators of the good management of an organisation and that the directors are fulfilling their directors' duties.<sup>53</sup>

This may be a particular issue for organisations that have large numbers of directors, bearing in mind that 4% of the NFP organisations surveyed had more than 15 directors, including one respondent with 40 and one with 45. Boards with this number of directors are unlikely to expect that directors will attend each (or even most) meeting(s). It is likely that Boards with this number of directors will have a core that attend regularly, and a peripheral group that are called on for expert advice and assistance in particular circumstances. For these organisations, the requirement to disclose attendance may be a telling exercise.

## 5.12. Marketing expenditure compared with fundraising receipts

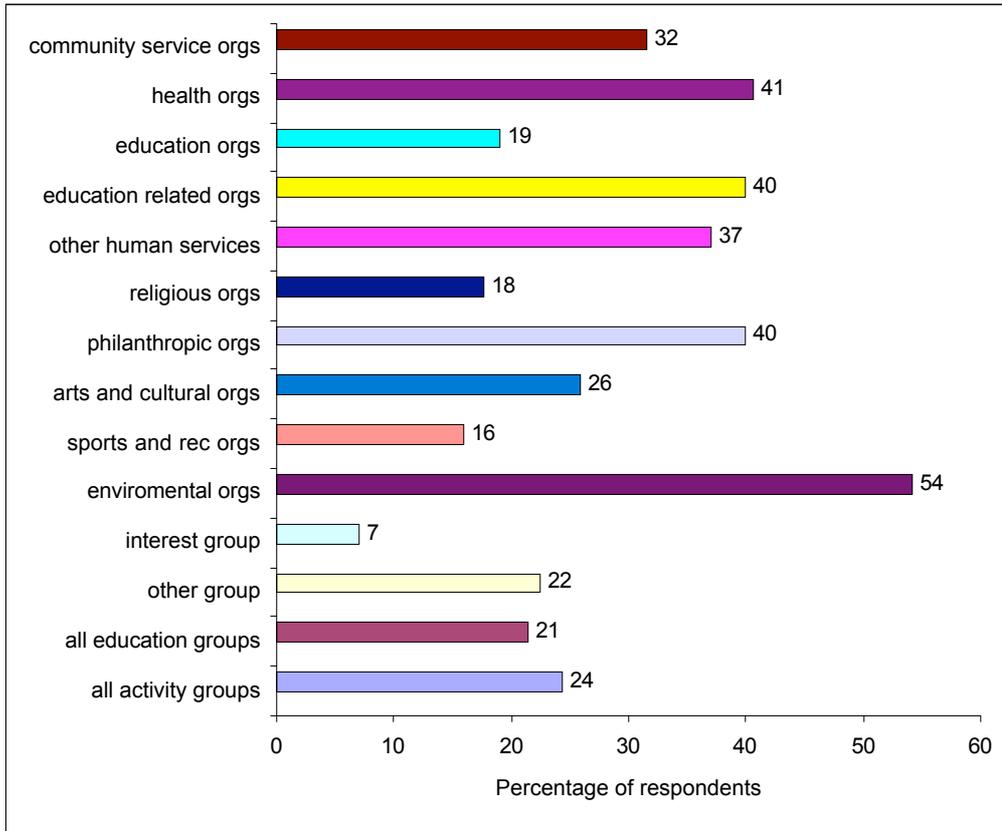
### 5.12.1. SURVEY DATA

The overall rate for respondents who thought 'marketing expenditure compared with fundraising receipts' should be disclosed was 24%. There was no significant difference for this response between small and large organisations. But public-serving organisations were significantly more likely to be in favour of this disclosure than member-serving organisations - 33% vs 17%. Similarly for those with PBI status - 34% vs 20% for non-PBI organisations.

Figure 14 shows the differences based on principal activity. The most striking result is for Environmental organisations, where a majority (54%) were in favour, which is almost twice the overall rate of 24%. Education Related (40%), Philanthropic (40%), Health (41%), Other Human Services (37%), and Community Services organisations (32%) were also significantly more likely to be in favour of this type of disclosure. Philanthropic organisations are often themselves grant-making bodies and this may explain why they were in favour of this type of disclosure (although, we note that they have not typically made this disclosure themselves). Interest Groups and Sports and Recreation were at the other end of the spectrum.

<sup>53</sup> See generally *Commonwealth Bank of Australia v Friedrich* (1991) 5 ACSR 115, esp. pp. 125 -6 and p. 197.

**Figure 14: Marketing expenditure compared with fundraising receipts should be disclosed, based on principal activity**



**5.12.2. CURRENT LEGAL REQUIREMENTS**

There is no requirement under the *Corporations Act* to disclosure marketing expenditure compared with fundraising receipts.

There are various State Fundraising or Collection Acts that regulate this matter. See Table 2.

**Table 2: Legislation governing fundraising<sup>54</sup>**

<b>State</b>	<b>Title of legislation</b>
Queensland	<i>Collections Act 1956</i>
New South Wales	<i>Charitable Fundraising Act 1991</i>
Victoria	<i>Fundraising Appeals Act 1984</i>
Tasmania	<i>Collections for Charities Act 2001</i>
South Australia	<i>Collection for Charitable Purposes Act 1939</i>
Western Australia	<i>Street Collections (Regulation) Act 1940</i>
Australian Capital Territory	<i>Collections Act 1959</i>

<sup>54</sup> Copied from *Review of Not-for-Profit Financial and Annual Reporting*, Chartered Accountants, May 2003, at <<http://www.icaa.org.au/services/index.cfm?id=A105977944>>, p. 16. The Fundraising Institute of Australia, at <[www.fia.org.au](http://www.fia.org.au)> is also a useful source of information.

The Regulations to the NSW *Charitable Fundraising Act* include specific requirements regarding information to be included in the annual accounts of organisations subject to the Act. The *Charitable Fundraising Regulation 1998* (Schedule 1, Part.7 Annual Financial Accounts) requires a comparison of the total costs of:

- fundraising to the gross income from fundraising
- net surplus from fundraising to the gross income from fundraising
- services provided by the authorised fundraiser to the total expenditure
- services provided by the authorised fundraiser to the total income received.

### 5.12.3. OBSERVATIONS

#### Difficulties with current requirements

In their recent report, Chartered Accountants of Australia are critical of the comparisons required under the NSW *Charitable Fundraising Act* outlined above (Heading 5.12.2) on the basis that:

they are at best generic and are focussed on fundraising activities. Users of a NFP's reports (Annual or Financial) would be better served by measurements that are specific to the NFP's total operation.<sup>55</sup>

Even in 1995 the Industry Commission found that most States lack the information management systems necessary to collect comprehensively the information and make it available to the public in a useable form. This effectively limits the accessibility of the information to the public.<sup>56</sup>

Professor McGregor-Lowndes has also noted the high default rates for annual financial reports under fundraising legislation:

Several studies have examined the annual financial report filing default rate of fundraising organisations under fundraising regulation. Two studies of the Victorian register of charities under *The Hospitals and Charities Act* have measured default rates. The first study in 1978 found that 49.9 percent of charities that were not subsidised by government funds defaulted in lodging annual returns and 45.7 percent of those charities that received government subsidies had defaulted.<sup>57</sup> Five years later, when the study was repeated on the same register of charities, it was found that 44.6 percent of charities were in default.<sup>58</sup> The default rate of Queensland charities under the *Collections Act* in 1989 was 38% and in 1992 was 31%.<sup>59</sup> It is probable that such rates of default still exist in some states and do not match the standards set by corporate regulators in business names registries or the ASIC. The annual reports to Parliament of such Departments never publish register default rates. Many regulators do not know what the default actually is at any time. Registers are only now being computerised in some states and there is no electronic filing of returns.<sup>60</sup>

#### Donor demand for this information

The issue of marketing expenditure compared with fundraising receipts is one of particular concern to donors of charities. For example, it has been identified by *Choice Magazine* as a key question for potential donors.<sup>61</sup> Mr Michael Walsh, executive director of Givewell, (a 'for-profit' company that profiles NFP organisations for donors and others), says public scepticism is understandable because there is no code of practice and no independent way of measuring accountability within the NFP sector.<sup>62</sup> In a study conducted by Givewell of a sample of 475 Australian charities, half of those in NSW and only 26% in Victoria disclosed their fundraising costs. By contrast, 83% of overseas aid charities disclosed their expenditure.

<sup>55</sup> Copied from *Review of Not-for-Profit Financial and Annual Reporting*, Chartered Accountants, May 2003, at <<http://www.icaa.org.au/services/index.cfm?id=A105977944>>, p. 17.

<sup>56</sup> Industry Commission Report n. 1, p. 244.

<sup>57</sup> Williams and Warfe, *The Charities Sector in Victoria - Characteristics and Public Accountability*, *Accounting and Finance*, May 1982, at pp. 59 - 61.

<sup>58</sup> McGillivray, Romano, Williams. *Regulating the Accountability of Charitable Associations: The Victorian Experience*, *Australian Journal of Public Administration*, Vol. 44, 1987, pp. 307 - 17.

<sup>59</sup> M. McGregor-Lowndes, C. McDonald & D. Dwyer, 'Public Fundraising in Queensland', Program on Nonprofit Corporations Working Paper No. 14, Brisbane, 1993, p. 18.

<sup>60</sup> See N. McGregor-Lowndes, 'Regulatory Infrastructure for Nonprofit Organisations', August 2000, Working Paper No. PONC97, Queensland University of Technology.

<sup>61</sup> 'The Give and Take of Charities', *Choice Magazine*, November 2002, p. 16.

<sup>62</sup> 'Australia - Taking Account of Making No Profit', *The Australian*, Dossier, 2 June 2001.

### Concerns about comparability

There remain, however, a number of problems with attempting to compare fundraising costs. The UK Strategy Unit Report recognised that fundraising costs vary widely largely due to factors beyond the organisation's control, 'such as the popularity of the cause, and the proportion of income from legacies and endowments'. In a similar vein, the Industry Commission accepted that there are many legitimate reasons why the fundraising costs of one NFP organisation may be high relative to others. It cited a number of examples:

- the organisation may be trying to develop a reputation and support base;
- there may be significant start-up costs with fundraising programs;
- an organisation's cause or programs may not immediately invoke widespread public sympathy or emotion;
- fundraising programs may not just aim to raise money from donors but also to educate and inform the public about issues; and
- fundraising may be aimed at attracting more than just money – it may also aim to attract volunteers or goods in kind.<sup>63</sup>

As mentioned previously, a major problem with disclosure of fundraising costs is standardisation of accounting methods for NFP organisations.<sup>64</sup>

The specific laws concerning fundraising are beyond the scope of this Report, but it seems obvious that they are an area that requires national unification and coordination. Not only is national standardisation necessary in order to carry out meaningful comparisons; there are dangers inherent in lack of coordination. By way of example, according to Ms Marsha Thompson, Minister for Small Business in Victoria (1999), there have been occasions when a charity has been closed in one State, and has subsequently registered in another state in order to fundraise.<sup>65</sup> The Industry Commission also identified inconsistencies in reporting and record keeping between States as a problem, and recommended uniformity or mutual recognition of legislation.<sup>66</sup>

## 6. RECORDING VOLUNTEER HOURS

An additional, important aspect of public donation is the donation of time. The Chartered Accountants of Australia recommended that NFP organisations give consideration to:<sup>67</sup>

- recognising as revenue and expense the value of donated services if the services would have been purchased had they not been donated
- disclosing by way of note to the accounts the contribution of volunteers if sufficiently accurate records of time contributed are maintained – this will satisfy the requirement of AASB 1004, Revenue, which includes revenue 'savings of outflows...that result in an increased equity during the financial year'.

In our opinion the recognition of the value and role of volunteers is an important aspect of disclosure for NFP organisations.

## 7. SLIDING SCALE OF REPORTING OBLIGATIONS?

### 7.1. Distinction based on public-serving or members-serving

In this section we consider two options for criteria for a sliding scale of reporting obligations:

- (a) one based on the public-serving and member serving distinction; and
- (b) one based on differences in size.

Should reporting obligations be different for a member-serving organisation compared with a public serving organisation? Is there any merit in arguing that the public interest in the affairs of public-serving organisations is greater than for member-serving organisations and, therefore, their public disclosure obligations should be correspondingly greater? Can member organisations be regarded as essentially private in nature even though 91% of respondents said they were income exempt? A distinction on the

<sup>63</sup> Industry Commission Report, n. 1, p. 236.

<sup>64</sup> See Headings 5.6.1 and 9.

<sup>65</sup> 'Pledge to crack down on "shonky" charities', *The Sunday Age*, News, p. 3, 21 November 1999.

<sup>66</sup> Industry Commission Report n. 1, Recommendations 9.1 and 9.2, p. 235 and p. 244.

<sup>67</sup> *Review of Not-for-Profit Financial and Annual Reporting*, Chartered Accountants, May 2003, at <<http://www.icaa.org.au/services/index.cfm?id=A105977944>>, p. 25.

basis of member vs public-serving is complicated by the fact that not all organisations can be neatly classified as member or public-serving; there are a number of hybrids, for example, universities, cooperatives.

A strong policy argument might be made that, for small, member serving organisations (such as sporting clubs or self-help groups), it is reasonable that they should only be required to disclose summary financial information to the public. Greater public good is served by preserving precious income from diminution on audit fees. This is clearly the view of the surveyed member-serving organisations. The data reported shows that the majority of Sports and Recreation organisations as well as Religious organisations were consistently of the view that the current reporting requirements were excessive, and opted for the most limited disclosure options.

Against this is the policy argument that, as the vast majority of member-serving NFP companies say that they receive exemption from income tax, this constitutes public (tax) money forgone and, therefore, the public have a right to access fully audited accounts to see how that public money has been used by the organisation. Put another way, the taxation privilege should carry with it a corresponding public disclosure responsibility, no matter the size or purpose of the organisation. As The Reverend Tim Costello recently commented concerning churches:

The churches have an enormously privileged position in society - not only do they not pay tax, but they are exempt from many of the fringe benefit rules as well. As a result, they need to be open and fully accountable.<sup>68</sup>

The data discussed in this Chapter shows that certain activity groups who identified very strongly as member-serving, such as Sports and Recreation as well as Religious organisations, showed a very strong trend against high levels of disclosure. However, it is our opinion that because both member and public-serving organisations receive taxation benefits and significant public funds, this does not seem to be a sound basis for a distinction in disclosure obligations.

### 7.2. Distinction based on size

Arguments for differences in disclosure based on size have been canvassed under various headings in this Chapter. After some consideration, it seems size is the only distinction that can logically be supported. There are numerous precedents for distinguishing between organisations on the basis of size. This is the practice in countries in which specialist NFP or charity legal forms and independent regulators have been created - as in the UK,<sup>69</sup> Canada, and the proposed NZ form.<sup>70</sup>

As has been discussed in Chapter 3, Legal Structure, and elsewhere, there is also a precedent for distinguishing between organisations on the basis of size Australia following the *First Corporate Law Simplification Bill 1995* which introduced the small proprietary limited company. The benefit of using size as the distinguishing feature is that it is more easily applied by 'lay' people and the NFP bodies themselves, and would, therefore, provide greater certainty than any test based on a member/public serving test distinction.

Further work is required to determine appropriate definitions of small and large in the NFP context. In this regard, the data reported in Chapter 1, Profile Data will be valuable. There are also some examples that could be drawn on from the incorporated associations' regime.<sup>71</sup>

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<sup>68</sup> G. Bearup, 'Praise the Lord and pass the chequebook', *The Age Magazine*, Good Weekend, 25 January 2003, pp. 14 - 19.

<sup>69</sup> In accordance with the Charities (Accounts and Reports) Regulations 2000 only a simplified version of the Annual Report is required of charities with an annual income of £250,000 or less; Annual Returns are not required of registered charities with a gross income or total expenditure for the year of under £10,000; the Accounts required of registered charities differ depending on the size of the charity. Audits are only required of non-company charities that have an income in excess of £10,000 or, for those charities with income less than £10,000 and have a total expenditure exceeding £250,000 in the financial year in question or in the two previous financial years. Charitable companies are required to have their accounts audited by a registered auditor if their gross income is over £250,000.

<sup>70</sup> The NZ Report by the Working Party on Registration, Reporting and Monitoring of Charities recommended that the type of financial information provided by NFP organisations as part of their annual return be determined by size. A summary of financial information would be required from all registered charities. Audited financial statements would be required only from those organisations that receive more than \$100,000 annually from public donations, excluding church collections and grants from grant making bodies: *Report of the Working Party on Registration, Reporting and Monitoring of Charities*, 28 February 2002, p. 20.

<sup>71</sup> See the comparative table in Appendix 5.

There should always be a right for ASIC to require any NFP company to prepare financial reports and to have them audited (as currently exists in relation to small proprietary companies under s 294(1) *Corporations Act 2001* (Cth)). Thought needs to be given to the percentage of members that should be able to make the same request - for small proprietary companies it is currently 5% of members (see s 294(1) *Corporations Act 2001* (Cth)). It has been suggested to us by an experienced lawyer in the field that this would be much too low, and that 25% may be more appropriate.

## 8. PENALTIES

### 8.1. Current position

ASIC charges a 'review fee' which is payable on a yearly basis, two months after the 'review date' to which the fee relates (*Corporations Act 2001* (Cth), s1351(3)). This 'review date' of a company is the date of registration of the company or scheme. The CLERP 7 laws brought in a new regime of 'review fees'. The review fee for public companies, which includes NFP companies limited by guarantee, is \$1,000. In contrast, the 'review fee' for proprietary companies is \$200.

As of 1 September 2003, the fee for the lodgement of annual financial reports is \$1,000 (increased from \$900).<sup>72</sup> However, some NFP companies limited by guarantee can pay a reduced fee (\$36)<sup>73</sup> if they fall within the definition of a 'special purpose company'. This term is defined in the regulation 2A *Corporations (Fees) Regulations 2001* and includes any company that holds a licence to omit the word limited from its name, or has objects that are useful to the community,<sup>74</sup> or has a constitution which requires the company to pursue charitable purposes only and to apply its income in promoting those purposes.

### 8.2. Enforcement

During 2002, ASIC found that many small public companies engaged in charitable or welfare activities, and which may be limited by guarantee, failed to comply with their lodgement obligations.

There is no automatic relief from the lodgement requirement under the *Corporations Act*, or by way of class order, for registered public companies, whether small companies or charitable organisations, or those engaged in NFP activities. In a recent statement on behalf of ASIC, the National Director, Mr Drysdale, warned:

ASIC is of the view that the status of a company as charitable, or small, not-for-profit company is not sufficient grounds to provide relief from the lodgement requirements, and advises companies that an application on this basis is unlikely to be successful. Whilst we would prefer to encourage a culture of compliance, and ensure that companies meet their reporting obligations under law, ASIC will not hesitate to take action against companies who fail to meet their legal obligations, and will seek appropriate remedies to ensure compliance, including enforcement through the Courts.<sup>75</sup>

### 8.3. Observation

Further inquiry should be carried out into the effectiveness of these penalties. While they are a good way to prompt commitment to laws, they may not be sufficient on their own. In Chapter 4, Regulatory Framework, we have made recommendations about the role of ASIC and the need for a sliding fee structure based on size. In conjunction with penalties, easy access to information about obligations and best practice procedures is vital. The recommendations we have made about the establishment of an independent NFP advisory body, and the role of ASIC, are also directed at improving compliance rates.

<sup>72</sup> 'Corporations (Review Fees) Regulations 2003; Corporations (Fees) Amendment Regulation 2003 (No 2)', reported in *Australian Corporate News*, Issue 12, 2 July 2003, CCH, p.133.

<sup>73</sup> Item 7, Schedule 1, *Corporations (Fees) Regulations 2001*.

<sup>74</sup> These include, but are not limited to, being formed for the purpose of providing recreation or amusement or promoting commerce, industry, art, science, religion, charity, patriotism, pension or superannuation schemes.

<sup>75</sup> ASIC Media Release 03 - 189, dated 19 June 2003, reported in *Australian Corporate News*, Issue 12, 2 July 2003, CCH, pp. 131 - 2.

We note comments by Professor Mark Lyons:

ASIC is not particularly interested in nonprofit companies but the law requires that it apply the same regulatory rigour to them as to publicly listed corporations. This means a high standard of reporting is required but in a format that is designed to provide information for investors. It is of little use to anyone wishing to review the performance of a nonprofit organisation, perhaps as a prelude to donating, or to discover the strength of its claim to speak for a segment of the population. It also means that rules for submitting annual reports and reporting changes in directors are rigorously enforced and high fines levied for noncompliance. Several medium sized nonprofits have been bankrupted by fines imposed by ASIC for relatively minor infringements.<sup>76</sup>

## 9. RECOMMENDATIONS

On the basis of the data and observations made in this Chapter we make the following specific recommendations for reform.

### **Recommendation: Reform of *Corporations Act* disclosure requirements**

The current disclosure obligations required by the *Corporations Act 2001* (Cth) (in particular the requirement for audited accounts by small NFP companies limited by guarantee) do not achieve the appropriate balance between legitimate public and stakeholder interest in disclosure, on the one hand, and the relative cost to the size of the organisation, on the other. A sliding scale of disclosure requirements based on size should be developed for NFP organisations, and be tailored specifically to the needs of stakeholders. There should be a minimum disclosure standard required of all NFP organisations, regardless of size, and this should include:

- summary or concise financial statement, based on an NFP specific accounting standard
- a description of the activities that have been carried out, and how they meet the objects of the organisation
- disclosure of whether or not directors have received remuneration.

For larger organisations, further information should be supplied. This could include:

- audited accounts
- disclosure of the amount (and possibly sources) of public funding.

Small organisations might be defined as organisations whose annual income or total annual expenditure is less than \$100,000. However, further consideration needs to be given to the criteria for determining size. ASIC, or a certain percentage of members, should have the residual power to require any organisation to be audited.

### **Recommendation: Introduce a NFP-specific Accounting Standard**

The 1995 Industry Commission's recommendation that the Australian Accounting Standards Board and Public Sector Accounting Standards Board develop suitable accounting standards for NFP organisations, should be implemented. Consideration should be given to elements from which it would be appropriate to exempt small organisations.

<sup>76</sup> See M. Lyons, 'The Legal and Regulatory Environment of the Third Sector', *Asian Journal of Public Management*, forthcoming, 2003.

**Recommendation: Review overall NFP disclosure obligations**

The survey data demonstrates that a review of the overall reporting obligations for NFP organisations is required. The data shows that current disclosure requirements:

- are not well tailored to the needs of the NFP sector and its stakeholders
- entail considerable duplication
- have an overall load that is too onerous for most small NFP organisations.

The current reporting requirements for fundraising are State-based, irregular and often duplicate the taxation and corporations law requirements. This duplication places an unnecessary administrative burden on NFP organisations, which often rely on volunteer labour. The reporting obligations under various Acts - including the *Corporations Act 2001* (Cth) and various State Fundraising and Collection Acts - should be unified. Multiple filings should be avoided and low-cost, online searching facilities should be available so as to maximise transparency. It is desirable that the reporting obligations should, as much as possible, constitute a 'one-stop' report that would satisfy the needs of various bodies.

A review of NFP disclosure requirements should include consultation with the NFP sector and their stakeholders. The review will also need to have regard to sometimes competing concerns of a range of organisations such as funding bodies, the Australian Taxation Office, State departments administering the Fundraising/Collection Acts and peak accountant bodies, with a view to minimising the current duplication of disclosure obligations.

## 10. ISSUES FOR FURTHER DELIBERATION

On the basis of the data and observations made in this Chapter the following are issues that we believe require further deliberation and discussion.

**Issue for further deliberation: Standard Information Return**

Consideration should be given to the desirability of developing a Standard Information Return, similar to the Annual Return proposed by the NZ Working Party on Registration, Reporting and Monitoring of Charities (see Appendix 4).

Consideration should be given to whether organisations should be asked to disclose their main purposes and activities. Matters for disclosure might include the number of years the activity has been carried out, in what geographical areas, and how those activities furthered the objects of the organisation. The Return might also include questions about how accountability to stakeholders is achieved.

**Issue for further deliberation: Disclosure of payments to directors**

Where directors, trustees or committee members or related parties (that is, relations or associates) receive benefits of any kind (including salaries, fees, honoraria, and in-kind compensation), these should be publicly disclosed. Consideration should be given to the application of Chapter 2E of the *Corporations Act 2001* (Cth) (related party transactions), or possibly new conflict of interest type-provisions, to all NFP companies. That is, removing the existing exemption for companies limited by guarantee that hold a licence to omit the word 'limited' from their name. This would be in addition to finding the most effective way of ensuring that all NFP organisations disclose remuneration of directors and officers.

### Issue for further deliberation: Fundraising accounting standards

Further consideration should be given to the way revenue from fundraising, gifts, memberships, dues and association fees, and the sale of goods and services, is disclosed. This is in addition to disclosure of moneys spent on administration, advertising, promotion and the like. This matter requires further consideration by the Australian Accounting Standards Board, as comparability between organisations is a vexed issue. Consideration should be given to including an estimate of the number of volunteer hours donated to the organisation, because the donation of time and labour is an important and unique aspect of the NFP sector.

## 11. CONCLUSION

Public disclosure requirements are linked to an organisation's legal structure. The myriad of structures under which NFP organisations operate has resulted in inconsistencies and significantly disparate disclosure obligations that are not based on any sound, overall public policy approach. Accountability relies on relevant, accurate and up-to-date disclosure. If the NFP sector as a whole is not seen to be accountable, public confidence will be jeopardised and donations put at risk. Current disclosure requirements under the *Corporations Act* do not meet the needs of NFP stakeholders nor do NFP organisations believe they are appropriate. Both the *Corporations Act* requirements, and the overall disclosure requirements for NFP organisations (including State-based fundraising legislation), are in need of review. The needs of both small and large NFP organisations and their stakeholders need to be prioritised. It needs to be a proactive, 'whole of government' approach and it needs to occur before there is any particular need to 'react'.

The survey data reported in this Chapter shows that the respondents are of the opinion that the current reporting obligations are in excess of those that they think should be required. This is not, of itself, reason to reduce disclosure. In fact, we have recommended greater disclosure on some issues such as description of activities, directors' remuneration and related party transactions. However, the key is the nature of the disclosure - *what* is required to be disclosed and *by whom* - rather than a blanket call for more information.

The concessional taxation treatment enjoyed by almost all respondents and the reliance on donations from the public, mean that even very small NFP organisations and those that are primarily member serving, should have a requirement to make some public disclosure. Any disclosure in addition to such a 'minimum requirement' needs to be carefully targeted and proportionate to risk - both to the risk of abuse and also to the risk of damage to public confidence. In general, this means that regulation of small organisations, where the sums of money involved are modest, should be lighter than regulation of large organisations, which handle large sums and may also have a disproportionate impact on public confidence.<sup>77</sup> With this principle in mind we have recommended a distinction between large and small NFP companies in determining what ought to be disclosed to ASIC. While small business gained concession several years ago, it is time for the NFP sector to demand some attention to their needs.

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<sup>77</sup> In this regard undertaken by the UK Strategy Unit is valuable. See UK Strategy Unit Report, n. 1, p. 30, para. 3.10.

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# APPENDIX 1: METHODOLOGY

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## 1. CHOICE OF SURVEY FOR DATA COLLECTION

The principal method of data collection for the Project has been a major survey. The original grant application envisaged a combination of a mailed questionnaire and a series of semi-structured interviews with directors, chief executive officers (CEOs) and legal/management advisors of NFP companies. The amount of funding actually received meant that it was not possible to undertake both forms of data collection. Given the paucity of even the most basic profile data on NFP companies,<sup>1</sup> the choice was made to undertake the survey by way of a mailed questionnaire. This approach was considered to be the most useful way to obtain a relatively accurate cross-sectional snapshot of NFP companies. Together with this profile snapshot, the survey was also seen as an effective way of obtaining large scale empirical evidence as to whether existing companies regulation is perceived by NFP companies (or at least the predominant group of them) as adequately meeting their needs, particularly in terms of structural suitability, disclosure and accountability requirements. Compared to say, face-to-face or telephone interviews, a mail-out questionnaire also has the advantages of:

- being a cost-effective way of obtaining large amounts of information from a large sample
- gives respondents time to consider their answers
- allows respondents to remain anonymous
- helps reduce interviewer bias
- gives geographical flexibility.<sup>2</sup>

### 1.1. Methodical limitations

It is, however, acknowledged that a survey is a 'heavy- metal' technique, with certain limitations:

- response rates from mailed surveys are generally lower than for face-to-face research
- respondents may choose whether to respond or not, leading to sample bias
- questions are generally not open-ended, thereby limiting the scope of responses (the questions asked do not necessarily match those most important to the respondent).<sup>3</sup>

These limitations have been mitigated to some extent through the inclusion of open-ended questions, and through ensuring a broad sample selection, as discussed below. Ideally, this largely quantitative survey data will, in the future, be supplemented by further qualitative research using a range of other techniques such as face-to-face interviews and case studies.

### 1.2. Sample selection

The questionnaire was sent to *all* registered companies limited by guarantee (except the small sub-set of superannuation trustee companies and those in external administration), thereby making it more akin to a census than a sample. Therefore there is no concern about sample selection or whether the sample was representative. That leaves only the question of possible bias arising from a non-response bias. This is discussed under Heading 5.

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<sup>1</sup> It is not even possible to identify the total number of NFP companies in Australia. ASIC's records do not separately identify this group. Neither the Australian Nonprofit Data Project (as reported in M. Lyons and S. Hocking, *Dimensions of Australia's Third Sector - Report of the Australian Nonprofit Data Project*, Centre for Australian Community Organisations and Management (CACOM) University of Technology, Sydney, 2000, especially p. 81), nor the recently released ABS Satellite Accounts ('Non-profit Institutions Satellite Account', ABS Cat. No. 5256.0 released 28 November 2002), distinguish the number of NFP companies from other forms of organisation.

<sup>2</sup> See M. Hager, S. Wilson, T. Pollak, P. Rooney, *Response Rates for Mail Out Surveys of Nonprofit Organizations: A review and Empirical Test* 32, June 2003, *Nonprofit and Voluntary Sector Quarterly*, 252 at p. 252-7.

<sup>3</sup> P. McNeill, *Research Methods*, 2<sup>nd</sup> edn, Routledge, London & New York, 1989, p. 47.

## 2. SURVEY FORMAT

A copy of the actual questionnaire is contained as Appendix 3.

A draft questionnaire was piloted with a trial group of eight CEOs/retired CEOs. Their (very useful) comments were taken into account in the final version.<sup>4</sup> Comments on an earlier draft were also kindly given by fellow academics and practitioners (legal, accounting and management) with experience in the field.<sup>5</sup>

The questionnaire addressed to the CEO was mailed to every registered company limited by guarantee (except those recorded as superannuation trustee companies and those in external administration). The questionnaire was divided into six main parts:

- A) General company profile - questions on principal activity, size (assets, liabilities, income, employees, volunteers, members), tax status, member-serving or public-serving etc.
- B) Legal structure - why a company was chosen as the legal structure and the success (or otherwise) of that choice etc.
- C) Stakeholders - who are the company's main stakeholders, what reporting (if any) is there to these stakeholders and have there been any tensions between them.
- D) Board composition and experience - demographics of those on the Board of Directors and their skills and experience, whether they are paid for their services etc.
- E) Board structure and procedures - how often the Board meets, induction of new members, the organisational role of the Board, advice received by the Board etc.
- F) Regulatory framework - what information (if any) should be made available to the public about the organisation, who is the most appropriate regulator, how well does ASIC perform etc.

The 10-page questionnaire with an explanatory covering letter was posted on 13 March 2002. Yellow paper was used to help distinguish the questionnaire and from general feedback, this seems to have been successful. The covering letter was addressed to the CEO and a reply-paid envelope was enclosed. The reverse of the covering letter had instructions for completion as well as space for contact details (for a copy of the results of the survey and/or willingness to participate in future focus groups, should they be held). On this page, all respondents were asked for their company name and number - simply to ensure that a follow-up letter did not get sent to those who had already completed it. The first page (covering letter and instruction sheet) was perforated and removed on receipt of the questionnaire. These 'first' pages were stored separately from the rest of the questionnaire to ensure confidentiality. In this way, no re-identification of the first page (with company name and number) and the completed questionnaire was possible.

While the questionnaire collected primarily quantitative information, qualitative data was also collected. The quantitative data was collected through: (a) closed questions that sought numeric ratings (for example, using a scale of 1 to 4, with a 'don't know' option where appropriate); (b) forced choice items (for example, 'Yes' or 'No'); and (c) multiple response options (for example, a list of possible documents that the respondent thought should be lodged with ASIC from which one or more could be chosen). Qualitative data was collected through open-ended questions that sought written comment or clarification.

The survey was promoted as widely as possible throughout the sector, on a variety of email lists, electronic bulletin boards and flyers<sup>6</sup> and a follow-up letter (also on yellow paper) was sent on 11 April 2002.

<sup>4</sup> We would like to thank Ms Barbara Hocking (Schizophrenia Australia Foundation), Ms Lyn Roberts (National Heart Foundation of Australia), Ms Lynette Moore (Alzheimer's Association Victoria), Mr Paul Geyer (Central Bayside Division of General Practice), Mr Lindsay McMillan (MS Society of Victoria Ltd), Ms Robyn Cowie (Vic Raid/Active Property Service Management Ltd), and Mr David Chalker for being the trial group of CEOs.

<sup>5</sup> We would like to thank Professor Myles McGregor-Lowndes (QUT), Professor Mark Lyons (UTS), Professor Ian Ramsay, Professor Richard James, Mrs Sally Sievers and Ms Lesley Alway (Phd candidate University of Melbourne), Dr Virginia Lewis (La Trobe University), Mr John Emerson (partner, Freehills, solicitors), Mr Robert Wright (solicitor), Mr Tony Lang (barrister), Ms Elizabeth Cham (National Director, Philanthropy Australia Inc), Ms Catherine Brown (consultant) and Mr David Gibbs (partner, McInnes, Graham & Gibbs, chartered accountants) for their thoughtful comments on the draft questionnaire.

<sup>6</sup> Notices were placed in *Philanthropy Alert*, Issue 11, 28 February 2002 and Issue 14, 29 April 2002; the internal email bulletin for Research and Evaluation Network, Department of Family and Community Services; 'Current Issues' section on the Centre for Philanthropy and Nonprofit Studies, Queensland University of Technology website at <<http://cpns.bus.qut.edu.au/>>; 'Community News' section of the weekly email bulletin 'Community Building News', produced by Infoxchange at <<http://www.infoxchnage.net.au/>>; 'Dramatic Online' at <<http://www.dramaticonline.com/>>; ProBono Australia E-newsletter, 18 April 2002 at <<http://www.probonoaustralia.com.au/>>; Centre for Corporate Law and Securities Regulation website, The University of Melbourne at <<http://cclsr.law.unimelb.edu.au/>>; one-page flyer sent with *Impact*, March edition, Australian Council of Social Service magazine and email bulletins by some of the State Councils for Social Service; March edition of the email newsletter by Australian Federation of Homeless Organisations; and the March

### 3. SAMPLE

The details of the registered office of all companies limited by guarantee were obtained from ASIC's records as at 1 March 2002. The questionnaire was sent to a total of 9817 companies limited by guarantee. The only companies limited by guarantee that were excluded were those recorded as 'superannuation trustee companies' (21 companies) and those that were in external administration. The sub-classification of superannuation trustee company identified in ASIC's records is no longer used so it was considered unhelpful to include this group when many of them may not be NFP companies. It was also not considered appropriate to include companies in external administration because a liquidator or administrator would be very unlikely to complete the questionnaire or to allow an employee to devote time to this.

Of the responses received, 59% of respondents were in fact the company's CEO.<sup>7</sup> Questions were also asked about whether the CEO was a director of the company in order to ascertain if the perspective was that of a person who was a member of the Board or an observer of the Board - an 'insider' or an 'outsider'. The results showed that 58% of respondents were 'outsiders'. This is in contrast to the earlier, smaller study by Steane & Christie in which their questionnaire was directed to the Chair (that is, an 'insider').<sup>8</sup> The questionnaire used in the Project was directed to the CEO rather than the Chair because it was thought that the CEO was the person most likely to be able to complete the questionnaire with the least amount of effort. In contrast, the Chair would be more likely to be a volunteer who would need to consult the CEO for some of the information in any event. It was also an opportunity to obtain a different perspective to Steane & Christie.<sup>9</sup>

### 4. RESPONSE RATE

The initial number of responses was about 1000. After a follow-up letter was sent on 11 April 2002, further responses were received until mid-August 2002. The total number of returns was 2089, with 1736 of those being completed questionnaires, 355 being 'returned to sender', and one being not completed at all, but returned in the reply paid envelope. Of the completed questionnaires, a small number did not have the company name or number on the perforated first page - these responses were still included in the data set.<sup>10</sup>

From the 300 or so people who rang or emailed after they received the follow-up letter and from the subsequent follow-up telephone survey that was conducted (see Heading 5), it is clear that there was a very high non-receipt rate. Similar non-receipt rates have been experienced in earlier studies and are not uncommon when there is reliance on a public register.<sup>11</sup>

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edition of the email newsletter for the Australian Council on Disability (National). We would like to thank these organisations for allowing the notice to be placed in their respective publications/websites.

<sup>7</sup> Question 7.4 asked: 'Are you (that is, the person completing this questionnaire on behalf of the company): the company's chief executive officer?' 'Yes' or 'No' (tick 'Yes' if you are the company's most senior employee even if you have a different title.)

<sup>8</sup> P. Steane & M. Christie, 'Nonprofit Boards in Australia: A Distinctive Governance Approach', 2001, 9 *Corporate Governance* 48 at 51.

<sup>9</sup> Steane & Christie, n. 8.

<sup>10</sup> On the basis of phone calls received from some of these respondents when they did receive the follow-up letter, it seems that the details were omitted from the first page because of a concern about confidentiality. There was, therefore, no need to exclude these responses from the data set.

<sup>11</sup> See M. McGregor-Lowndes, 'Nonprofit Corporations – reflections on Australia's Largest Nonprofit Insolvency', 1995, 5 *AJCL* 417 at p. 420: 'After the collapse of the NSC [National Safety Council], the Victorian Corporate Affairs Commission wrote to all Victorian companies with section 66 licences [licence to omit the word "limited" from company name] to request a copy of their audited financial statements...The Commission could only make contact with 62% of the companies on their register.' See also results of a similar study conducted by McGregor-Lowndes of companies listed on the Queensland register to which 35% replied: M. McGregor-Lowndes, 'Regulatory Compliance of Two Forms of Nonprofit Enterprise', unpublished LLM thesis, Griffith University, 1989, p. 91.

When the non-receipt rate is taken into account, the response rate is estimated to be 39%.<sup>12</sup> Getting about a third of companies responding was very pleasing given the length of the questionnaire (10 pages), the detailed knowledge of the organisation required to complete it and the fact that the majority of NFP companies rely on volunteers.<sup>13</sup> Having the imprimatur of both The University of Melbourne and Philanthropy Australia and the prior advertising within the sector seems to have contributed to the response rate. The response rate is similar to earlier Australian studies, including that conducted by Steane & Christie,<sup>14</sup> and is common for mail-out surveys.<sup>15</sup> It also reflects the subject of the survey was an organisation rather than an individual. Research shows that where the questions are about the characteristics of an organisation (such as the number of employees or annual budget), rather than about the individual (such as the respondent's sex, age or annual income), the typical response rate is substantially lower.<sup>16</sup>

## 5. NON-RESPONSE AND SAMPLE BIAS

### 5.1. Follow-up telephone survey

In order to explore whether there were any systematic differences between those organisations who participated in the study and those who did not (that is, to check if the sample was in any way biased), a follow-up telephone survey was conducted in August 2002.<sup>17</sup>

The sample was selected from the total population of non-responders to the original questionnaire. Companies were excluded if the questionnaire sent to them had been returned to the sender or was undeliverable. A random sample, stratified by State, of non-respondents was drawn. The population from each State/Territory was sorted by street number to avoid any bias in location within the State.<sup>18</sup> Contact numbers for the selected companies were then found using either White Pages online, or by searching the web for a company web site. If no contact number or address could be located this was noted and a new company selected randomly. The companies were contacted by telephone. The research assistant<sup>19</sup> asked to speak with the CEO or equivalent person. If they were not available but would be available within the next few days a message was left and a note made of when to call back. If they would not be available for more than a week the assistant would explain why he was calling and asked if there was anyone else who may know about the survey.

Once put through to the relevant person, he would explain why he was calling (including that there were many valid reasons for not completing the survey, and that we were interested in discovering why some companies had not responded as a way of checking on possible sample bias). The person was then asked if they recalled receiving the survey:

- a. If they did not, they were asked if anyone else may have received it (if yes, asked to speak with that person).
- b. If it appeared they had not received it, they confirmed the address we had for them.
- c. if they *did* recall receiving it, they were asked why they had not completed it
- d. As a final question, they were asked how many employees and volunteers the company had, and approximate income of the company.

<sup>12</sup> The lower bound estimate was 33%, the upper bound was 47%.

<sup>13</sup> There were 86.6% of respondents with one or more volunteers and 26.1% with no full or part-time employees.

<sup>14</sup> See the Victorian Corporate Affairs mail-out and the McGregor-Lowndes survey, n. 11. The response rate for the Steane & Christie survey (n. 8, pp. 51–2) was 34% (118 responses received from a total sample of 350) - note, this study did not rely on a public register for addresses.

<sup>15</sup> W.L. Neuman, *Social Research Methods: Qualitative and Quantitative Approaches*, 2nd edn, Allyn & Bacon, Boston, 1994.

<sup>16</sup> See M. Hager, S. Wilson, T. Pollak, P. Rooney n. 2, pp. 254–5 where they note that in such surveys an acceptable rate can be as low as 15%. Even if no allowance is made for non-receipt, the 'raw' response rate was 17.7% (namely, 1736 completed out of 9817 sent).

<sup>17</sup> Prior to August 2002 replies were still coming in.

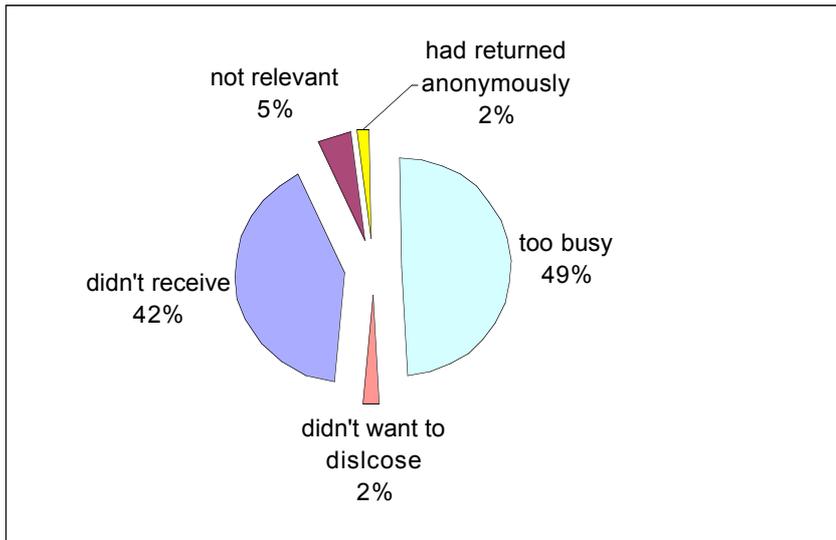
<sup>18</sup> For example, sorting by company name may have resulted in regional clumps where the region name was used as the company name. Similarly for street names and postcodes.

<sup>19</sup> All telephone survey calls and interviews were conducted by Michael O'Neill during his time as a research assistant on the Project. We would like to acknowledge and thank him for his work.

If a company was uncooperative or uncontactable, a further company was randomly sampled to replace it.

As is invariably the case, it was difficult to contact people and get their co-operation. The final telephone sample comprised 57 non-respondents. While there is obviously a limit to what information can be obtained from such a sample, no evidence of bias was found - the non-respondents contacted were from both large and small NFP companies spread across a range of activities similar to our respondents.<sup>20</sup> Of the telephone sample, 49% said they were 'too busy', 42% said they 'did not receive it', 5% said it was 'not relevant to them', 2% did not want to give the information requested and 2% had actually returned the questionnaire but had done so anonymously.<sup>21</sup>

Figure 1: Telephone survey, non-response reasons



### 5.2. Other evidence of non-receipt

The information obtained from the follow up telephone survey about a high non-receipt rate was consistent with information obtained from over 300 phone calls and emails prompted by the follow-up letter sent in April 2002. The majority of these people reported not receiving the initial questionnaire but that they did (eventually) receive the follow-up letter. Non-receipt was often because it had gone to the company's registered office, which was different from its postal address (typically a post office box).<sup>22</sup>

### 5.3. Sample bias

In conclusion, the follow-up data from non-respondents showed a substantial heterogeneity to the main survey data in terms of company size, reported income, assets and liabilities (see Chapter 2, Profile). This heterogeneity did not indicate any markers of sample bias.

<sup>20</sup> Of the sample of 57 non-respondents, 37 were prepared to give an indication of their company's income over the telephone - of these 37 companies, 68% had income of less than \$3 million, 24% had income between \$3-5 million and 8% had income of more than \$5 million.

<sup>21</sup> That is, they had not completed the company name and number section on the first page but, in fact, their response was already included in the 1736 completed questionnaires.

<sup>22</sup> A company's registered office cannot be a post office box: *Corporations Act 2001* (Cth), ss 3, 100, 142, 144, 145, 173 and Pt 1.5 para 3.7; *Corporations Regulations 2001* (Cth), reg. 1.0.14. The ASIC register that is open to the public does not disclose a company's postal address.

## 6. ANALYSIS OF THE DATA

The analysis of the data consisted of four main stages. First, the data was cleaned and checked. Second, frequency tables were produced for the different variables. Third, cross-tabulations were produced to compare the NFP companies of different sizes, principal activities and other characteristics. Where variables were ordinal or nominal (which was in most cases) we used the chi-squared test of independence to test for significant differences between the samples of NFP organisations based on different characteristics. Fourth, where we had 'measured' data, for example, on the number of Board members or the frequency of Board meetings, we used the students' T-Test to compare means for the different samples of respondents.

### 6.1. Coding

In relation to the qualitative data collected (for example, where respondents have added comments or descriptions in the space provided), in most instances we have read the responses and then grouped them with similar responses. A descriptive label has been allocated to each group so that we could draw frequencies - for example, X% gave reason A, and Y% gave reason B and so on. Coding responses in this way helped us develop and refine our interpretations of the data. The coding procedure we used is described as 'latent' or 'semantic' coding.<sup>23</sup> Latent coding examines the text for the underlying or implicit meaning, or themes in the content of the text. We considered it to be the most appropriate method given that most of the questions answered in this way were based on personal opinion or perception. The use of coding for particular questions is indicated in the respective sections of the Report.

### 6.2. Collapsed charts

For a few questions, graded options were given. For example, in question 4.2 the options to circle in for response were (1), (2), (3), (4), (0) and respondents were told that (1) and (4) represent very definite positions and the numbers in between represent intermediate positions and thus, (1) = strongly disagree, (4) = strongly agree and (0) can't say. In some instances, in order to show the refined patterns more clearly, the 'can't say' or 'don't know' (0) responses were excluded, and the 'strongly agree' and 'agree' responses were collapsed to 'agree'. Similarly, the 'strongly disagree' 'disagree' were collapsed to 'disagree'. This was done only where the collapsed chart did not result in any distortion of the refined patterns. If there was a significant number of 'can't say' / 'don't know' responses these were noted in the text or in a footnote.

## 7. SUBSEQUENT FEEDBACK

A Summary of Preliminary Findings was distributed to all respondents to the survey who indicated that they wanted to receive the results. This was by ticking the relevant box and providing contact details on the reverse page of the covering letter. This was accompanied by an email/letter saying that feedback on the initial recommendations for reform was very welcome. This request was met with an enthusiastic response, and a number of respondents emailed or wrote to us with their opinions concerning the Preliminary Findings.<sup>24</sup>

The Summary of Preliminary Findings were also distributed widely to the media, the original triallists, relevant the government departments (for example, the Department of Family and Community Services, relevant Department/Registrar for Incorporated Associations in each

<sup>23</sup> W.L. Neuman, *Social Research Methods: Qualitative and Quantitative Approaches*, Allyn & Bacon, Boston, 2000, p. 295, quoted in Flack & Ryan, 'Accountability of Charitable Organisations: Meanings and Mechanisms', conference presentation at ANZTS, Auckland, November, unpublished, p. 12, 2002.

<sup>24</sup> In particular, we would like to thank Dr Paul Morgan, Deputy Director of SANE Australia, for his detailed and helpful comments. Also Mr A.D. Lang, barrister, Ms Alice McDougall, Freehills, solicitors, and Professor Myles McGregor-Lowndes Queensland University of Technology for their comments at various stages of the Project. Also Mr Stephen Judd, CEO, The Hammond Group; Mr John Fry, Chairman, Frontiers Australia; Mr Alan Graham Executive Officer Australian Council of National Trusts and Mr Ian Dwyer, President, Kiandra Ski Club for their comments and feedback on the Preliminary Findings.

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State/Territory, the Federal Treasurer) and other contacts. Some media coverage was received<sup>25</sup> and this also generated further feedback. Several presentations have been made to a variety of audiences (both academic and to those working in the NFP sector),<sup>26</sup> which has also provided an opportunity for useful feedback. On two occasions other organisations with an interest in the recommendations made in the Preliminary Findings used the opportunity to gather feedback from their constituents to inform their positions.<sup>27</sup> The survey data was subsequently provided to us and has partly informed the recommendations made in this Report.

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<sup>25</sup> ABC Radio National interview 8.15am 4 March 2003; 'Non-profits may get new rules', *The Age* 28 February, 2003; 'Donors query executive pay', *Australian Financial Review*, 5 May 2003.

<sup>26</sup> Presentations by Ms Woodward include: *Building Better Boards A Dialogue for Nonprofit Organisations*, July, Sydney, organised by Nonprofit Governance & Management Centre (inaugural conference attended by more than 400 people); seminar for the Centre for Philanthropy and Nonprofit Studies at the University of Queensland, September 2002; *Doing Well*, bi-annual ANZTSR (Australian and New Zealand Third Sector Research Association) research conference, Auckland, November 2002 (conference paper published on conference website at <<http://www.uws.edu.au/ashs/anztsr/>>); Annual ACROD (National Industry Association for Disability Services) Conference, a conference for the Chief Executive Officers of their member organisations (approx 200 people) Canberra, 19 May 2003; seminar for the pro bono clients of Freehills, solicitors, Sydney, 17 June 200; and *Piercing it together – equity, empowerment & change*, ACOSS (Australian Council of Social Service) Annual Congress, Canberra 13 November, 2003.

<sup>26</sup> At the ACROD conference following the speech given by Ms Susan Woodward, note 26, ACROD asked participants to fill out a survey. A workshop was held at the Freehills seminar note 26, after Ms Woodward's presentation, during which participants discussed the recommendations made, and generated group views on their value for the sector.

<sup>26</sup> A copy of the survey form is contained in Appendix 3.

<sup>26</sup> *First Corporate Law Simplification Act 1995* (Cth) and *Company Law Review Act 1998* (Cth).

<sup>26</sup> For earlier Australian studies see C. McDonald, *Board Members' Involvement in Nonprofit Governance* Working Paper No. 16, Program on Nonprofit Corporations, Queensland University of Technology, 1993. (This was a study that involved the analysis of 242 questionnaires collected from 1218 NFP organisations registered under the *Collections Act 1966* (Qld), however, the legal nature of the organisations was not discussed); J. Radbourne, *Recruitment and Training of Board Members for the 90's and Beyond*, Working Paper No. 24, Program on Nonprofit Corporations, Queensland University of Technology, 1993, (a study that involved surveys, interviews and observations of Board meetings of thirteen Queensland arts organisations; the organisations 'were selected randomly and represented a variety of art forms and legal structures', p. 7); and P. Steane & M. Christie, n. 8 (a study that involved the analysis of one hundred and eighteen questionnaires collected from three hundred and fifty NFP organisations; again there was no distinction as to the legal nature of the organisations).

<sup>26</sup> Lyons & Hocking, n.1.

<sup>26</sup> For example, the Business Regulatory Advisory Group that has given input on reforms proposed as part of both the Simplification Program and the Corporate Law Economic Reform Program. This group is comprised of representatives of peak business (that is, 'for-profit') groups such as the Australian Institute of Company Directors, the Australian Stock Exchange and the Business Council of Australia. See also McGregor-Lowndes 'Regulatory Infrastructure for Nonprofit Organisations', Working Paper No. PONC97, August 2000, Queensland University of Technology.

<sup>27</sup> At the ACROD conference, following the speech given by Ms Susan Woodward, (see n. 26), ACROD asked participants to fill-out a survey. At the workshop held at Freehills, (see n. 26), after Ms Woodward's presentation which participants were divided into groups to discuss the recommendations made, and generated a group view on their value for the sector.

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## APPENDIX 2: RESEARCH PROFILES

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### 1. MS SUSAN WOODWARD

Ms Susan Woodward is a lecturer in the Faculty of Law, and a member of the Centre for Corporate Law and Securities Regulation at The University of Melbourne. Ms Woodward has published substantial articles in refereed journals on the topics of directors' duties and the implications of company law reforms on NFPs (see, for example, 'Not-for-Profit Companies - Some Implications of Recent Corporate Law Reform', 1999, 7 *Company & Securities Law Journal*). She is also a co-author (with Mrs Sievers and Ms Helen Bird) of *Corporations Law - in principle*, 6<sup>th</sup> edn, Law Book Co., 2003, and accompanying *Teachers' Resources* which is used widely by law and non-law students throughout Australian tertiary institutions. The book was also the founding book in the 'In Principle' series of books published by Thomson Legal & Regulatory, and this series was awarded the 'Winner of the Tertiary Book Series' category at 10th Annual Australian Excellence in Educational Publishing Awards 2003.

Previously, in private practice, she acted for several NFP organisations. She has been on several Boards of management of community organisations and is currently an honorary director of a NFP company limited by guarantee.

In relation to the Project, Ms Woodward has published:

- A comprehensive article 'Not-for-profit motivation in a for-profit company law regime - baseline data', 2003, 21 *Companies & Securities Law Journal* 102–33 (reprinted, with permission, in *International Journal of Civil Society Law* 1 INT. J. SOC. LAW at <<http://www.law.cua.edu.Students/Org/IJCSL>>).
- An article 'Not-for-profit organisations: do they fit the company mould?', *Keeping Good Companies*, Journal for the Institute of Chartered Secretaries, June 2003 pp. 278–83.
- Together with Ms Marshall, 'The more the merrier? Stakeholders in not-for-profit companies' accepted for publication by *Third Sector Review*, Journal for Australian and New Zealand Third Sector Research organisation (ANZTSR) (forthcoming April 2004).
- Together with Mrs Sievers and Ms Marshall, a substantive law reform submission to the NSW Department of Fair Trading in response to their Consultation Paper, 'Review of the Associations Incorporations Act NSW'.
- Articles in *Australian Philanthropy* Issue 53 Summer 2003-2004 (Journal of Philanthropy Australia Inc.) and *Impact* Summer 2004 (News Quarterly of the Australian Council of Social Service).

She has also delivered presentations on the Project to:

- *Building Better Boards - A Dialogue for Nonprofit Organisations*, Sydney, July 2002, organised by Nonprofit Governance & Management Centre (inaugural conference attended by over 400 people involved in the management of NFP organisations).
- Graduate and undergraduate law students at The Melbourne University.
- Seminar hosted by the Centre for Philanthropy and Nonprofit Studies at the University of Queensland, September 2002.
- *Doing Well* ANZTSR (Australian and New Zealand Third Sector Research Association) 6<sup>th</sup> Biennial Conference, Auckland, November 2002.
- Annual ACROD (National Industry Association for Disability Services) Conference, for the Chief Executive Officers of their member organisations (approximately 200 people), Canberra, May 2003.
- Together with Ms Marshall, seminar/workshop for Freehills, solicitors, as part of their pro bono services for NFP organisations, Sydney, June 2003.
- *Piecing it together - equity with empowerment and change*, Australian Council of Social Service Annual Congress, Canberra November 2003.

## 2. PROFESSOR IAN RAMSAY

Professor Ian Ramsay is an eminent corporate law scholar and is the Director of the Centre for Corporate Law and Securities Regulation at The University of Melbourne. He is well known for his report on the independence of auditors and has published extensively on directors' duties, conflicts of interest and issues relevant to corporate governance and accountability. In addition, he is the

co-author of one of the main corporate law treatises in Australia, *Ford's Principles of Corporations Law*. Professor Ramsay has provided pro bono advice on issues of corporate law to a range of NFP companies and has published on the topic of eligibility requirements for directors of those NFP companies which have a focus on disability issues: see 'Managing Disability: Who can be a Director?', 1999, 12 Interaction No. 4, *Journal of the National Council on Intellectual Disability*, pp. 9–12.

## 3. MS SHELLEY MARSHALL

Ms Shelley Marshall is a researcher in the Centre for Corporate Law and Securities Regulation, and an Associate of the Centre for Employment and Labour Relations Law, The University of Melbourne. Ms Marshall has been working as a researcher on the Project since January 2003 and has co-authored (with Ms Woodward) the article 'The more the merrier? Stakeholders in not-for-profit companies'. She also published an article 'The Stakeholding Theory of Corporate Governance: Can it deliver upon its promises?', Working Paper No. 17, Centre for Employment and Labour Relations Law, Faculty of Law, The University of Melbourne, 2000. Prior to her work as a research assistant on this Project in the Law Faculty, she practiced as a solicitor with a Victorian plaintiff law firm and worked in the area of legal compliance with an Australian industry group. She has been a Board member of, and honorary legal advisor to, several NFP organisations, and has provided legal advice to not several NFP organisations concerning incorporation within Australia and internationally.

## 4. MRS SALLY SIEVERS

Until 1999 Ms Sievers was a Senior Lecturer in the Faculty of Law, Monash University where she had worked for more than twenty years. She is now a member of the Centre for Corporate Law and Securities Regulation at The University of Melbourne. Mrs Sievers has, for many years, been one of the few Australian legal academics researching and writing on matters relevant to the NFP sector. She was part of the research team whose report led directly to the introduction of the *Associations Incorporation Act 1981* (Vic) and is the author of one of the two Australian texts on non-profit associations (*Associations and Clubs Law in Australia and New Zealand*, 1996, 2<sup>nd</sup> edn, (1<sup>st</sup> edn 1989)). Her recent publications include 'Incorporation of Non-Profit Associations: The Way Ahead?', 2000, 18 *Company & Securities Law Journal*, pp. 311–25 and 'Incorporation and Regulation of Non-Profit Associations in Australia and other Commonwealth Law Jurisdictions', 2001, 13 *AJCL* 124 at 142. Mrs Sievers is also the author of Title 435 'Voluntary Non-Profit Associations' in *Halsbury's Laws of Australia* (looseleaf) and a recent author of Chapter 9.1 'Incorporation of Community Groups' in the *Lawyers Practice Manual Victoria*. In 1993 and 1995 she was awarded ARC Small Grants for research projects on NFP associations. She has been a Board member of, and honorary legal adviser to, several NFP organisations. As already mentioned, she is also a co-author (with Ms Woodward and Ms Helen Bird) of *Corporations Law - in principle*, 6<sup>th</sup> edn, Law Book Co., May 2003 and accompanying *Teachers' Resources*.

## APPENDIX 3: SURVEY FORM

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Copy of survey form – March 2002

Copy of reminder letter – 9 April, 2002



**PHILANTHROPY**  
*Australia*

*Questionnaire on company law issues affecting*  
**NOT-FOR-PROFIT COMPANIES**



**THE UNIVERSITY OF**  
**MELBOURNE**

Dear Chief Executive Officer,

---

***This questionnaire is important*** - please take time (about 20 minutes) to complete it so that the results of this large scale survey can help us to determine whether or not existing company laws adequately meet the needs of not-for-profit companies. Information from this survey will be useful for future law reform proposals - for example, any reforms about the "establishment of an independent administrative body to oversee charities and related entities" as recommended by the Federal Government Inquiry into the Definition of Charities and Related Organisations (June, 2001). *It is vital that we receive as many responses as possible so that we can document accurately the characteristics and needs of not-for-profit companies. Your participation is voluntary and confidential. If you complete the contact details section (see over), we will provide you with a summary of the results as soon as it is available.*

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This survey is being conducted as part of a joint Australian Research Council (a division of the Department of Education, Training and Youth Affairs) research project. This questionnaire has been sent to you as Chief Executive Officer (or equivalent) of a company limited by guarantee that appears on the public register of companies maintained by the Australian Securities and Investments Commission. We have written to **ALL** companies limited by guarantee that are on this register. We have used this category of company because we understand that the vast majority of companies in this category are engaged in not-for-profit activities. If, however, your company is not a not-for-profit organisation, we would still be grateful if you could complete questions 1.1 and 1.2 (this will take less than a minute), and return the questionnaire in the enclosed reply paid envelope.

***Participation and use of data***

Your participation in this study is completely voluntary. By returning the enclosed questionnaire, you and your company will be taken to have consented to participation in the study. The company's name and number (which is the only identifying information that you are asked to provide) will be removed from the rest of the questionnaire as soon as it is returned. For this purpose, this page has been perforated and will be stored separately from the questionnaires in order to ensure that re-identification is not possible. In this way, anonymity will be preserved. Whereas information collected in this study may be published, at no time will individuals or company names be used in any publication. The data will not be used for purposes other than for research and will be destroyed after five years.

If you would like to be advised of the results of this survey and/or to participate in any future focus groups, please provide contact details on the next page where indicated. (Again, to preserve confidentiality, this page will be removed and retained separately from the rest of the questionnaire.)

Thank you for your time and co-operation.

Yours sincerely,

Ms Elizabeth Cham - National Director, Philanthropy Australia Inc.  
(ph (03) 9620 0200 fax (03) 9620 0199)

Prof Ian Ramsay and Ms Susan Woodward - Centre for Corporate Law and Securities Regulation  
The University of Melbourne (ph (03) 8344 6938 fax (03) 8344 5285)

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## Instructions

1. Please complete questions A and B (Company details) below and then the questions on the following pages. As appropriate, please print any written response, tick the most relevant box or circle the number that most accurately reflects your view.
  2. If your company cannot properly be described as a 'not-for-profit' organisation, please complete only questions 1.1 and 1.2 on the next page. Otherwise, please complete all questions – this should only take about 20 minutes.
  3. Place the completed questionnaire in the enclosed reply paid envelope; seal the envelope and post by 2nd APRIL 2002.
- 

If you have any concerns about the conduct of this research, please contact the Executive Officer, Human Research Ethics, The University of Melbourne, Melbourne 3010 ph. (03) 8344 7507, fax. (03) 9347 6739

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## Future contact (optional)

- i. If you would like to be notified of the results of this survey, please indicate below and provide contact details.
- ii. It may be that, after we have analysed the results of this survey, we will run focus groups to discuss particular issues that have arisen from the survey. Please indicate if you (or someone else from the company) would be willing to be contacted about participation in such a group. You will not be contacted unless you indicate this willingness and, even if this contact does occur, there would be no obligation to participate.

The lists of those wishing to be notified of the results and those who have indicated a willingness to be contacted will be retained separately from the survey data and will be used for no other purpose than that indicated.

- yes, I would like to be notified of the results of the survey  
 yes, I am willing to be contacted about focus group discussions

My contact details are as follows: (please print)

Name .....

Company Name .....

Address .....

..... P/C .....

Phone number ..... Fax number .....

Email address .....

---

## Company details (all respondents to complete)

A. Company name:.....

This is the company's name as it appears on the company's certificate of registration and the name used when filing any documents (for example, an annual return) with the Australian Securities and Investments Commission (ASIC), rather than any business name that may be used in activities conducted by the company.

References in the following survey to "the company" are references to the company named above.

B. Australian company number ACN \_\_\_\_\_

*To preserve confidentiality, this page will be detached and stored separately, and the company's name and number will be removed from any published data*

**PART A - GENERAL COMPANY PARTICULARS**

**1. Principal activity**

1.1 Is the company a not-for-profit organisation?  
 (Note: a not-for-profit organisation may make profits and have surplus funds, but its constitution prohibits the distribution of any profits to its members.)

- Yes (please proceed with the rest of the questionnaire)
- No (please complete question 1.2 only and then return the questionnaire in the enclosed reply paid envelope without completing the other remaining questions)

1.2 If 'no', what is the company's principal activity?  
 (please specify).....  
 .....  
 .....

1.3 If 'yes', please indicate the principal nature of the company's activities by ticking ONE of the following boxes and (where necessary) printing a description of the activity. (The classification of activities is based on that used in the Australian Nonprofit Data Project.)

**Community services**

- 1  child care
- 2  accommodation for the aged
- 3  disability services
- 4  youth services
- 5  other residential care
- 6  other non-residential care
- 7  other community service (please specify).....  
 .....

**Health**

- 8  not-for-profit private hospital
- 9  not-for-profit public hospital
- 10  nursing home
- 11  primary care service
- 12  health agency (please specify type).....  
 .....

**Education**

- 13  preschool    14  school    15  university
- 16  other education (please specify).....  
 .....

**Education related**

- 17  research                      18  university union
- 19  parent association

**Other human services**

- 20  housing                      21  employment service
- 22  community transport    23  legal
- 24  other human services (please specify).....  
 .....
- 25  Religious organisation

**Philanthropic**

- 26  trustee of self-administered charitable trust
- 27  volunteer referral centre
- 28  fundraising intermediary
- 29  grant making charitable trust or institution

**Arts and culture**

- 30  library, museum, art gallery
- 31  parks and gardens
- 32  performing arts
- 33  film and video production
- 34  radio and television
- 35  other arts or culture (please specify).....  
 .....

**Sport and recreation**

- 36  sport                      37  social club
- 38  other recreation/hobby (please specify).....  
 .....

Environment

**Interest group**

- 40  labour                      41  business or professional
- 42  peak body
- 43  other interest group (please specify).....  
 .....

**Other**

- 44  business services
- 45  accommodation (eg, youth hostel)
- 46  books and publishing
- 47  emergency services
- 48  Not otherwise specified (please specify).....  
 .....  
 .....

1.4 Is the company's primary purpose to:

- serve its members and supporters
- OR (please tick only one box)
- serve the public

1.5 Does the company hold a licence to omit the word "Limited" (or "Ltd") from its name?

- Yes     No     Don't know

1.6 Is the majority of the company's income exempt from income tax?

- Yes     No

1.7 Are donations to the company (or any fund administered by the company) tax deductible?

- Yes     No

**2. Number of members, employees and/or volunteers**

**2.1.1 Members**

How many members did the company have at 1 March 2002? (We mean 'members' in the legal sense, that is, those people or organisations named in the register of members kept by the company pursuant its obligations under the Corporations Act.)

- 1  1                      2  2 - 9                      3  10 - 19  
 4  20 - 49                      5  50 - 99                      6  100 - 499  
 7  500 - 1,000                      8  more than 1,000

2.1.2 Of the total number of members as at 1 March 2002, approximately how many were:

- 1 individuals .....  
 2 organisations .....  
*(please print a number, or zero, on each line)*

**2.2 Employees**

How many employees (whether full or part-time) did the company have at 1 March 2002?

- 1  none                                      2  less than 5  
 3  5 - less than 20                      4  20 - less than 50  
 5  50 - less than 100                      6  100 - less than 1,000  
 7  more than 1,000

**2.3 Volunteers**

For 2001, estimate the total number of volunteers (whether full or part-time and including volunteer Board members) that provided assistance to the company?

- 1  none                                      2  less than 5  
 3  5 - less than 20                      4  20 - less than 50  
 5  50 - less than 100                      6  100 - less than 1,000  
 7  more than 1,000

**3 Size**

**3.1.1 Income**

As at the end of the company's last financial year, please indicate gross income from all sources (where relevant, please include fundraising, government funding, fees for service, subscriptions, commercial sales, interest income, bequests, philanthropic grants, corporate sponsorship and any other non-government grants).  
*(please tick only one box)*

- 1  less than \$500  
 2  \$500 - less than \$10,000  
 3  \$10,000 - less than \$100,000  
 4  \$100,000 - less than \$500,000  
 5  \$500,000 to less than \$1 mil  
 6  \$1 mil - less than \$5 mil  
 7  \$5 mil - less than \$10 mil  
 8  \$10 mil or more

3.1.2 What percentage of income would you estimate comes from government sources?

..... % *(please print a number or zero)*

**3.2 Assets**

As at the end of the company's last financial year, please indicate the total value of the company's assets by ticking one box.

- 1  less than \$500  
 2  \$500 - less than \$10,000  
 3  \$10,000 - less than \$100,000  
 4  \$100,000 - less than \$1 mil  
 5  \$1 mil - less than \$5 mil  
 6  \$5 mil - less than \$10 mil  
 7  \$10 mil or more

**3.3 Liabilities**

For the company's last financial year, please indicate the company's total liabilities by ticking one box.

- 1  less than \$500  
 2  \$500 - less than \$10,000  
 3  \$10,000 - less than \$100,000  
 4  \$100,000 - less than \$1 mil  
 5  \$1 mil - less than \$5 mil  
 6  \$5 mil - less than \$10 mil  
 7  \$10 mil or more

**PART B – LEGAL STRUCTURE**

**4. Choice of structure**

4.1 Please indicate how important the following reasons were for choosing a company as the form of incorporated legal structure rather than, for example, an incorporated association or co-operative?

*(indicate your response by circling one number - numbers '1' and '4' both represent very definite positions, the numbers in between represent intermediate positions.)*

(1) not at all important, (4) very important, (0) don't know

- requirement of grant maker 1 2 3 4 0
- organisation's size 1 2 3 4 0
- national or multi-state organisation 1 2 3 4 0
- public perception and status 1 2 3 4 0
- taxation/financial advice received at the time 1 2 3 4 0
- legal advice received at the time 1 2 3 4 0
- scale of trading activities 1 2 3 4 0
- preferred to deal with Australian securities and Investment Commission rather than State regulator 1 2 3 4 0

other important reasons *(please specify)*.....  
 .....  
 .....  
 .....

4.2 From your experience with this company, would you say that the choice of this form of legal structure (that is, a company):

(1) strongly disagree, (4) strongly agree, (0) can't say

- has caused difficulties 1 2 3 4 0
- is readily understood by the company's directors 1 2 3 4 0
- is readily understood by the company's members 1 2 3 4 0
- is readily understood by those dealing with the company (such as funding bodies) 1 2 3 4 0
- has added significant expense 1 2 3 4 0
- involves manageable reporting obligations to members and Australian Securities and Investments Commission 1 2 3 4 0

(4.2 continued)

- has been sufficiently flexible to meet the organisation's needs over time (for example, if a merger has been necessary) 1 2 3 4 0

- has added a lot of paperwork 1 2 3 4 0

other comments.....  
 .....  
 .....  
 .....

**5. Group structure**

5.1 Does the company have any subsidiary companies or related entities? (Note: For the purposes of this question, a division within the company is not a related entity.)

yes  no

5.2 If 'yes', please indicate the number of each of type:

- 1 ..... proprietary limited company (Pty Ltd)
- 2 ..... public company (Ltd)
- 3 ..... trust/foundation
- 4 ..... parent company
- 5 other *(please specify)*.....

**PART C – STAKEHOLDERS**

**6. Who are the company's stakeholders?**

By the word 'stakeholder' we mean those groups of people, other organisations, or even an individual who have a direct and legitimate interest in monitoring the activities and good management of the company. By way of example, the company's members, clients to whom the company provides services or, in the case of a church-based company, the church to which it is affiliated.

Bearing this definition in mind, please indicate;

- who you regard as the company's most important stakeholder(s) (up to a maximum number of three)

- weight their importance out of 100 (for example, 1 = 40%, 2 = 30%, 3 = 30% - total 100%), and

- complete the associated questions for each of them.

**6.1.1 Stakeholder A**

(description).....  
 % importance.....

6.1.2 Does the company provide any regular report to this stakeholder?

yes  no

6.1.3 If 'yes', is it as a result of a mandatory obligation or does the company provide it voluntarily?

voluntary  mandatory

6.1.4 Has there been any significant tension between this stakeholder (or any individual within the group) and the company OR between this stakeholder and any other stakeholder in the company?

yes  no

6.1.5 If 'yes', please explain the nature of the tension and, if it has been resolved, how it was resolved.

.....  
.....  
.....  
.....  
.....

6.2.1 Stakeholder B

(description).....  
% importance.....

6.2.2 Does the company provide any regular report to this stakeholder?

yes  no

6.2.3 If 'yes', is it as a result of a mandatory obligation or does the company provide it voluntarily?

voluntary  mandatory

6.2.4 Has there been any significant tension between this stakeholder (or any individual within the group) and the company OR between this stakeholder and any other stakeholder in the company?

yes  no

6.2.5 If 'yes', please explain the nature of the tension and, if it has been resolved, how it was resolved.

.....  
.....  
.....  
.....  
.....

6.3.1 Stakeholder C

(description).....  
% importance.....

6.3.2 Does the company provide any regular report to this stakeholder?

yes  no

6.3.3 If 'yes', is it as a result of a mandatory obligation or does the company provide it voluntarily?

voluntary  mandatory

6.3.4 Has there been any significant tension between this stakeholder (or any individual within the group) and the company OR between this stakeholder and any other stakeholder in the company?

yes  no

6.3.5 If 'yes', please explain the nature of the tension and, if it has been resolved, how it was resolved.

.....  
.....  
.....  
.....  
.....

**PART D – BOARD COMPOSITION AND EXPERIENCE**

We are interested in the 'make-up' of the company's Board – the demographics of the Board and their experience and skills. This may highlight differences between 'not-for-profit' and 'for-profit' companies.

7. Board composition

7.1.1 How many directors are currently on your Board?

..... (write the total number of directors)

7.1.2 Are there currently any unfilled Board positions?

yes  no

7.1.3 If 'yes', what is the total number of current, unfilled Board positions?

..... (write the total number of current, unfilled Board positions)

**Non-executive directors**

7.2.1 Of the total number of directors (as stated in question 7.1.1), how many are non executive directors (that is, those directors who are not employees of the company)?

..... (write the total number of non-executive directors)

7.2.2 Are any of the non-executive directors paid directors' fees (other than out-of-pocket expenses) by the company?

yes  no

7.2.3 If 'yes', please give a general indication of the total annual fees paid to the non-executive director(s) in the company's last financial year.

\$.....

7.2.4 If 'no', do you believe any of the company's non-executive directors should be paid directors fees?

yes  no

7.2.5 Are any of the non-executive directors or their associates paid by the company for other work, for example, for legal or accounting advice?

yes  no

7.2.6 If 'yes' please give a general indication of the type of work undertaken.

.....  
 .....  
 .....  
 .....

**Executive directors**

7.3.1 Of the total number of directors (as stated in question 7.1.1), how many are executive directors (that is, those directors who are employees of the company)?

..... (write the total number of executive directors)

7.3.2 Of these executive directors, how many are full-time employees and how many are part-time employees? Please write a number, including '0' if applicable, for EACH.

..... full-time ..... part-time

7.3.3 Is the Chairperson of your Board an executive director (that is, company employee) or non-executive director (that is, not a company employee)?

executive director OR  non-executive director

7.3.4 Is the Chief Executive Officer (or equivalent) a director (that is, a voting member of the Board rather than a person who attends Board meetings because of their position)?

yes, a Director OR  no, not a Director

7.4 Are you (that is, the person completing this questionnaire on behalf of the company):

- the company's chief executive officer?  yes  no  
 (tick 'yes' if you are the company's most senior employee even if you have a different title.)

If 'no', please describe your position.....

.....

- a director?  yes  no

**How are Board members chosen?**

7.5.1 Of the total number of directors currently appointed, how many are: (please put a number or zero on each line.)

..... appointed by members

..... appointed by an organisation or individual (for example, pursuant to a clause in the company's constitution)

..... appointed by the Board (for example, to fill a casual vacancy or co-opted for a particular skill)

7.5.2 In your experience with this company, are Board elections contested?

1  always                      2  usually  
 3  sometimes                    4  rarely

7.5.3 Is any director a substantial donor or an associate of a substantial donor?

yes  no

7.5.4 If 'yes', how many directors?

..... (write the total number)

7.6.1 Assume that members are one of the company's stakeholders and that all directors represent the interests of members. Has any director been appointed primarily for the purpose of representing the interests of any of the company's other stakeholders (including, but not limited to, other non-member stakeholders listed in question 6)?

yes  no

7.6.2 If yes, please specify how many directors for which of the stakeholder(s).

- number of directors..... stakeholder.....

- number of directors..... stakeholder.....

- number of directors..... stakeholder.....

7.6.3 Is there a clause in the company's constitution that provides for certain interests to be represented on the Board?

yes  no

(if 'yes', it would be appreciated if you could enclose a photocopy of the clause in the Reply Paid envelope with this questionnaire.)

7.7.1 Has any director been appointed primarily for the purpose of representing the interests of a substantial supplier or purchaser of goods/services to/from the company?

yes  no

7.7.2 If 'yes', please specify how many directors for which goods/services.

- number of directors..... goods/services.....

- number of directors..... goods/services.....

7.8.1 Please complete the following information about the Board. Please write a number (including '0' if applicable) on EACH line for (A) and (B) to show the number of board members of each gender, age group and background.

A. female
..... 18 - 24 yrs ..... 25 - 39 yrs
..... 40 - 59 yrs ..... 60 - 72 yrs
..... 72+ yrs
..... English not first learnt language
..... Aboriginal or Torres Strait Islander or descendant

AND

B. male
..... 18 - 24 yrs ..... 25 - 39 yrs
..... 40 - 59 yrs ..... 60 - 72 yrs
..... 72+ yrs
..... English not first learnt language
..... Aboriginal or Torres Strait Islander or descendant

7.8.2 Has there ever been difficulty recruiting Board members?

yes  no

7.8.3 If 'yes', why?.....

.....
.....
.....
.....
.....
.....

7.9.1 Has there ever been difficulty retaining Board members?

yes  no

7.9.2 If 'yes', why?.....

.....
.....
.....
.....
.....
.....

7.10.1 Within the last five years, has a director ever been removed from their position on the Board before the expiration of their term? (For example, by a resolution of the members.)

yes  no

7.10.2 If 'yes', by whom?.....

.....
.....
.....

7.10.3 Why?.....

.....
.....
.....
.....
.....
.....
.....
.....
.....
.....

**8. Board experience, skills and knowledge**

8.1 How would you describe the experience and skills of your Board as a group in each of the following areas:

(1) very inadequate, (4) very adequate, (0) not relevant

- understanding of consumer/client perspective 1 2 3 4 0
- management/governance 1 2 3 4 0
- law 1 2 3 4 0
- fundraising 1 2 3 4 0
- understanding of carer perspective 1 2 3 4 0
- government relations 1 2 3 4 0
- accounting/finance 1 2 3 4 0
- social work 1 2 3 4 0
- education 1 2 3 4 0
- medical 1 2 3 4 0
- marketing/media 1 2 3 4 0
- human resources 1 2 3 4 0
- information technology 1 2 3 4 0
- business/community partnerships 1 2 3 4 0
- investment 1 2 3 4 0
- philanthropic 1 2 3 4 0

other (please specify any other skill that you think is necessary for your Board) .....

.....

.....

.....

8.2 Do you believe that the Board members understand that, under the Corporations Act, they can be personally liable - for example, if they act without sufficient care and diligence or if they allow the company to continue to trade when it is unable to pay its debts? Please tick ONE box and, if possible, add a comment about the level of the Board's awareness and knowledge of their legal duties as directors.

- 1  all Board members aware
- 2  most of the Board members aware
- 3  only some of the Board members aware
- 4  none of the Board members aware

comment.....

.....

.....

.....

**PART E – BOARD STRUCTURE AND PROCEDURES**

**9. Board structure**

9.1.1 Does a group of directors, or a board committee, deal with management matters on behalf of the Board?

- yes  no

9.1.2 If 'yes', how often does this group meet? (please tick only one box)

- 1  daily 2  weekly 3  monthly
- 4  other (please specify) .....

9.2 Does the Board have any other committees?

- yes  no

9.3 If 'yes', please specify.....

.....

**10. Board procedures**

10.1 How often does the full Board of Directors meet? (please tick only one box)

- 1  fortnightly (or more often) 2  monthly
- 3  every two months 4  quarterly
- 5  twice yearly 6  yearly
- 7  other (please specify) .....

10.2 Are Board meetings ever held by any of the following means:

- telephone conference  yes  no
- video conferencing  yes  no
- decision made by email or fax, then ratified at next Board meeting  yes  no
- other electronic means (please specify) .....

10.3 Please indicate which, if any, of the following papers are distributed before Board meetings:

(1) never, (2) one in four times, (3) two in four times, (4) always

- previous minutes 1 2 3 4
- report on activities 1 2 3 4
- financial report 1 2 3 4
- other (please specify) .....

10.4 Typically, how long do Board meetings take?

(please tick only one box)

- 1  less than 1 hour
- 2  1-2 hours
- 3  more than 2 hours
- 4  other (please specify) .....

10.5 Typically, how many Directors attend Board meetings?

(please tick only one box)

- 1  less than 1/4
- 2  1/4 to less than 1/2
- 3  1/2 to less than 3/4
- 4  3/4 or more

10.6 How does the Board decide most issues?

(please tick only one box)

- consensus
- mix of consensus and voting
- consensus, but as a matter of procedure, vote always taken
- vote

10.7.1 Are you aware of any situation in the past five years where an actual or potential conflict of interest has arisen between the interests of a director (or a stakeholder whose interests they represent) and the interests of the company?

- yes
- no

10.7.2 If 'yes', what procedure was followed?.....

.....  
 .....  
 .....  
 .....

10.8 When a new director is appointed, indicate which (if any) of the following occurs:

- receive a copy of the last annual report  yes  no
- receive a copy of the company's constitution  yes  no
- are briefed by senior staff  yes  no
- receive a copy of strategic and business plans  yes  no
- go on site visits  yes  no  not applicable

other (please specify).....  
 .....  
 .....

10.9.1 Overall, do you feel your company operates 'formally' enough in terms of its processes?

- 1  yes
- 2  no
- 3  not sure

10.9.2 If not, why not.....

.....  
 .....  
 .....

10.10.1 Does the company pay for directors' and officers' insurance?

- yes
- no

10.10.2 If 'no', is directors' and officers' insurance provided by the government?

- yes
- no

10.10.3 During the last five years, are you aware of any actual or threatened legal claims against any of the company's directors for a breach of legal duty?

- yes
- no

10.10.4 If 'yes', please specify the general nature of the claim(s)

.....  
 .....  
 .....

10.10.5 If any directors' fees are paid, do the company's accounts disclose this fact?

- yes
- no

11 Organisational role

We are interested in your views on the role of the Board in the company. Please indicate how much you agree or disagree with the following statements about the Board's main role within your company.

(1) strongly disagree, (4) strongly agree, (0) not sure

- to act as a general advisory body 1 2 3 4 0
- to determine strategic directions & monitor performance against plan 1 2 3 4 0
- to participate in the company's management and/or its operations 1 2 3 4 0
- to guide and monitor the company's financial position 1 2 3 4 0

(11 continued)

- to bring together individuals with sufficient reputation/connections to assist with fundraising & grant applications 1 2 3 4 0
- to monitor and advise on government policy environment 1 2 3 4 0
- to represent the interests of particular stakeholders 1 2 3 4 0
- to appoint the chief executive officer and to review their performance 1 2 3 4 0

other (please specify).....  
 .....  
 .....

**12 Company secretary**

12.1 Is the company secretary (appointed for the purposes of the Corporations Act): (please tick only one box)

- 1  a director
- 2  an employee
- 3  a person from outside the company

12.2 Does the company secretary have any experience or training in: (you may tick more than one box or none at all)

- 1  law    2  accounting    3  management
- other (please specify).....

**13 Advice received**

13.1.1 Has the company received any free legal advice?

- yes     no     don't know

13.1.2 If 'yes', was the advice obtained as a result the actions/connections of a Board member appointed to the Board primarily for their legal expertise?

- yes     no     don't know

13.2.1 Has the company received any free accounting, financial or investment advice?

- yes     no     don't know

13.2.2 If 'yes', was the advice obtained as a result the actions/connections of a Board member appointed to the Board primarily for that expertise?

- yes     no     don't know

13.3 Have directors received any information about their legal obligations as directors?

- yes     no     don't know

13.4 Do the company's auditors charge for their services (other than for out-of-pocket expenses)?

- yes     no     don't know

**PART F – REGULATORY FRAMEWORK**

**14 Regulation**

Recently a Federal Government Inquiry has recommended "the establishment of an independent administrative body to oversee charities and related entities" (see p11 and Chapter 32 of the Report of the Inquiry into the Definition of Charities and Related Organisations, June 2001, available at <http://www.cdi.gov.au>). To date, the Government has made no specific response to this recommendation, but we are interested in your views.

14.1 What information (if any) do you believe should be available to the public about your organisation?

- 1  no information

OR (tick one or more boxes)

- 2  name and registered office
- 3  summary financial information
- 4  fully audited accounts
- 5  if total public funding is over \$100,000, disclosure of all sources of public funding
- 6  copy of constitution
- 7  description of activities
- 8  specific financial information regarding remuneration of directors and senior management
- 9  attendance of directors at Board meetings
- 10  marketing expenditure compared with fundraising receipts
- 11  other (please specify).....

If possible, brief reason for this answer?.....  
 .....  
 .....  
 .....





**PHILANTHROPY**  
*Australia*

*Questionnaire on company law issues affecting*  
**NOT-FOR-PROFIT COMPANIES**



**THE UNIVERSITY OF**  
**MELBOURNE**

9th April, 2002

Dear Chief Executive Officer,

In mid-March you should have received a (yellow) questionnaire and a reply paid envelope from us. The questionnaire was sent to all companies limited by guarantee that appeared on the public register of companies as at 1 March 2002.

**If you have not yet returned the questionnaire, we would be very grateful if you could do so within the next week.**

If you need another copy of the questionnaire or did not receive a reply paid envelope, please call or email Susan Woodward: (03) 8344 6938, s.woodward@unimelb.edu.au. The postal address for the return of the questionnaire is Susan Woodward, Law School, The University of Melbourne, Victoria, 3010.

It is vital that we receive as many responses as possible so that we can document accurately the characteristics and needs of not-for-profit companies. As stated in the letter that accompanied the questionnaire, the questionnaire is confidential and the data will only be used for research purposes.

We hope you are able to support this project.

Yours sincerely,

Ms Elizabeth Cham – National Director, Philanthropy Australia Inc.  
(ph (03) 9620 0200 fax (03) 9620 0199)

Prof Ian Ramsay and Ms Susan Woodward –  
Centre for Corporate Law and Securities Regulation  
The University of Melbourne (ph (03) 8344 6938 fax (03) 8344 5285)

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## APPENDIX 4: OVERSEAS DISCLOSURE FORMS

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1. Example of Standard Information Return – United Kingdom
2. Sample Standard Information Return – Canada
3. Sample Charity Annual Return – New Zealand

### *Box 6.7: Example of a Standard Information Return*

#### Achievement against objectives

What were your objectives for last year and how far did you achieve them?

What are your objectives for the coming year and *how will* you achieve them?

#### Impact

How do *you* measure your impact? What are your success measures?

#### Performance Improvement

Do you use any of the following recognised quality tools? (tick boxes)

Social Audit; Excellence Model; PQASSO; Investors in People; *etc.*

#### Stakeholder Involvement

Whom do you see as your main stakeholders? **How** do you ensure accountability to them? How do you listen to and act *on* their views?

#### Governance

How are your trustees selected **and** equipped for their role?

#### Fundraising

What fundraising activities do you undertake and why?

Fundraising ratio for the last year **together** with explanatory text

Fundraising ratio, averaged over last five years together with explanatory text

#### Campaigning

What **sort** of campaigning work, if any, do you undertake? Are *you a* member of any campaigning alliances (if so which)?

#### Trading

Do you own any subsidiary trading companies or are you involved in any significant joint ventures with other organisations (**not-for-profit**, public or private)? What were their activities, turnover and profits?

#### Reserves and Investment

What is your investment strategy, **including** your policy on ethical investment?

What is your reserves policy and *what are* your reserves currently?

### *Transparency of investment policies*

6.13 Currently, pension fund trustees must disclose their ethical investment stance to their members. However, donors to, or funders of, a charity have no rights to know whether that charity chooses to invest its assets ethically or not - despite the fact that these assets can often be very substantial. Ethical investment is a

matter of some public interest: a recent NOP survey<sup>44</sup> shows that over 40% of the members of the public surveyed would prefer to support charities who invest ethically, while 14% would only support charities which did so. Disclosure about the way in which assets are invested, as well as the size of those assets, should form an important part of the Standard Information Return.

<sup>44</sup> The Guardian Society (2001) *The goodness business*. 27th June.



C4 Did the charity carry on programs, directly or indirectly, outside Canada? ..... 2100  Yes  No  
 If yes, were any carried out:  
 by employees or volunteers of the charity? ..... 2110  Yes  No  
 under agency agreement, contract, joint-venture, or similar arrangements? ..... 2120  Yes  No  
 through gifts to qualified donees? ..... 2130  Yes  No  
 by other means? ..... 2140  Yes  No

C5 For programs the charity managed directly, outside of Canada, list the countries or regions where programs were carried on. Do not include countries or regions where programs were managed by a qualified donee.

--	--	--	--	--	--

C6 Did the charity issue scholarships, bursaries, awards, prizes, or honoraria to an individual during the fiscal period? ..... 2300  Yes  No

C7 A charity may pursue political activities that are non-partisan, related to its charitable purposes, and limited in extent. During the fiscal period, did the charity carry out political activities or provide assistance to another organization to carry out political activities? (See the guide for information on political activities.) ..... 2400  Yes  No

C8 If the charity carried on fundraising activities, check all fundraising methods that it used during the fiscal period.

2500 <input type="checkbox"/> Advertisements/posters/flyers/radio or TV commercials	2560 <input type="checkbox"/> Fundraising dinners/galas/concerts	2620 <input checked="" type="radio"/> Telephone solicitations
2510 <input checked="" type="radio"/> Auctions	2570 <input type="checkbox"/> Fundraising sales (e.g., cookies, chocolate)	2630 <input type="checkbox"/> Tournaments/sporting events
2520 <input type="checkbox"/> Bingo/casino nights	2580 Mail campaigns	2640 <input checked="" type="radio"/> Walk-a-thons/bike-a-thons (etc.)
2530 <input type="checkbox"/> Collection plates/boxes	2590 Planned-giving programs	2650 <input type="checkbox"/> Other
2540 Door-to-door solicitation	2600 <input type="checkbox"/> Targeted corporate donations/sponsorships	2660 Specify:
2550 <input checked="" type="radio"/> Draws/lotteries	2610 <input checked="" type="radio"/> Targeted contacts	

C9 Did the charity use incentive-based compensation (e.g., bonuses, commissions, finder's fees, honoraria) for fundraisers? ..... 2700  Yes  No  
 If yes, were these incentives paid to:  
 contracted fundraisers? ..... 2710  Yes  No  
 staff or volunteers? ..... 2720  Yes  No

C10 Did the charity charge fees for, or otherwise receive regular revenue from goods, services, or the use of the charity's assets? ... 2800  Yes  No

C11 Did the charity make gifts to qualified donees? ..... 2900  Yes  No  
 If yes, you must attach a list with the name of each qualified donee and its location, BN/registration number, the total amount of the gift for the fiscal period, the amount, if any, of specified gifts, and whether or not it is an associated charity. List the qualified donees in the order of the total amount of the gifts made, starting with the largest. Use the worksheet included in the guide or a sheet with the same information in the same format and attach it to this return.

C12 If the charity received non-cash gifts (gifts in kind) for which it issued tax receipts, check all the types of gifts that apply.

3000 <input checked="" type="checkbox"/> Artwork/wine/jewellery	3040 <input checked="" type="radio"/> Cultural property	3080 Publicly-traded securities/mutual funds
3010 Building materials	3050 <input checked="" type="checkbox"/> Ecological property	3090 Privately-held securities
3020 <input checked="" type="checkbox"/> Clothing/furniture/food	3060 <input checked="" type="radio"/> Machinery/equipment (including computers/software)	3100 <input type="checkbox"/> Other
3030 <input checked="" type="radio"/> Vehicles	3070 <input checked="" type="radio"/> Hedge funds/life insurance policies	3110 Specify:

**Section D - Compensation**

Compensation includes all forms of remuneration (e.g., salaries, fees, and honoraria) and benefits (e.g., personal use of a car or office space).

D1 How many permanent, full-time, compensated positions did the charity have in the fiscal period? ..... 3600

D2 How many positions indicate the number of positions in each of the following annual compensation categories. Include only those positions that are permanent, full-time positions.

3700  \$1-\$39,999    3710  \$40,000-\$79,999    3720  \$80,000-\$119,999    3730  \$120,000 and over

D3 On average, how many part-time or part-year employees did the charity employ in the fiscal period? ..... 3800

D4 What was the total expenditure on compensation for part-time or part-year employees in the fiscal period? ..... 3850 \$ ..... 00

D5 Did the charity compensate any of its directors/trustees or like officials, during the fiscal period?..... 3900  Yes  No

D6 Except for compensation, did the charity, directly or indirectly, transfer any part of its income or assets to individuals or organizations not at arm's length to the charity? ..... 3950  Yes  No

**Section E - Financial Information**

© Please attach a copy of the charity's financial statements to this return..... 4000 Attached

© May we make the attached financial statements available to the public?..... 4010  Yes  No

© Was the financial information reported below prepared on an accrual or cash basis? 4020  Accrual  Cash



Assets		Liabilities					
..	and	-	4100	•	and accrued liabilities	4300	..00
	receivable	length	4110			4310	..00
	receivable	others	4120		payable owing	4320	..00
		length parties	4130			4330	..00
			4140		Total liabilities (add lines 4300 to 4330)....	<b>M</b>	..00
Inventories			4150				
			4160				
			4170				
	oi		4200				..00

Please show figures to the nearest single dollar. Do not show cents. See the guide for an explanation of the terms.

Revenue		4500	..00
		4510	..00
	4510		..00
Total other gifts		4530	..00
Revenue from federal government	4540		..00
Revenue from provincial/territorial governments	4550		..00
Revenue from municipal/regional governments	4560		..00
Total revenue from government (add lines 4540, 4550, and 4560)		4570	..00
Interest and investment income		4580	..00
Proceeds from disposition of assets	gross	4600	..00
	net	4610	..00
Rental income (land and buildings)		4620	..00
Memberships, dues, and association fees (non tax-receipted)		4630	..00
		4640	..00
		4650	..00
Total revenue (add lines 4500, 4510, 4530, 4570, 4580, and 4600 to 4650)			..00
Expenditures (Enter all expenditures, whether or not on charitable programs)			
Advertising and promotion		4800	..00
Travel and vehicle		4810	..00
Interest and bank charges		4820	..00
Licences, memberships, and dues		4830	..00
Office supplies and expenses		4840	..00
Occupancy costs		4850	..00
Professional and consulting fees		4860	..00
Education and training for staff and volunteers		4870	..00
Salaries, wages, benefits, and honoraria		4880	..00
Donated and purchased supplies and assets expensed for the fiscal period		4890	..00
Amortization of capitalized assets		4900	..00
Research grants and scholarships as part of charitable programs		4910	..00
Other expenditures		4920	..00
Total expenditures before gifts to qualified donees (add lines 4800 to 4920)			..00
Total charitable programs expenditures included in line 4950	5000		..00
Total management and administration expenditures included in line 4950	5010		..00
Total fundraising expenditures included in line 4950	5020		..00
Total political activity expenditures included in line 4950	5030		..00
Total other activity expenditures included in line 4950	5040		..00
Total gifts to qualified donees		5050	
Total expenditures (add lines 4950 and 5050)		5100	..00

We will calculate your disbursement quota based on the information you provide on this return.  
If you want to do your own calculation, see the disbursement quota worksheet in the guide.

**Additional Information**

- F1 What were the total expenditures on programs outside Canada during the fiscal period, excluding gifts to qualified donees? .... 5400 \$ .00
- F2 If the charity retained contracted fundraiser(s), enter:
- a. the gross revenues collected by the fundraiser(s) on behalf of the charity ..... 5450 \$ .00
  - b. the amounts paid to and/or retained by the fundraiser(s) ... . 5460 \$ .00
  - c. the net fundraising revenue received by the charity (line 5450 minus line 5460) ..... 5470 \$ .00
- F3 If the charity has written permission to accumulate property, enter:
- the amount accumulated for the fiscal period, including income earned for the fiscal period on previously accumulated funds. . 5500 \$ .00
  - the amount disbursed for the fiscal period for the specified purpose we have granted permission for ..... 5510 \$ .00
  - the amount deemed to be a tax-receipted gift for the fiscal period (See the guide) ..... 5520 \$ .00
- F4 Of the tax-receipted gifts received by the charity for the fiscal period, enter:
- the total amount of tax-receipted non-cash gifts (gifts in kind) ..... 5600 \$ .00
  - the total amount of tax-receipted tuition fees ..... 5610 \$ .00
  - the total amount of tax-receipted ten-year gifts ..... 5620 \$ .00
  - the total amount of tax-receipted bequests ..... 5630 \$ .00
- F5 If the charity received ten-year gifts or bequests in a previous fiscal period and used them to reduce its disbursement quota, enter the amount, if any, spent in the fiscal period. (See the guide.) ..... 5700 \$ .00j
- F6 If the charity is taking a special reduction, which we have pre-approved, to its disbursement quota, enter the special reduction amount for the fiscal period. (See the guide.) ..... 5750 \$ .00
- F7 Did the charity acquire a non-qualifying security or allow a donor to use any of the charity's property under the circumstances described in the guide during the fiscal period? (See the guide) ..... 5600  Yes  No

**Section G - For Foundations On**

Note: See the guide for an explanation of the terms and requirements of this section.

- G1 In the fiscal period, did the foundation acquire control of a share-capital or for-profit corporation? . . . . . 6000  Yes  No
- G2 Indicate the average value of investment property not used for charitable programs or administration during:
- the 24 months before the beginning of the fiscal period ..... 6050 \$ .00
  - the 24 months before the end of the fiscal period ..... 6060 \$ .00
- G3 Did the foundation incur debts at any time during the fiscal period other than for current operating expenses, in purchasing or selling investments, or in administering charitable programs? ..... 6100 Yes  No
- G4 For private foundations only: At any time during the fiscal period, did the foundation hold any shares, rights to acquire such shares, or debts owing to it that meet the definition of a non-qualified investment? ..... 6150  Yes  No

**Section H - Certification**

H1 To be completed by a director/trustee or like *official* of the charity. It is a serious offence under the Income Tax Act to provide false or deceptive information.  
I certify that the information given on this form, the basic information sheet, and any attachments is, to the best of my knowledge, correct, complete, and current.

Name (please print)  
Signature

Position in charity  
Date signed

**Section I - Confidential Data**

I1 Physical location (address) of the charity (Do not use rural route or post office box *numbers*.)

Number, street, apt. no., or lot and concession no.  
City  
Province or territory and postal code

Postal code:

I2 Location of the charity's books and records

Number, street, apt. no., or lot and concession no.  
City  
Province or territory and postal code

Postal code:

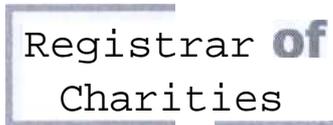
I3 Name and address of the person who completed this return

Name  
Firm name (if applicable)  
Number, street, apt. no., R.R. no., or P.O. box no.  
City  
Province or territory and postal code

Postal code:

Phone number ( )

Fax number ( )



## Charity Annual Return

For the year ended 30 June [03] (including balance dates ending in the 03 calendar year).

Information in sections A, B and C has been taken from your registration form or last annual return. Please update any of this information to highlight any change in your organisation or its activities.

This information will be entered onto the computerised Registrar of Charities database. The information that you have supplied will be publicly available at our office and on this website.

### A. Contact Details

- 1 Please give the legal name by which the organisation is known.
- 2 Please give any other names by which the organisation is known (including any acronyms).
- 3 Is the organisation a branch, subsidiary section, parish, congregation or other internal division of another registered charity or other organisation?  
 Yes  No

If Yes, please provide details below:

- 4 Street address:



Mailing address (if different from street address):

Telephone:

- 7 Fax:

- \$ Contact person (name and position e.g. secretary):

- 9 Contact person's email address:
- 10 Please supply a list of the names and addresses of all members of the governing board or governing authority of the organisation (e.g. trustees, parish priest etc). Type each part of the name and address on a new line e.g.:
- John Smith  
1/10 Main Street  
GORE

## B. Charitable Purpose

- 11 Year ~~in which the org~~ organisation first operated or intends to operate:
- 12 Are you registered under any other Act of Parliament, and if so what is your registration number?
- Company number:
- IRD number:
- Charitable Trusts Act number:
- Incorporated Societies Act number:
- Maori Land Court number:
- Other, please specify:
- 13 What are the areas of your main charitable purposes and activities? Select all boxes that apply.
- 14
- |   |  |
|---|--|
| <input type="checkbox"/> Education                | <input type="checkbox"/> Health                |
| Religion  | Indigenous persons                             |
| Poverty   | <input type="checkbox"/> Employment            |
| Disaster relief                                   | Crime prevention                               |
| <input type="checkbox"/> People with disabilities | <input type="checkbox"/> Science               |
| Public work and utilities                         | <input type="checkbox"/> Research              |
| Community development                             | <input type="checkbox"/> Culture               |
| Aged persons                                      | Environment                                    |
| Young persons                                     | <input type="checkbox"/> Animals               |
| Family services                                   | <input type="checkbox"/> Other (see 15. below) |
| Housing   |  |
- 15 If you selected Other at 14. above please describe your main charitable purposes and activities:

## C. Activities

Please provide details of the main activities that will be carried out in order to further the objects in the entity's governing document.

16a Object 1:

16b Activities:

17a Object 2:

17b Activities:

18a Object 3:

18b Activities:

19a Object 4:

19b Activities:



20 Add information about any additional objects and activities:

21 Name the charities that will benefit on a winding up of the organisation:



- 22 Does the entity operate outside New Zealand?  
 Yes  No
- 23 Does the entity fund any activities outside New Zealand?  
 Yes  No
- 24 Do you intend to raise money from the public?  
 Yes  No
- 25 Do you intend to provide services under government contract?  
 Yes  No

**D. Balance Date (Being the End of Your Financial Year)**

26 Your balance date (dd/mm/yy):  
/ /

**E. Annual General Meeting**

27 Date of last annual general meeting if applicable (dd/mm/yy):  
/ /

**F. Income**

28 Income from:

Investments: New Zealand company dividends	
All other investments (excluding New Zealand company dividends)	
Subtotal income from investments	<input type="text"/>
Donations from the public	
Trading activities	<input type="text"/>
Grants from other registered charities	
• Government contracts or grants	
• Income from members (including subscriptions)	
Other	
Total	<input type="text"/>

**G. Outgoings**

29 Note: Take all figures from your accounts and allocate overheads such as administration and depreciation as appropriate to your organisation.

Service delivery and activity costs (including overhead and administration costs)

Total grants made within New Zealand

Grants made <i>within</i> New Zealand to other registered charities	
Grants made overseas	<input type="text"/>

Fundraising costs

Retained surplus (deficit):

Total

**H. Net Worth**

30 Current assets

*Long term assets*

Total assets

Current liabilities

*Long term liabilities*

Total liabilities

Balancing figure/Equity

**I. Benefits**

32 Have any of the following benefited in any way, directly or indirectly from the entity?

- a. Trustees
- b. Others involved in managing the organisation
- c. A relative or business associate of a. or b.
- d. A partner, relative or business associate of a partner

 Yes  No

If yes, specify amount:

**J. Declaration**

[If filing online, you will complete this section when the form is returned to you.]

33 I declare that the above information is true and correct and that the charitable objectives outlined above have been actively pursued throughout the relevant year.

Signed:

Date:

Submit Clear

[CHARITY REGISTRATION FORM](#) [HELP WITH REGISTRATION](#) [UPDATE CHARITY DETAILS](#) [CHARITY ANNUAL\\_RETURN](#)

[HOME](#) [CONTACT THE REGISTRAR](#) [CHARITY POLICY](#)

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## APPENDIX 5: COMPARATIVE TABLE INCORPORATED ASSOCIATIONS LEGISLATION

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The original draft of this comparative table was prepared by Mrs Sally Sievers as at June 2003.

REFORMING NOT-FOR-PROFIT REGULATION

	ACT	NT	NSW	QLD	SA	TAS	VIC	WA
<b>ELIGIBILITY</b>								
Specific definition		4(1) (admin power to certify others)			18(1)	2(1)(a), (b) (admin power to declare others to be eligible)		4(1) (admin power to approve others)
Non-specific	14(1)		7(1)	2, 5(1)			3(1)	
Definition of gain	5		4	4(1)	18(6)		3(2)	4(4)
Prohibition on trading	14(2), 109 (penalty)	4(1)	7(2)(a), 66 (penalty)	5 (prohibition on financial gain)	18(5)	2(1), 21(2)	10(4A), 51(1)	4(2)
Exemptions	15	4(1) (trading assoc)	4(h), Reg 10 (charities)	5			51(4)-(6)	
<b>INCORPORATION PROCESS</b>								
Prior notice/advertisement of intention to apply		5-6, 25A-25B (trading assoc)		10-11 (may be required in specific cases)				6-7
Reservation of name	37		13		53A			
To include denoter of NFP status in name	36	9(2), 9A, 25L (trading assoc)	12(3)	29-33 (unless exempt)	20(3)(a)(ii)	9(3)-(4)	12, 12A	10(b)
Procedure	18	7, 25C (trading assoc)	8-9	6-9	19	7-8	4-5, reg 5A	5-7
As of right	19		10(1)	12 (power to grant OR refuse)	20		7(1)	9(1)
Some exceptions			10(2) (scale or nature of activities etc)	10-13	20(2)		7(2)	9(2)

Appendix - Comparative Table Incorporated Associations Legislation

	ACT	NT	NSW	QLD	SA	TAS	VIC	WA
Discretionary		8, 25D (trading assoc)				8(1)		
Effect of incorporation	22	9(1), 25J (trading assoc)	15	21, 25	25	11-12, 21	14, 16	10, 13
Limited liability, etc	51	21	16	27	21(2)	27	15	12
Ultra vires	24		17-18,	26	27-28		17	15
Agency & other issues	47		31-36 (pre-reg contracts), 60-61 (agents, constructive notice)	28	26	20	19, 20 (pre-reg contracts, 41-42 (constructive notice)	14
Transfer of Incorporation				Part 11				
Directed / voluntary from Association to Company	82 (voluntary), 83 (directed)	25AR (trading associations only)	10(2), 56-58, regs 17-18 (directed/ voluntary to Corps Act or Co-op)	105K-105N (to co-op)	42		31AA (vol), 31AB (directed)-31A (includes co-op)	34 (to some other Act)
Voluntary to Association			48-49	105A-105J (co-op to Assoc.)		25A-25B	10-11, reg 5C	
<b>RESTRUCTURE, AMALGAMATION</b>								
Amalgamation	26-28		46	79-88	22	25	31, regs 5G-5H	
Branches				74-78				
<b>CONSTITUTION</b>								
Statement of objects/purposes	29		8-9, 19				5(1), 21(1)	

## REFORMING NOT-FOR-PROFIT REGULATION

	ACT	NT	NSW	QLD	SA	TAS	VIC	WA
Objects clauses	29	9(1)(b),	19(1)	46(2)(b), regs sch 3	23A(1)(a)			
Rules	31-32	15, 25U (trading assoc)	11	46	23		6, 21(2)	16-18
Minimum content	32, sch	25T (trading assoc)	11(1), Sch 1	Reg 7, regs sch 3	23A(1)(c)		6(a), sch	16, sch 1
Model rules	regs		Reg 9, regs sch 1	Reg 8, regs sch 4	67(2)(a) (none prescribed)	16, regs	21(2)(b), reg 29, sch 5	
As default rules	31(2)		19(2),(3)	47(1), 51		16(3)	21(3)	
Alteration of rules	33	16, 25V (trading assoc)	20	48, regs sch 3 cll 8-9	23A(1)(c) (to be included in rules), 24, 24A (by court order)	18	22	17, 19 (objects)
By special resolution	33(1)		20(1)	48(1)	24(1) (subject to rules)	18(1)	22(1)	17(1)
Proportion of membership required for special resolution	_ (70)		_ (5)	_ (2)	_ (3)	_ (23)	_ (29)	_ (24)
Administrative approval		16(3)		48(5)-(8)	24(5) (name only)	10(2) (name), 18(4) (objects)	44(2)-(4)	18 (name), 19 (objects)
No effect until lodged	33(5)	25V(4)(5)-25Y (trading assoc)	20(3)	48(8), 49 (no effect unless approved)	24(7) (name only)	18(4)	22(2) (lodged for approval and approved)	17(2)
Rules take effect as contract	48		11(2)	71(1)	23(1)		14A(1)	
<b>MANAGEMENT</b>								
Committee/board structure is mandatory	60			60-61, 61A (eligibility)				
Public officer	57-58	12-14, 25R-25S (trading assoc)	22	65-67 (secretary)	56	14-15	24-28, reg 5E	

Appendix - Comparative Table Incorporated Associations Legislation

	ACT	NT	NSW	QLD	SA	TAS	VIC	WA
Registered office	121(1)(optional)			17			13A (registered address)	40 (lodging an address for service is optional)
Requirement of registered office to be open	121(1)							
AGM required	69		26	55-57	39 (prescribed assoc only)		30	23
Special resolution	70		5	2, 3	3	23	29	24
Removal of directors/committee members	63			64(1) (rules), 64(2)(automatic on death, bankruptcy conviction etc), regs sch 3 (to be included in rules)	30 (automatic on death, bankruptcy, conviction etc)			
Meetings			See sch 1 (to be included in rules)	See sch 3 (to be included in rules) and s 133 (irregularities)	23A(1)(c) (to be included in rules)	22A (10% of members may call a meeting)		
Technology permitted				63(2) (management c'ttee)				
Proxies permitted	To be in rules, Sch 1		To be in rules, Sch 1				To be in rules, Sch	
Voting procedure	To be in rules Sch 1		To be in rules, Sch 1				To be in rules, Sch	
Mandatory Insurance			42-45, reg 14	70				

REFORMING NOT-FOR-PROFIT REGULATION

	ACT	NT	NSW	QLD	SA	TAS	VIC	WA
Duties of Committee				63 (regular meetings)				
Fiduciary duties					39A		29A	
Duty to disclose certain interests	65				31-32		29B-29C	21-22
Insolvent trading			37-38		49AD			
Membership rights			To be in Rules, Sch 1			22A (10% of members may call a meeting)		
Judicial review	49-53			71-73			14A92)-(4)	
Natural justice	50			71(3)	40		14B(3) (grievance procedure)	
Oppression					61			
<b>DISCLOSURE</b>								
Registered office	121(2)-(3) (if it has a regd office)			17			13A (reg address)	40 (lodging an address for service is optional)
Change in Officers	59 (public officer) 62 (committee)	14 (public officer) 25S (trading assoc)	25 (public officer) 21A (register of committee members kept by public officer.)	68 (sec, pres, treasurer)	56(5) (public officer)	15 (public officer)	28 (public officer)	
Change in constitution/rules	33	16, 25V (trading assoc)	20(2)	48	24(2)	18(2)-(6)	22	17 (rules), 19(objects)



Appendix - Comparative Table Incorporated Associations Legislation

	ACT	NT	NSW	QLD	SA	TAS	VIC	WA
Notify any other changes	38 (name), 26-27 (amalgamation)	17 (name), 25Z (name of trading assoc)	14 (name)	35-38 (name)		10(2) (name)	13, reg 6 (name)	18 (name)
Financial records kept	71	25AG(1) (trading assoc)	28(1)(a)	Regs 9-10, regs schs 3 & 5	39C(all assoc), 35(1), reg 8 (prescribed assoc)	23A	30A	25
Annual report/return lodged	79	25(3) (balance sheet), 25AI(4) (balance sheet – trading assoc)	27	59(4) (unless exempted: 59(5)), reg 11	36, reg 9 (periodic return for prescribed assoc)	24B (unless exempt)	30(4), reg 5F, 30(4)(aa) (prescribed assoc)	
Financial report presented to members	73	25AI(3) (trading assoc)	26(6), 27(1)(b)	59(1)(c), regs sch 3 Pt 2	35(6) (prescribed assoc)		30(3)	26 (annual accounts)
Only concise/summary financial report lodged	79 (annual return)	25(3) (balance sheet), 25AI(4) (balance sheet – trading assoc)	27(1)	59(4), regs 11-12 (public may inspect: 59(6))			30(4) (prescribed assoc must lodge audited accounts)	
Financial reports to comply with Accounting Standards	76(3) (prescribed associations)				No, but see the standards required by s 37		Reg 7, sch (prescribed assoc)	
Financial reports audited	76 (prescribed associations)	25AI(2) (trading assoc)		59(1)(b) (must be independent but need not be registered auditor), regs sch 3 Pt 2	35(2) (prescribed assoc), 23A(1)(c) (to be included in rules of prescribed assoc)	24 (auditor or approved person, unless exempt)	30B (prescribed assoc, auditor or approved person )	

REFORMING NOT-FOR-PROFIT REGULATION

	ACT	NT	NSW	QLD	SA	TAS	VIC	WA
Minutes books			28(2)	Regs sch 3, cl 6-7	51			
Sliding scale	74, reg 12-13						3, reg 7	
Register of members –who has access?	67 (members)	25AF (trading assoc) open to public		18, reg 16 (public access)			Sch (to be in rules)	27 (members) 28 (rules) & 29 (record of office-holders) may also be inspected by members
Sources of funding (Fundraising Appeals Acts)	Sch 1 (to be included in rules)		Sch 1 (to be included in rules)				Sch 1 (to be included in rules)	
<b>EXTERNAL REGULATION</b>								
Investigation, etc	99-105	25AT-25AZD	67 (records)	119-120	10, 11, 62	24A	37C-37Q	39(3)-(7) (limited power)
Direction to migrate	83	25AR (trading assoc)	10(2), 56-58, regs 17-18		42		31AB	34
Cancellation of incorporation	93	23A-23G (dissolution by Registrar)	54-55, 55A-55b (vol)	93-94D, reg 14	44-49	34-36	36E-37	35
<b>FINANCIAL DIFFICULTIES</b>								
Compromise with creditors					40A			
Voluntary administration					40B			
<b>DISSOLUTION</b>								
Voluntary winding up	88		50	89	41(1)(b) (decl of solvency required: 41C)	32 (incorporates CA by reference)	33	30



Appendix - Comparative Table Incorporated Associations Legislation

	ACT	NT	NSW	QLD	SA	TAS	VIC	WA
Compulsory winding up	89-90	20, 25AP-25AQ (trading assoc)	51	90-91	41(1)(a), (3) (by the court), 41(1)(c), (7)-(8) (on certificate of registrar)	32 (incorporates CA by reference)	34 (by the court), 35-36B (on certificate of registrar)	31
<b>SURPLUS ASSETS</b>								
According to the rules or a special resolution		25T (trading assoc: to be in rules)	53(2), 55B(1) (vol cancellation)	92, regs sch 3 cl 14	43(2)	33(1)	33A-33B (vol only)	33 (distribution plan)
Subject to external approval	92, 94-98	2, 25AP (trading assoc)	53(2A)(a), 55B(1)(a) (vol cancellation)		43(3)-(4)	33(1)-(2)		33(6)-(12), 36
No distribution to members	92 (by implication)		53(2A)b), 55B(1)(b) (vol cancellation)		43(1)			33(2)
<b>COMPANY SEARCHES / PUBLIC REGISTER</b>								
Name and OAN/ABN	9-11	Reg 7	59	16, 18, 40, reg 16	6	29	39-40	37
Registered office	121 (optional)			17, 18 reg 16				40 (address for service – if lodged)
Office holders	62	Public officer 12-14, 25R-25S (trading assoc)	21A(6) (kept by public officer, public can inspect)	68	56 (public officer)	24B(1A) (details of committee to be lodged if exempted from annual return)	28 (public officer)	

REFORMING NOT-FOR-PROFIT REGULATION

	ACT	NT	NSW	QLD	SA	TAS	VIC	WA
Details of shareholders / members	67 (members only)	25AF (trading assoc)						
Copy of rules / constitution	18,30,33	15-17, 25T-25V (trading assoc)	20, 59	53(1)(sec must allow members to inspect)			5, 22	37(1)
Basic details of any changes registered	59,33,62	14, 16-17, 25R-25V (trading assoc)	20, 22,25, 59	16,17,18, 40, 68, regs 16-17	19, 24	7(2)(b), 15, 18	22, 28	37(1)
Penalties	108 (General offence provision)	S 27A (general offence provision) 25, 25AI (public officer for failure to lodge balance sheet) also other specific penalties for breaches	66, 68,-71 (officers deemed liable for offences by assoc)	Management committee members liable for specific penalties for breaches, eg 57, penalties for false/misleading information: 19-20	14 (general offence provision), 57 (penalty for officers for non-compliance with Act)	18 (public officer liable for failure to lodge change of address etc), 21 (assoc liable if raises funds from public) 24 (penalty for failure to lodge accounts)	49 (false & misleading statements), 50-50A (general penalty provisions), 50B (penalty notices), 51 (trading)	42 (c'ttee members liable if assoc breaches Act) 43 (false & misleading statements)

