Charities and Not-For-Profits Commission

This information sheet provides an overview of the *Australian Charities and Not-for-profits Commission* (ACNC) and some of the consequences of the *Australian Charities and Not-for-profit organisations Commission Act 2012* (Cth) (ACNC Act) for arts organisations that are 'not-for-profit' organisations that meet the legal definition of being a 'charity'. The ACNC Act came into force on 3 December 2012.

This information sheet could be relevant to any institution or organisation that is a public library, public museum or public art gallery or an Indigenous Art Centre or any 'not-for-profit' organisation, where that institution or organisation satisfies the legal test of having a charitable purpose that is for the public benefit.

The ACNC Act establishes the ACNC. The role of the ACNC is to be the independent regulator for charitable organisations.

The purpose of the ACNC is to:

- register organisations as charities;
- maintain, protect and enhance public trust and confidence in the charitable sector;
- promote transparency in the sector by providing a searchable public register so that anyone can look up information about registered charities;
- work with state and territory governments and agencies to provide a 'report-once, use-often' reporting framework for charities; and
- assist registered entities to comply with and understand their obligations under the ACNC Act.

What is the effect on arts organisations?

Arts organisations that meet the legal meaning of charity and the ACNC requirements for registration are eligible for register with the ACNC. Registration is required before an organisation can receive charity tax concessions from the ATO, such as deductible gift recipient (DGR) status. There is also a range of Commonwealth concessions, exemptions or benefits that depend on a charity being registered with the ACNC.

The ACNC can only register charitable organisations. An organisation that is a 'not-for-profit' but is not a charity, is not required to register with the ACNC.

However, as a result of changes to DGR laws in September 2021, from 14 December 2021 registration as a charity with the ACNC is a precondition for DGR endorsement for *all* non-government DGRs (except for ancillary funds or DGRs that are specifically listed by name in tax law). While this precondition has already been around for the majority of general DGR categories, it has now extended the requirement to the remaining general DGR categories – including the ROCO category (ie the DGR category for organisations approved for entry on the Register of Cultural Organisations (ROCO). Australian organisations can be listed on ROCO if they meet the requirements including that their principal purpose is to promote cultural activities in Australia such as visual arts, arts or languages of Indigenous persons, music, film, literature, crafts and design.) See our **info sheet** for more information.

Who is eligible to register?

The ACNC website describes a charity that is eligible to register with the ACNC as being a **not-for-profit** that:

- has a **charitable purpose** that is for the **benefit of the public**
- has no disqualifying purposes (such as to promote unlawful activities)
- is not a political party or government body individual, sole trader, or partnership
- meets other ACNC rules for registration.

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The ACNC has the responsibility for deciding whether an organisation can be registered as a charity under the ACNC Act. The ACNC website provides a registration checklist and a guide form to completing the ACNC online registration.

The ACNC website also provides guidance as to what are the appropriate 'charitable purposes' of an arts organisation and identifies the selection of 'cultural activities' as being an appropriate choice when an arts organisation uses the ACNC website to register as a charity. Note that an arts organisation that is a charity can have more than one recognised charitable purposes and can engage in more than one of the charitable activities that are identified by the ACNC.

Aboriginal and Torres Strait Islander corporations registered with the Office of the Registrar of Indigenous Corporations (ORIC) under the *Corporations (Aboriginal and Torres Strait Islander) Act 2006* (CATSI Act) are eligible to apply for registration with the ACNC as a charity.

What is a charity?

A 'charity' has a special legal meaning that is set out in the *Charities Act 2013* (Cth). As identified earlier, a charity must be a **not-for-profit** organisation that has a **charitable purpose** that is for the **benefit of the public**. The 'purpose' of an organisation is what is identified in the governing documents as the mission of the organisation; that is, the reason for which the organisation was established, or the goal to which the activities of the organisation are intended to work to achieve. A charity may have more than one purpose that is recognised as a charitable purpose. The recognition of the charitable status of an organisation requires that all of the purposes of the organisation must be charitable, except purposes that can be described as 'incidental or ancillary' to achieving the charitable purposes.

The governing documents of an organisation are the formal documents that describe the purpose(s) of the organisation, and the activities the organisation can carry out and the organisational processes and rules for managing the organisation. Examples include: constitutions, articles of association, trust deeds, charters and rule books.

The ACNC publishes a template constitution for a charitable company limited by guarantee.

The *Charities Act sets out* a statutory definition of charity that recognises 12 kinds of purpose that are charitable, including the purpose of:

- advancing culture
- promoting reconciliation, mutual respect and tolerance between groups of individuals that are in Australia
- promoting or protecting human rights
- engaging in activities that are beneficial to the general public that may reasonably be regarded as analogous to, or within the spirit of, any of the purposes that the Charities Act recognises as being a charitable purpose.

The *Charities Act acknowledges that engaging in advocacy, such as to* promoting or opposing a change to any matter established by law, policy or practice in the Commonwealth, a state, a territory or another country, is a charitable purpose where the advocacy is directed to promoting or opposing a change to any matter established by law, policy or practice that is related to one or more of the purposes that the Charities Act recognises as being a charitable purpose.

The *Charities Act requires that t*he charitable purpose must be for the public benefit. That is, achieving the purpose(s) of the organisation must be of some benefit to the public generally or a sufficient section of the public, such as for the benefit of artists and creators of cultural material in a local community, a state or territory or throughout Australia.

The legal meaning of 'charity', including 'charitable purpose', 'not-for-profit' and 'public benefit' are described on the ACNC website.

What is 'not-for-profit'?

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Whether an organisation is not-for-profit is determined by what it does with the profit it makes (if any). A not-for-profit organisation cannot be run for any profit, gain or benefit of its members, the people who run it or their close relations. For example, an art centre or gallery which distributes dividends to its members is outside what is accepted as being a not-for-profit organisation. On the other hand, an art centre or gallery which puts the money it makes back into the community for the purposes of fostering the creation of more art, is a not-for-profit organisation.

This does not mean that not-for-profit organisations cannot make a profit; rather, any profit made must be used to further the organisation's purposes. This also does not mean that not-for-profit organisations cannot employ people; they can certainly pay staff reasonable remuneration for their services.

Arts Law publishes *Business Structures and Governance: A Practical Guide for the Arts*, which provides a user-friendly guide to the different business structures for arts organisations and provides helpful information about starting up an organisation and meeting the ongoing compliance obligations of an organisation.

Why register with the ACNC?

The ACNC Act establishes the ACNC Register. Arts organisations registered on the ACNC Register will now be subject to a number of additional new legal obligations. These new legal obligations are discussed below.

Some arts organisations have already been automatically registered on the ACNC Register. These include those registered with the Australian Taxation Office (ATO) as organisations with:

- deductible gift recipient (DGR) status and/or
- public benevolent institution (PBI) status.

Registration on the ACNC Register is necessary if an organisation wishes to obtain or maintain its DGR or PBI status and the requirements for this are set out in this Information Sheet.

Having DGR status permits an organisation's supporters to obtain tax deductions on their gifts and donations to the organisation. Being endorsed as a DGR is a separate process to being registered by on the ACNC Register. Organisations with PBI status benefit from a number of tax exemptions. Again, being endorsed as a PBI is a separate process to being registered on the ACNC Register.

Charities and the Australian Tax Office

Obtaining registration as a DGR or PBI entity provides an organisation with the status recognised by the Australian Tax Office (ATO) related to the fund raising activities of the organisation.

The ATO has set out rules that a not-for-profit organisation must comply with in order for the ordinary and statutory income to be exempt from income tax. *Taxation Ruling TR 2015/1* (25 February 2015) has the title 'Income tax: special conditions for various entities whose ordinary and statutory income is exempt' and sets out two special conditions that income tax exempt entities (such as charities or not-for-profit organisations) must satisfy in order to maintain their income tax exempt status. Those special conditions are:

- the entity must comply with all the substantive requirements in its governing rules (**governing rules condition**); and
- the entity must apply its income and assets solely for the purpose for which the entity is established (**income and assets condition**).

The 'substantive' requirements in an entity's governing rules are the rules that state what the entity is required and permitted to do, and what those, who control the entity, are required and permitted to do in respect of the entity. The governing rules are usually found in the constitution although the governing rules that define the entity's rights and duties may be found in other documents of the organisation any may also be found in other sources, such as legislation and the common law. The

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'substantive' requirements can be contrasted to 'procedural' requirements, such as the rules for conduct of meetings and voting rules.

The income and assets condition is directed at compliance with the 'purpose' of the charity or not-for-profit organisation. The purpose of an organisation will usually be found in the constitution and is the charitable purpose or purposes that are discussed above. However there can be other factors to consider in order to determine what is the purpose of the organisation, including policies and plans, administration, finances, history and control, and any legislation governing the operation of the entity.

A charity may have a purpose which is incidental or ancillary to its charitable purpose. The Taxation Ruling states that the income and assets condition will not be breached merely due to an entity having an incidental or ancillary purpose.

The question that managers and directors of income tax exempt entities need to consider is: has the entity applied its income and assets solely for the purpose(s) for which the entity is established?

The consequences of breaching the governing rules condition and the income and assets condition are that the entity can lose its income tax exemption for the income year in which the breach or breaches occurred. Therefore breach of these two conditions will have serious consequences for any the charity or not-for-profit organisation.

The ATO has stated that the Taxation Ruling will be strictly applied, however the Taxation Ruling itself states that the income and assets condition will still be satisfied where:

- the misapplication or misapplications are immaterial in amount, and
- there is a one-off misapplication or occasional, unrelated misapplications of part of the income or assets of an entity for a purpose other than the purpose for which the entity is established.

The Taxation Ruling state consequences of non-compliance will also depend on whether:

- corrective action has been taken in relation to the breach or misapplication within a reasonable time;
- the corrective action has resulted in, or will result in, the entity being placed in the position (or substantially the same position) it would have been in had the breach or misapplication not occurred, and
- the entity notifies the ATO of the non-compliance and the remedial steps taken to address the non-compliance.

The managers and directors of income tax exempt entities therefore need to understand the scope of the governing rules condition and the income and assets condition and to continually review the operations of the organisation to ensure the strict compliance with these two conditions. If appropriate legal advice should be obtained to either make sure the activities and policies of the organisation are consistent with the purposes described in the governing documents or advice should be sought if there is non-compliance with the two conditions so that the notification to the ATO of the breach or misapplication of income or assets will result in the organisation maintaining its income tax exempt, notwithstanding the breach of the two conditions and misapplication of the income or assets.

Registration with the ACNC

Registration with the ACNC is a free process and is not compulsory if an organisation does not have, or desire, DGR or PBI status and registration will attract a number of additional legal obligations and consequences. These include:

- governance standards
- external conduct standards
- record keeping obligations
- reporting obligations

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- duties to notify and
- submission to ACNC enforcement powers.

These are dealt with in turn below.

Governance standards

The governance standards will be a set of requirements that registered organisations need to meet. The Government has stated that the aim of the governance standards will be to ensure a minimum level of accountability across the sector.

The ACNC Act states that the aim of the governance standards will be to give the public confidence that registered organisations:

- pursue their purposes
- manage their affairs openly, accountably and transparently
- use their resources effectively and efficiently and
- minimise the risk of mismanagement.

External conduct standards

The external conduct standards will be a set of requirements about that registered organisations must meet if they send funds outside Australia or engage in activities outside Australia. The ACNC Act states that the aim of the external conduct standards will be to give the public confidence that funds sent outside Australia by registered organisations are reaching legitimate beneficiaries and being used for legitimate purposes; and that both funds sent and activities engaged in outside Australia will not contribute to terrorist or other criminal activities.

The Australian Council for International Development (ACFID) is the peak body for Australia's non-government aid and international development organisations. All ACFID members commit to comply with the ACFID Code of Conduct (the ACFID Code).

Record keeping obligations

ACNC registered organisations must keep certain records. There are penalties if these are not kept correctly.

There are two types of records that a registered organisation must keep:

- financial records, and
- records that explain the operations of the organisation.

Both types of records are discussed below.

For both kinds of records, registered organisations must keep sufficient records to enable:

- the ATO to assess their compliance with any taxation law; and
- the ACNC to assess their entitlement to registration and their compliance with the ACNC Act.

Financial records

Registered organisations have to keep financial records that:

- correctly record and explain their transactions, financial position and performance; and
- allow true and fair financial statements to be prepared and audited.

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Not all registered organisations need to have audited accounts, but they must keep their records in a way that would allow an audit to occur.

Records that explain the operation of a registered organisation

Registered organisations must keep records that correctly record and explain their operations. Depending on the size of the organisation, this may include any governing rules, policies and procedures; annual reports; minutes of governing body meetings; and similar documents.

For both types of records, the records must be written and be in English or readily accessible and easy translated into English. Registered organisations generally have to keep records for seven years. Failure to keep these records in accordance with the record keeping requirements in the ACNC Act is an offence.

Reporting obligations

Registered organisations must provide two types of reports to the ACNC:

- annual information statements (AISs), and
- annual financial reports (AFRs).

The ACNC also has the power to request additional reporting from registered organisations in certain situations.

The ACNC has the power to deregister charities that fail to comply with their reporting obligations. Charities that are deregistered can regain their charity status by completing the overdue reporting. However the revocation of charity status may have serious consequences for the organisation, including reputational damage, so that organisations registered with the ACNC should attend to their reporting obligations and also inform the ACNC of any change of address and other contact information so that the ACNC knows where to send reminder notices.

Annual information statements

AISs are reports that registered organisations must provide to the ACNC. The Commonwealth Government has stated that AISs are designed to ensure that organisations are operating transparently and are accountable to the public. In particular, the information in the AISs must be sufficient to enable the ATO to assess their ongoing:

- tax compliance
- entitlement to ACNC registration and
- compliance with the ACNC Act.

Annual financial reports

AFRs are financial reports that are required to meet specific reporting standards set out by the ACNC. Only certain registered organisations are required to submit AFRs.

AFRs can contain both operational and financial information and are required to include detailed reports about the financial positions of registered organisations. The first AFR for registered organisations will fall due on or before 31 December 2014 with reporting due for the 2013-14 financial year, or six months after the end of an approved substituted accounting period.

Duties to notify

Registered organisations have duties to notify the ACNC if certain events occur. If a registered organisation does not comply with the duty to notify within the timeframes set by the ACNC Act then it is liable to pay administrative penalties. The timeframes for when an organisation must notify are different, depending on the size of the registered organisation.

The events which are required to be notified to the ACNC include the following:

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- changes of name
- changes of address for service
- changes to the 'responsible persons' (people who responsible for the governance of the charity including directors or committee members, or its trustees)
- changes of governing documents (such as its constitution, rules or trust deed); and
- any significant breaches of the ACNC Act or non?compliance with governance standards or external conduct standards.

Submission to ACNC enforcement powers:

The ACNC Act provides that organisations registered on the ACNC Register are subject to the following enforcement powers of the ACNC:

- **Warning notice:** warning notices will be in writing and will describe the circumstances in relation to the relevant contravention or non-compliance.
- **Directions:** registered organisations will have to comply with all ACNC directions irrespective of anything to the contrary in their governing rules or contracts or arrangements with third parties.
- **Suspension and removal of responsible persons:** the ACNC has the power to suspend and to remove a member of the organisation's governing body under certain circumstances.
- **Cancel an organisation's registration:** the ACNC may cancel an organisation's registration if it:
  - is or was not entitled to registration
  - provided information on its application for registration that was materially false or misleading
  - has not complied with (or is likely not to comply with) a provision of the ACNC Act or governance or external conduct standards
  - is insolvent or in administration or
  - has requested cancellation.

Need more help?

If you have questions about any of the topics discussed above please contact Arts Law.

Seminars, training and information on legal issues faced by not-for-profit community organisations are provided by Justice Connect.

Links to Arts Law's ACNC related articles and briefings are set out below:

- Charity registration is now a precondition for Deductible Gift Recipients
- ACNC Legislation passed 1 November 2012
- Practical effects of the ACNC

In addition, the ACNC website contains fact sheets and guides and links to some of these are set out below:

- Factsheet: Arts associations
- Factsheet: Who can register with the ACNC
- Factsheet: What are 'governing documents'?
- Factsheet: What is a 'responsible person'?
- Factsheet: Aboriginal and Torres Strait Islander corporations – applying for charity registration with the ACNC

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- Commissioner's Interpretation Statement: Indigenous charities
- Factsheet: Deductible gift recipients (DGRs) and the ACNC
- Factsheet: Other Commonwealth benefits and exemptions available
- Factsheet: Ongoing obligations of registered charities
- Guide for board members: My charity and the ACNC
- Template constitution for a charitable company limited by guarantee

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