



ARTS LAW CENTRE OF AUSTRALIA

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General Manager  
Corporations and Financial Services Division  
Department of the Treasury  
Langton Crescent  
PARKES ACT 2600

By email: [UPComments@treasury.gov.au](mailto:UPComments@treasury.gov.au); [Stephen.Powell@treasury.gov.au](mailto:Stephen.Powell@treasury.gov.au)

Dear Sir/Madam

### **Submission on the Financial Reporting of Unlisted Public Companies**

The Arts Law Centre of Australia (**Arts Law**) thanks you for the opportunity to provide a submission to the Treasury on the issue of financial reporting of unlisted public companies. The reporting requirements on the not for profit sector (NFPs), including the arts, is significant in view of the resources available to most NFPs, we therefore welcome a review which aims to reduce this regulatory burden on the NFP sector.

We note that in the preparation of this submission, Arts Law has had the benefit of the discussion of issues by the NFP Expert Think Tank and the draft submission prepared by PILCH Victoria. Arts Law has also benefited from feedback on drafts of our submission and in this regard wishes to acknowledge the assistance of Kevin Golding and Atul Joshi at the Australia Council and Steven Miller, Arts accountant and Honorary Treasurer for Arts Law and Helen O'Neil, Australian Major Performing Arts Group.

### **About the Arts Law Centre of Australia**

Arts Law was established in 1983 and is the national community legal centre for the arts. Arts Law is a not for profit company limited by guarantee.

Arts Law provides expert legal advice, publications, education and advocacy services each year to more than 5,000 Australian artists and arts organisations operating across the arts and entertainment industries.

Arts Law is also part of the network of 207 community legal centres around Australia.

### **About our clients**

Our clients not only reside in metropolitan centres, but also contact us from regional, rural and remote parts of Australia, and from all Australian states and territories. Arts Law recognises the diversity in the arts community and our client base is multi-cultural, and both Indigenous

and non-Indigenous. Arts Law supports artists and arts organisations from across all art sectors, including visual arts and crafts, music, performing arts, literature, film, community arts and new media.

Arts Law supports the broad interests of artistic creators, the vast majority of whom are emerging or developing artists. A significant portion of our work is for the arts organisations which support them, the majority being NFPs. In 2006 approximately 25% of the subscribers of Arts Law were NFPs, accounting for approximately 600 legal advices provided during the year.

The comments that we make in this submission are informed by the services we provide to our diverse client group.

### **About our approach to issues affecting artists and other creators**

As an independent organisation giving legal advice to the arts community nationally, Arts Law is in a unique position to comment on the issues affecting arts organisations. Arts Law also has an extensive education program and is regularly asked to present seminars on governance issues affecting arts organisations, including financial and other accountability issues.

In view of the wide exposure that Arts Law has to governance issues affecting arts NFPs, a primary concern for Arts Law is the extent to which accountability requirements for companies limited by guarantee are over burdensome for an extremely under-resourced sector.

### **Regulatory Framework for Arts NFPs**

Arts Law agrees with the overarching comments of the Expert Think Tank and PILCH that the regulatory framework for NFPs is complex and confusing. Arts Law is often asked for advice by unincorporated groups establishing an incorporated organisation and we have to explain the different possibilities available to them, which may include companies limited by guarantee, incorporated associations, co-operatives, as well as Aboriginal corporations in some instances. For organisations run exclusively by volunteers or with very limited staff, working through the different options and their requirements is daunting and unnecessarily complicated.

We agree with PILCH's recommendation that Federal and state governments should work together to establish a nationally consistent regulatory regime for NFPs.

We are also strongly of the view that modernisation and consistency is required with regard to the public fundraising activities, charitable and taxation status of NFPs.

### **Financial Records and reporting to external body**

Arts Law agrees with the two guiding principles developed by the Expert Think Tank and endorsed by PILCH:

- a) all NFP organisations should continue to be required to maintain proper financial records and accounts; and
- b) all NFP organisations should be required to report to an external regulator because of the public nature of their purpose.

However, it is important that a minimum standard of disclosure be developed that is appropriate to the size and circumstances of NFPs.

Arts Law agrees with the Expert Think Tank's conclusions that given the variety of NFPs, which applies equally in the arts, a one size fits all model is not appropriate and there should be differential reporting obligations based on the size and income of the organisation. The cost of full audits can be prohibitive for many small arts NFPs and yet the national structure of a company limited by guarantee is required in view of the activities and likely growth of the organisation.

For example, many NFP arts organisations operate in more than one state, or tour exhibitions or performances in more than one state. Because of this interstate activity a company limited by guarantee provides the greatest protection for limitation of liability and means that reporting and auditing is streamlined with one system, as opposed to the varied and sometimes inconsistent reporting requirements if the organisation is incorporated in several states and/or has reporting obligations to ASIC if it has registered for an Australian Registrable Business Number (ARBN).

Arts Law agrees with the observation of PILCH that even if the reporting requirements for NFPs are improved, unless all State and Federal funding agencies are included in these discussions, NFPs may find themselves no better off, if Government agencies continue to require a level of financial reporting which is more onerous than the legal requirements.

#### **Specific questions in Treasury Discussion Paper**

Our responses to each of the questions raised in the Discussion Paper are briefly outlined below.

- A. Do you support the introduction of a differential reporting regime based on size for companies limited by guarantee? If so, what do you consider to be the appropriate criteria (both in terms of the indicators of size and the quantum of those indicators) for differentiating between those companies that are required to report and those companies that are exempt?**

Arts Law supports the introduction of a differential reporting regime based on size. We agree with the conclusion of the Expert Think Tank that a minimum public disclosure standard should be applied for all NFPs regardless of size, but full audited accounts should only be required from larger NFPs. As outlined in the submission by PILCH

*The think tank group agreed that, as a guide, the audit function should not cost more than 1% of the annual income of the organisation. A two-tier reporting regime should be introduced such that NFPs under, for example, a \$500,000 income threshold, would be required to report, but in accordance with a standard that is simplified and tailored to the NFP situation: ie, less onerous than the current full accounting standards or proposed SME regime. (The \$500,000 threshold was chosen as a benchmark based on a full audit cost of approximately \$5,000 for a small NFP organisation.)*

- B. Do you believe it is appropriate to differentiate between companies limited by guarantee by the nature of their operations rather than just size? If so, what nature of operations do you believe warrants greater transparency?**

Arts Law believes the income of the NFP (ie the 'size') is an appropriate basis on which to differentiate. Arts Law supports simplified and streamlined reporting for NFPs based on size and nature of their operations (ie operating in the arts industry).

- C. Do you consider that companies limited by guarantee that receive any money through grants should have financial reporting requirements? If so, can this obligation be satisfied by the company providing special purpose financial reports**

**to the grantor rather than preparing general purpose financial reports under the Corporations Act?**

NFPs that receive grants should be accountable to the grantor for the delivery of the program, service or project for which the money was received. Indeed, many grantors place contractual obligations upon grantees to comply with substantial reporting requirements. However, the reporting requirements imposed by grantors are not necessarily appropriate in terms of the scope of the financial reporting required. Moreover, grantors are not necessarily equipped or qualified to undertake monitoring of financial reporting for NFPs. For these reasons Arts Law is of the view that it is not appropriate that grantors/funders become de facto regulators of the NFP sector. It is much more appropriate that a useful minimum reporting requirement is established and that the external regulator is better placed to support NFPs in the reporting and accountability requirements.

It is important that all NFPs have an appropriate, minimal level of financial record keeping and reporting which increases public confidence in the NFP sector and helps to ensure the good governance of the NFP organisations. Arts Law supports less onerous financial reporting for NFPs based on size and nature of the operations and for them to report either to ASIC or a special purpose regulator of NFPs. Arts Law does not support the suggestion that companies limited by guarantee be required to provide special purpose financial reports to the grantor.

In preparing this submission, Arts Law consulted with the Australia Council. Arts Law supports the Australia Council's comments that "the financial reporting requirements of funding bodies should be satisfied by general purpose financial reporting, to avoid organisations having to provide separate financial reports to multiple funding partners. Indeed the Cultural Ministers Council endorsed this approach in 2003. All arts funding agencies have standardised reporting requirements for arts organisations in receipt of multi-year funding from both the Australia Council and State and Territory arts agencies." This is good as far as it goes however many arts organisations will still be faced with a plethora of different forms of financial accountability due to the varied requirements of funding bodies.

The AMPAG noted that there were "serious issues with the introduction of international accounting standards including disclosures required by the pro-bono directors and most serious of all, treatment of government grants on a cash rather than an accrual basis. For all non-profits required to do accrual accounting it is highly disruptive not to be able to treat government grants in the same way as box office, fee, sponsorship and donation income".

**D. If you support some companies limited by guarantee being exempted from financial reporting, what percentage of members should be required in order to require an exempt company limited by guarantee to prepare a financial report?**

Arts Law does not support some companies limited by guarantee being exempted from financial reporting.

Arts Law agrees with the conclusion of the Expert Think Tank and PILCH that allowing for a percentage of members to require an audit could be used for disruptive and damaging purposes and it would be better if a residual power allowed a member to seek an independent review by ASIC or other regulator of NFPs (see final comments below). Arts Law is of the view that either ASIC or other regulator of NFPs should take a proactive approach in supporting NFPs.

**E. If you support the retention of financial reporting requirements for all companies limited by guarantee, do you consider that there is scope to reduce the amount of financial information these companies are required to report? If so, what type of**

**financial information do users need companies limited by guarantee to report (for example, related-party disclosures)?**

Arts Law agrees with the conclusion of PILCH that a simplified minimum form of disclosure should be developed as a baseline, with additional requirements for larger NFPs.

**F. Do you consider that there is a need to harmonise the financial reporting requirements of companies limited by guarantee and incorporated associations to provide a consistent reporting framework for not-for-profit entities in Australia?**

Yes, it is imperative that a simplified baseline reporting requirement be established and that there be standardisation between reporting requirements for companies limited by guarantee and incorporated associations. As part of this process government departments which provide funding should rely on this information rather than imposing unnecessary additional or different requirements. Arts Law encourages Treasury to liaise across Government in this regard.

**G. If some companies limited by guarantee were to be exempt from financial reporting, do you consider there is value in these companies continuing to be subject to some level of non-statutory external assurance as a means of promoting good governance? If so, what should this assurance relate to and how do you think this regime should be introduced (for example, through best practice guidelines issued by the professional accounting bodies)?**

We refer to our previous comments and agreement with the Expert Think Tank and PILCH position that no NFP should be exempt from a requirement of baseline public disclosure. We also agree that it would be of assistance if in addition to this requirement, best practice guidelines and low cost accessible training packages were developed for NFPs.

**H. For those companies limited by guarantee that are required to prepare financial statements, do you consider that there is a need to change the current audit requirements? If so, which aspects of the current requirements need to be reformed?**

We again refer to our previous comments and our agreement with the PILCH position that there

*"needs to be a tailored two-tiered accounting standard for NFPs. The cost of auditing and a shortage of expertise within the accounting profession about NFP financial reporting issues are major problems for the sector."*

**I. Do you support amending the Corporations Act so that companies limited by guarantee are specifically prohibited from distributing profits to members in the form of dividends?**

Again Arts Law agrees with the observation by PILCH that *"companies limited by guarantee are generally assumed to be NFPs and as such they should not be permitted to distribute dividends or assets to members. The Corporations Act should be amended accordingly."*

## **Final Comments**

### **Proposal for a specialised NFP Regulator**

Similar to the model in place for Indigenous corporations, Arts Law sees merit in the establishment of a specialist regulator for NFPs that has a greater focus and interest in the

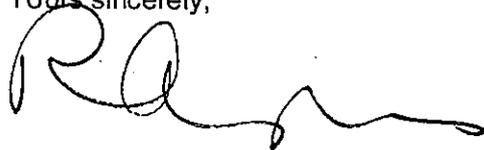
support, development and accountability of the NFP sector. The current ASIC regime can be **extremely** difficult for under-resourced NFPs to navigate and comply with. A more supportive regulatory body with appropriate investigative powers should help strengthen the NFP sector, the benefits of which would flow to the broader Australian community which relies heavily on the diverse services provided by our sector.

### **NFPs, Charities and Tax**

In 2003 when the Government was examining charities, Arts Law made a submission to the Board of Taxation, that there was a lot of confusion and misunderstanding, by those in the wider community as well as charities themselves, as to the differences between charities, Public Benevolent Institutions (PBIs) and Deductible Gift Recipients (DGRs). This in turn leads to confusion as to what tax relief an entity is entitled to under each category. At that time we noted that endorsement by the ATO for each of these categories requires significant work by an organisation and it is becoming increasingly problematic working with definitions, particularly of PBIs, which are very outdated. We noted then that it was a lost opportunity not to examine the need to bring greater clarity and efficiency to the law in this regard. The same problems still remain and whilst we commend the Government for examining the issue of financial accountability we suggest that the complexity of issues for NFPs with regards to charitable status and differing taxation benefits remain and continue to need reform.

If you would like any further information about this submission please do not hesitate to contact me.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Robyn Ayres', written in a cursive style.

Robyn Ayres  
Executive Director  
Arts Law Centre of Australia