

Summary of preliminary findings from the questionnaire on company law issues affecting not-for-profit companies

Thank you to those who completed our survey of not-for-profit companies in 2002. The numerical data has now been entered and much of the analysis is complete. We are still looking at many of the comments and, as the final stage of this three year project, are preparing a detailed research report with law reform recommendations. It is hoped that this report will help to engender debate about the regulation of 'not-for-profit' (NFP) organisations. We welcome feedback about the following findings and draft recommendations.

Response Rate

The data in this report is based on responses from 1,688 NFP companies limited by guarantee. Taking into account non-receipts, the response rate is estimated to be 39%.

Survey Results

Part A – General Company Particulars

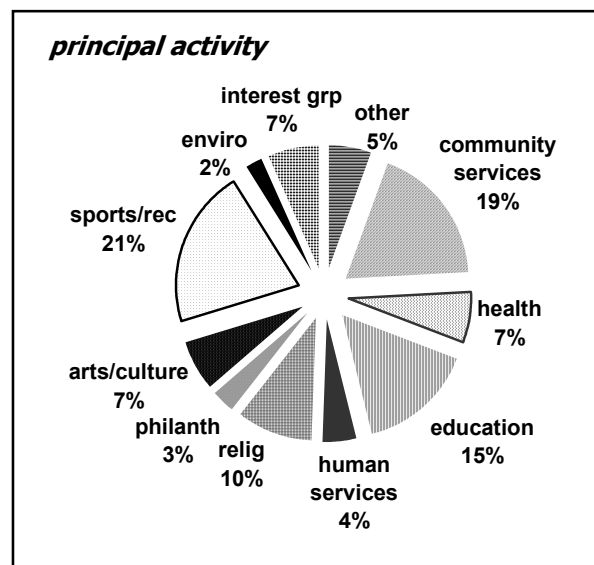
Nature of activities

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.

General profile of NFP companies

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 not part of a group structure: only 14% had subsidiary or related entities
- was small to medium in size
- 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 companies (income of more than \$10 million and assets of more than \$10 million), with a good spread of all sizes.

The majority could be said to be small to medium in size - 72% of respondents had less than 20 employees and 60% had less than 100 members. Interestingly, 88% of respondents could be said to be within the s 45A Corporations Act 2001 (Cth) definition of "small" (namely, had at least two of the following - consolidated gross operating revenue of <\$10 mil, consolidated gross assets of <\$5 mil and <50 employees). Thus, these organisations could, from a company law point of view, have chosen to be a proprietary limited company and, because of their size, they would have had minimal reporting obligations (for example, no requirement to prepare and lodge audited accounts).

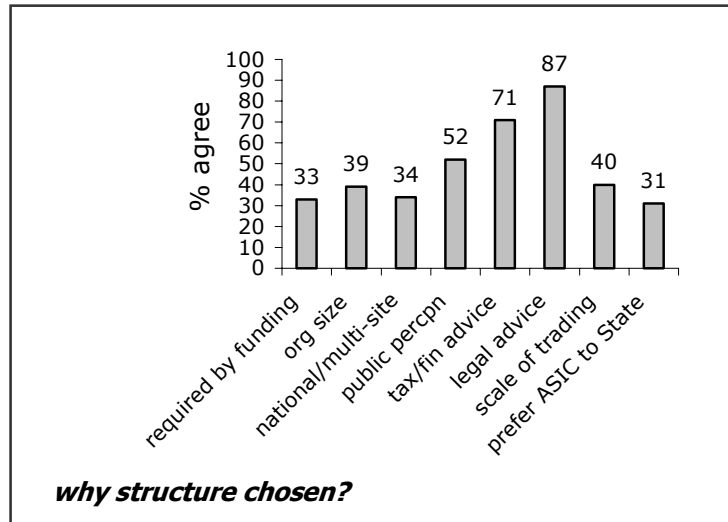
Part B – Legal Structure

Choice of Structure: Factors behind choice of legal form

The questionnaire asked respondents to rank the importance of various reasons why a company was chosen as the legal structure, rather than, for example, an incorporated association.

The most significant findings concerning this question were as follows:

- 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;
- over a third (34%) indicated that being a “national or multi-state organisation” was an important factor in their choice of a company structure;
- 40% 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 – 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; and
- “public perception and status” was important to the majority (52%). This supports anecdotal evidence that ‘serious’ or ‘more sophisticated’ NFP organisations are companies rather than incorporated associations.



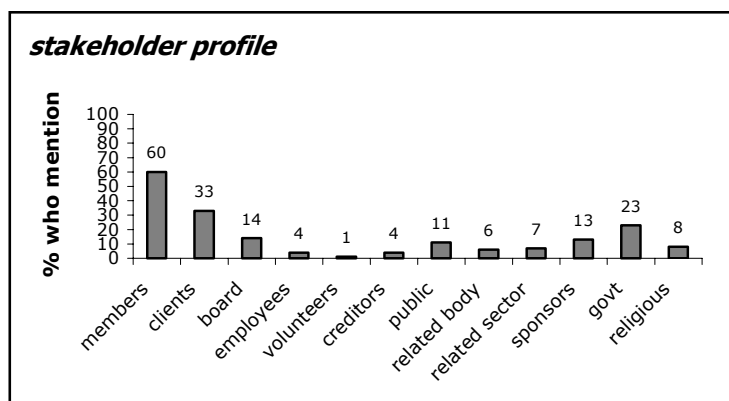
Success of a company legal structure

There was no clear evidence of any overall dissatisfaction with the company structure. The dissatisfaction that was expressed was about the expense (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, members, and those dealing with the company and that it has been a flexible structure with manageable reporting obligations.

Part C – Stakeholders

Who are the company’s stakeholders?

In contrast to ‘for-profit’ companies, there are a multiplicity of stakeholders in NFP companies. Members were the most often cited stakeholder even though 46% of respondents said they were primarily public-serving rather than member-serving. Interestingly, volunteers were almost never viewed as stakeholders although 86% of respondents had at least one volunteer.



Reporting to stakeholders

The split between those (a.) respondents who said that the report they provided to any of their stakeholders was provided on a voluntary basis, compared with (b.) those that said that they did so on a mandatory basis was fairly even (59% as opposed to 55%). The proportion of stakeholders that respondents said were not provided with any report was 20%, which seems quite high given that the questionnaire defined a stakeholder as a group or person ‘who has a direct and legitimate interest in monitoring the activities and good management of the company’.

Part D & E – Board Composition, Experience, Structure and Procedures

Board of directors and management

The typical respondent board of directors:

- was comprised of 8 unpaid, non-executive directors: 77% had Boards comprised entirely of non-executive directors and 8% said that their non-executive directors (i.e. not employed by the company) received payment in addition to out-of-pocket expenses
- was predominantly male: only 26% of directors were female, although nearly three-quarters (74%) had at least one female director on their Board
- was comprised of 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
- does not represent a particular stakeholder: 85% do not have any donors as directors; 79% said they did not have a director that represented the interests of stakeholders other than members
- makes decisions based on a consensus based style: only 9% vote without using consensus methods

Recruiting and retaining board members

Nearly a third (29%) of respondents reported difficulty recruiting directors with further analysis showing 'small' companies having slightly more difficulty than 'large' companies (30% as against 21% respectively). 16% reported difficulty in retaining directors. Small companies are twice as likely as large companies to have trouble.

Board experience, skills and knowledge

Respondents were generally positive about the experience and skills of their Board as a group. 80% 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. There were only two areas in which majority of respondents did not feel that the skills and experience of the board 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.



Part F – Regulatory Framework

What information should be available to the public and other stakeholders?

The questionnaire asked what information should be available to the public. The main results were as follows:

- 9% thought that no information should be made available to the public;
- 89% thought that a description of activities should be available to the public;

- only 39% agreed that fully audited accounts should be available to the public – that is, only 39% agreed that they should have to disclose what they are currently required by the *Corporations Act* to disclose,
- the majority (56%) were of the opinion that summary financial information was sufficient.

Thus, this 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, in fact, required by the *Corporations Act* to make (namely, fully audited accounts).

Satisfaction/dissatisfaction with ASIC?

From their experience, the respondents were asked to rank a series of statements about their dealings with ASIC. The results showed some dissatisfaction with ASIC’s performance. The majority of respondents agreed with only one positive statement, namely that ASIC has an important public information role to play (which is not even a statement about whether the respondents think ASIC is performing that role well). However, 70% of respondents thought that the *Corporations Act* and the way it is implemented is more appropriate for ‘for-profits’ than NFPs. This suggests that it is the fact that ASIC is not a specialist NFP regulator, rather than the way ASIC carries out its role, that has created dissatisfaction among NFP companies.

A new regulator?

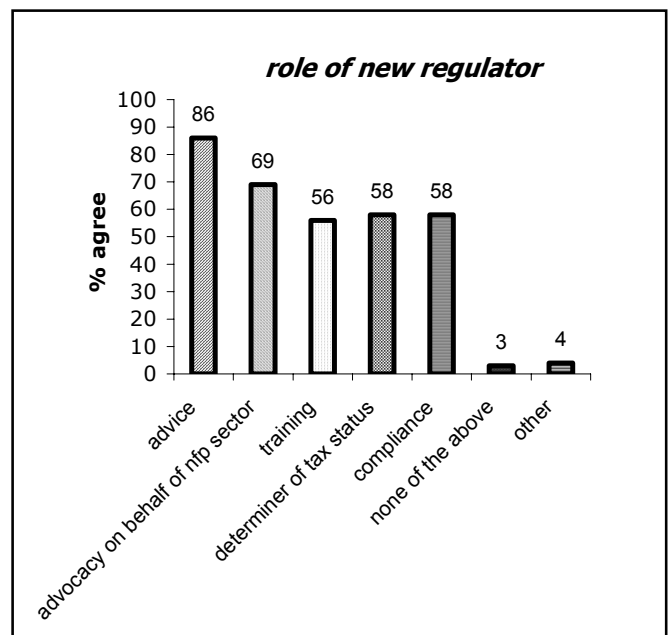
Respondents were asked if they agreed with the Charity Definition Inquiry recommendation about the establishment of a new administrative body to oversee charities and related entities. The majority (54%) were in favour of the recommendation – this becomes nearly three quarters (74%) when the significant ‘not sure’ group (36%) and non-responses (6%) are removed. Comments written on the survey below the question about the 2001 Charity Definition Report recommendation (by the ‘not sure’ group of respondents), suggest that most were concerned about additional regulation and even more paperwork. Many were unaware of the exact nature of the Inquiry’s recommendation and wanted more information.

Responses to the further question of whether, assuming this recommendation was implemented, respondents thought the new body should “have jurisdiction over corporate regulation of not-for-profit companies *instead of ASIC*” were a little more ambivalent. A third (33%) said ‘yes’, 25% said ‘no’, 36% were ‘not sure’ and 6% did not answer the question. When the ‘not sure’ group are removed, a majority of 57% are in favour.

More analysis of the large ‘not sure’ group is being conducted, but it is suggested that the ambivalence about a new regulator instead of ASIC (at least in part) reflects the respondents’ view of the alternatives. As mentioned earlier, nearly a third (31%) of respondents identified a preference for ASIC over a State regulator as an important factor in their choice of incorporated legal form. Anecdotal evidence suggests that organisations requiring structures outside the model rules have difficulties dealing with State based incorporated association authorities. Therefore, respondents may not have a positive experience/view of a NFP specific regulator. Other respondents were (from their comments) hesitant to provide an opinion in favour of a new regulator without a more fleshed out option before them.

Role of a new regulator

Respondents were asked if the Charity Definition Inquiry’s recommendation for the establishment of an independent administrative body was implemented, “which of the following roles do you think such an independent body should have?” Respondents were in favour of combining both compliance (58%) and determination of charitable status (58%) with advice (86%), sector advocacy (69%) and training (56%).



Proposals for reform

It is hoped that the data from this survey can be used to engender debate. Our final research report (end 2003-2004) will consider these (and other) issues. We welcome your comments on these proposals:

a) new NFP company structure under Corporations Law:

Whether a company limited by guarantee is the most appropriate structure - is it time to introduce a specialist form of company structure instead of or in addition to incorporated associations? In 1995 the Industry Commission recommended a specialist form of company for "Community Social Welfare Organisations" and the United Kingdom Cabinet Office has recently recommended the establishment of two new types of company (the "Community Interest Company" and the "Charitable Incorporated Organisation"). The myriad of legal structures for NFP organisations hampers accountability and regulation which, in turn, have implications for donor confidence in the sector;

b) different company law reporting requirements for NFPs depending on their size and purpose:

Whether the extent and nature of the disclosure should vary depending on factors such as size, member-serving vs public-serving and taxation status? The vast majority (91%) of NFP companies say they enjoy the privilege of income tax exemption. This gives rise to a public policy argument that, as consideration for this *privilege*, there should be a corresponding *responsibility* of public accountability and disclosure. But what is the balance between reporting obligations that meet the specific needs of NFPs and their stakeholders, and obligations that are unduly onerous or do not provide helpful information?

c) a new NFP regulator:

Who is the most appropriate regulator – there is a level of dissatisfaction with ASIC. Should a specialist unit be established within ASIC to deal with the particular needs of NFP companies? Should simple steps such as a plain language guide for NFP companies and/or reduced fees be implemented? Is it time for the States to refer their powers over incorporated associations to the Commonwealth and rationalise the regulation of NFP corporate bodies?

Three options for a new NFP regulator:

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

- i. 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 co-operatives);
- ii. 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 (however, this is likely to have constitutional law limitations like those experienced by the Corporations Act regime); or
- iii. introduction of a single, Commonwealth statutory regime for all corporate bodies (that is, 'for-profit' and 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). This would ensure national regulation by ASIC and the development/refinement of specialist form (or forms) of corporate entity for NFP organisations generally.

Based upon the findings of this survey and further consideration, it is our preliminary opinion that the latter (option iii) is preferable.

Further Comments Welcome

We welcome your feedback on the issues raised in this Summary of Preliminary Findings. Please feel free to email or write to us at the addresses noted below. We will provide updates on the project over the next year, including information about the release of the full report upon its completion on our website at <http://cclsr.law.unimelb.edu.au>

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It should be noted that none of the observations in this report are intended as legal advice. If any of the information in this Summary of Preliminary Findings concerns you, please consult your legal advisor.