



Regulatory Impact Statement

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TRIM Number

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Date Received

RGU Officer

Information

When writing a RIS agencies should:

- Complete each relevant section in the RIS template sufficiently, to enable informed responses on the policy issue, objectives, options and impacts;
- In the consultation phase, ask questions which prompt respondents to confirm and challenge the analysis, including estimates of the magnitude, scope and range of the impacts. In addition, ask respondents if there are further problems, feasible options or further impacts that should be considered; and
- Ensure that any assumptions made are clearly defined.

Submissions and Queries

Name of Proposal

Financial reporting under the *Associations Incorporation Bill 2014*

Department/Agency

Department of Commerce

Name of Contact

Melissa Rosair

Position

Legal Policy Officer

Postal Address

Level 7, 219 St Georges Terrace

Perth WA 6000

Email

melissa.rosair@commerce.wa.gov.au

RIS Details

Comments and submissions are invited on the proposal, in response to information provided in this RIS. Agencies may elect to make all responses to the Consultation RIS publicly available. Written comments and submissions should be forwarded between the start and end dates, as detailed below. This document will then be developed into the Decision RIS.

Agencies should provide the following information at the relevant stages of RIS development

Consultation RIS Lodged

N/A

Consultation Start Date

N/A – Extensive consultation already completed

Consultation End Date

N/A

Consultation Web-Link

N/A

Decision RIS Lodged

17/6/14

Executive Summary

This decision regulatory impact statement ("DRIS") on the financial reporting requirements of the Associations Incorporation Bill 2014 ("the Bill") has been prepared in accordance with the Regulatory Impact Assessment Guidelines for Western Australia, and covers the following areas:

- statement of the issue;
- objectives;
- option to address the issue;
- impact analysis;
- consultation;
- preferred option; and
- implementation and evaluation strategy.

The reporting requirements will not add significantly to the regulatory burden because:

- over 90% of associations will not be affected;
- most of the remaining associations will already be reporting at an increased level;
- the requirements are harmonised with other state and Commonwealth legislation and will minimise inconsistencies in reporting requirements;
- the sector fully supports the proposed tiers; and
- this level of reporting has been recommended by the Auditor General and other bodies as being a minimum responsible level of financial reporting.

The Department has conducted an assessment of the potential costs of the proposed financial reporting requirements and has concluded that these requirements are a significant and much-needed improvement on the financial reporting requirements under the current *Associations Incorporation Act 1987* (WA) ("the Act"). The Bill's proposed regulatory regime is not a disproportionate response to the level of risk that varying sizes of associations present and ensures that associations are transparent and financially accountable to their membership. The three-tiered system of financial reporting is sensitive to the fact that the vast majority of associations in WA are tier 1 associations (i.e. revenue of less than \$250,000 p.a.) and as such do not require the same level of regulation as larger tier 2 and tier 3 associations.

The financial reporting system has been designed to ensure that WA associations are not subject to additional regulatory burden that would come from having different requirements across different states, territories and the Commonwealth.

The proposed changes have received widespread stakeholder support from associations, the members of associations and subject-matter experts in the not-for-profit sector.

1. Statement of the Issue

A) Key facts

- There are approximately 17,542 associations incorporated in Western Australia under the Act.
- Of these 17,542 associations at least 90% are tier 1 associations. This means that 15,788 associations generate revenue of less than \$250,000 per annum.
- The Department estimates that of the remaining 1,754 associations that fall within tiers 2 (\$250 000 - \$1 000 000 revenue) and tier 3 (>\$1 000 000 revenue), there are around 526 tier 2 associations (i.e. 3% of 17,542) and there are around 1,228 tier 3 associations (i.e. 7% of 17,542).
- Incorporated associations are an important part of the not-for-profit sector. Most Western Australians are directly or indirectly involved in an incorporated association, either through participating in sporting or special interest activities, through the donation of money¹, receiving of services or working as a volunteer. There is significant community investment and interest in associations and how they are run. As noted by the Auditor General in the *Regulation of Incorporated Associations and Charities* report of May 2005² ("Auditor General's report"), government regulation is important to maintaining public confidence in the operation of these groups.

B) Current legislation does not provide adequate guidance

The financial reporting obligations under the Act are minimal. Section 25 requires accounting records to be kept and section 26 requires annual accounts showing the financial position of the association to be submitted to members at the annual general meeting.

The Act does not provide any guidance or clarity about the form that the financial reports should take and does not require any independent scrutiny of the reports in the form of a review or an audit. As noted in the Auditor General's report³, "*The level of financial accountability shown by the management committee to the members is limited. Although accounts are required to be presented at the annual general meeting, unlike other Australian states there is no legislative requirement for these to be audited*" (p23-24).

The importance of audited financial statements for associations controlling significant amounts of funds is highlighted in the Auditor General's report, which provided an example of an insolvent association that failed to maintain adequate books and records and therefore continued to operate for a year because it was not aware it was insolvent. The Auditor General's report suggested that "*Audited accounts would provide members with an increased level of assurance that the accounts show a true and fair view of the association's financial transactions and position*".⁴ The Auditor General reiterated his concern about the lack of auditing in his submission to the Associations Incorporation Bill ("Green Bill") in 2006.

C) Stakeholder concern about financial accountability of associations

The Auditor General's concerns are consistent with complaints against associations received by the Department every year. In the last year, approximately 60% of complaints made concerned allegations about financial accounts and/or financial mismanagement. For

¹ Some associations hold charitable collections licences under the *Charitable Collections Act 1946* (WA) which enable them to collect donations.

² page 18.

³ pages 23-24.

⁴ page 24.

example:

- financial records not being kept;
- lack of access to financial records;
- financial reports not being provided to members or presented at the annual general meeting;
- financial reports not being properly prepared;
- financial reports not audited;
- discrepancies in the accounts;
- fraud;
- financial mismanagement; and
- insolvency.

The nature of these complaints evidences the importance that members of associations, and the public more generally, place on proper financial accountability of associations. The public recognises that financial reporting is an important vehicle by which financial accountability can be discharged, particularly when financial reports have been afforded independent scrutiny, either in the form of a review or audit.

The *Not-for-Profit Fraud Survey 2014*, a survey of not-for-profit organisations in Australia (including incorporated associations) conducted by audit firm BDO, found that one quarter of not-for-profit organisations considered fraud to be a problem, with the risk of fraud increasing with the size of an organisation.

D) The need for harmonisation with other jurisdictions

A comparison of the financial reporting requirements of the Bill, the Act and other associations legislation in Australia is found at **Attachment A**. The comparison also includes the requirements for companies limited by guarantee under the *Corporations Act 2001* (Cth) ("Corporations Act"), being similar entities to incorporated associations because of their not-for-profit nature, and for charities registered under the *Australian Charities and Not-for-Profits Commission Act 2012* (Cth) ("ACNC Act"), some of which are incorporated associations.

Attachment A reveals that, other than Tasmania (which has the oldest associations legislation in Australia), Western Australia is the only jurisdiction that does not have a system of financial reporting that ensures regulatory requirements are commensurate with the size (and hence the risk) of the association.

According to the 2010 Productivity Commission report *Contribution of the Not-for-Sector* ("Productivity Commission report"), the financial reporting requirements for companies limited by guarantee were amended in September 2010 to "address the disproportionate cost of reporting .. through a three tiered differential reporting framework" and are regarded as a model for other jurisdictions.⁵ It is important to note that at the time that Cabinet approved drafting of the Bill (August 2010) and the Regulatory Gatekeeping Unit approved the associated Preliminary Impact Assessment these changes for companies limited by guarantee had not commenced.

The Productivity Commission report concluded that the current regulatory framework for not-for-profit organisations (which include incorporated associations) is "characterised by uncoordinated regimes at the Commonwealth and state/territory levels" and that "disparate

⁵ page 118.

reporting and other requirements add complexity and cost, especially for organisations operating in more than one jurisdiction".⁶ Ultimately, the Productivity Commission recommended that Australian governments pursue harmonisation of state and territory based associations legislation.

As indicated by Attachment A, the *Associations Incorporation Reform Act 2012* (Vic) ("Victorian Act"), being the most recently amended associations legislation in Australia, adopts an almost identical tiered system to that applying to companies limited by guarantee under the Corporations Act, as does the new ACNC Act.

The need to harmonise associations legislation was also acknowledged in the 2007 State Services Authority (Victoria) report *Review of Not-for-Profit Regulation*⁷, which recommended that associations legislation be harmonised across different jurisdictions and be closer aligned with the Commonwealth because nationally consistent regulation would reduce the administrative burden. Similarly, in a joint submission to Consumer Affairs Victoria prior to the amendments to the Victorian Act, the professional accounting bodies (CPA Australia and the Institute of Chartered Accountants in Australia) expressed concern about the inconsistent requirements across Australia for not-for-profits generally, whether they are incorporated associations or companies limited by guarantee.

2. Objectives

The key policy objective is to produce a system of financial reporting that enables associations to discharge their financial accountability obligations whilst minimising the regulatory burden by ensuring that these obligations are commensurate with the risk presented by each association.

3. Options to Address the Issue

Current legislative requirements

The Act currently requires all incorporated associations to keep accounting records and to present their accounts to members at an annual general meeting but there is no requirement that those accounts are independently scrutinised, either through a review or audit of the accounts.

Over time, various changes regarding the Act's financial reporting and auditing requirements have been proposed, either through a two-tier or three-tier system of reporting, with escalating requirements as the size of the association increases.

The Associations Incorporation Bill 2006 ("Green Bill")

The Green Bill (which was the subject of extensive public consultation in 2006) proposed a three-tier system of financial reporting. The key features of the Green Bill were as follows:

- A three-tiered system, based on the revenue or assets of the association.⁸
- Tier 1 associations allowed to use either the cash or accrual methods of accounting.
- Financial statements for all associations must give a true and fair view of the financial

⁶ Page 113.

⁷ September 2007.

⁸ Tier 1 – revenue or assets <\$100 000; tier 2 - \$100 000 to \$1 000 000; tier 3 - >\$1 000 000.

performance and position of the association.

- Financial statements for tiers 2 and 3 associations must comply with accounting standards.
- All associations must undertake an “audit”⁹, with the qualifications of the “auditor” increasing as the size of the association increases (i.e. tier 1 need not be audited by a professional, tier 2 by an accountant or auditor, tier 3 by a registered company auditor).

The Department’s report on the Green Bill, *Your Views in Summary – an Overview of Written Submissions to the Associations Incorporation Act Review* (“Your Views in Summary report”), revealed strong support for a three-tiered system with reporting and auditing requirements that increase with the size of the association, strong resistance to public accountability from small incorporated associations and suggestions that the \$100 000 threshold for tier 1 associations should be increased.

2010 Cabinet approval to print

Post the Green Bill, a policy view was taken that a three-tier system added too much complexity for associations and that a two-tier system was more suitable. The decision to introduce a two tier system was publically disclosed in the Response to Public Comment on the Green Bill in April 2008.

On 16 August 2010, Cabinet approved drafting instructions to amend the Act whereby the financial reporting and auditing requirements of associations would be based upon a two-tier classification of associations according to size. A PIA was completed in relation to the 2010 Cabinet Submission and RGU approved the PIA.

Subsequent to the 2010 Cabinet submission, the Department met with experts who specialise in accounting and auditing of not-for-profit entities, including charities and incorporated associations (“Accountants Working Party” or “AWP”). The AWP submitted that a three-tier system of financial scrutiny for associations was more appropriate than a two-tier system, and they noted that the Corporations Act had been amended in 2010 to introduce a three-tier system for companies limited by guarantee. Given the three-tier system applicable to companies limited by guarantee, it was suggested that the introduction of a two-tier system in WA may be open to criticism on the basis that it would impose a higher requirement, being a formal audit, for associations with revenue over \$500,000 when companies limited by guarantee with the same revenue need only undertake a review. Such disparity in formal audit requirements may be viewed as additionally unsuitable, given the ability for associations to transfer their incorporation to the Corporations Act. The AWP also favoured imposing less stringent auditing requirements on smaller associations by allowing for a review.

The Department found that a major advantage of Western Australia adopting the three-tier system of the Corporations Act (which Victoria has also adopted) rather than the two-tier system put forward in the Cabinet submission, was that there would be greater financial accountability for associations with revenue between \$250 000 and \$500 000, as they would be required to undertake at least a review. However, the burden on associations with revenue between \$500 000 and \$1 000 000 would be reduced as they would benefit from the cost savings of undertaking a review rather than an audit. Arguably, the option of a review for tier 2 associations allows for some level of financial accountability while placing the burden of an audit on associations with significantly more revenue (i.e. greater than \$1 000 000).

Accordingly, the proposed financial reporting requirements under Part 5 of the Bill retain a

⁹ Since a qualified professional was not required to perform the independent scrutiny of the accounts, note that the audit required was not an audit within the technical meaning in the auditing standards.

three-tiered system, but also minimise the reporting burden on smaller associations by increasing the threshold of tier 1 to \$250,000 and not requiring a review or audit for tier 1 as follows:

- Tier 1: <\$250 000 revenue¹⁰ – financial statements prepared using the cash or accrual methods of accounting and must give a true and fair view¹¹, with no review or audit required (unless a review or audit is required by members or directed by the Commissioner);
- Tier 2: \$250 000 to \$1 000 000 revenue – financial statements must comply with accounting standards and must give a true and fair view; must be reviewed by a member of a professional accounting body¹² (unless an audit is required by members or directed by the Commissioner);
- Tier 3: >\$1 000 000 revenue – financial statements must comply with accounting standards and must give a true and fair view; must be audited by a member of a professional accounting body holding a public practice certificate.

The proposed financial reporting requirements of the Bill, which are a significant improvement on the Green Bill and the Act are based on the following key design principles:

- Classifying an association as tier 1, 2 or 3 for reporting purposes based on revenue, which is easy to calculate but not overly burdensome on associations that are asset rich but revenue poor i.e. those that generate small amounts of revenue but that hold a large asset that it has no intention to sell (such as the property where the association's activities are conducted).
- Consistent with stakeholder feedback, increasing the revenue threshold for tier 1 associations with respect to a financial year from \$100 000 to \$250 000, with the result that more associations will fall into tier 1, where the reporting requirements are minimal and there is minimal departure from the requirements under the Act as it currently standards.¹³
- Not requiring tier 1 associations to review or audit their financial statements in order to minimise the regulatory burden on the vast majority of associations, estimated to be at least 90% of the total number of associations incorporated in WA.
- Building in safeguards to allow for individual circumstances of an association i.e. the members may, by resolution, require a review or audit of a tier 1 association or audit of a tier 2 association; a review or audit may be directed by the Commissioner; the Commissioner may exempt an association from the requirements of a particular tier where the association has experienced a one-off increase in revenue for a financial

¹⁰ in respect of a financial year. Note also that the Bill's tier thresholds are based on revenue only so as to not be overly burdensome on associations that generate small amounts of revenue but that may hold a large asset that it has no intention to sell (such as the property where the association's activities are conducted).

¹¹ of the financial position and performance of the association.

¹² Note that the qualifications of reviewers and auditors will be prescribed under the regulations. Stakeholders that have been consulted on the Bill are also aware of these proposed qualifications. Note that the qualifications for a reviewer are consistent with the Corporations Act, the ACNC Act and the Victorian Act. The qualifications for an auditor are lower than the Corporations Act and the ACNC Act, because of stakeholder concerns about the shortage of registered company auditors in WA, which has also been confirmed by accounting/auditing experts.

¹³ Unlike the Act, the Bill expressly permits either cash or accrual accounting. This is an important step in continuing to minimise the reporting burden on smaller associations.

year (that would otherwise push the association into a higher tier).

- Allowing a tier 2 association to undertake a review of its financial statements instead of an audit.¹⁴

Further, it is intended that the proposed regulations that are to be made under the Act will allow an audit to be performed by a member of a professional accounting body (holding a public practice certificate) as an alternative to a registered company auditor, given stakeholder concerns (expressed in the Your Views in Summary report as well as elsewhere) that there were not enough accountants and auditors in public practice to service a high level of audit requirement.¹⁵

The Green Bill required a solvency declaration to be prepared by the committee members of all associations. The new requirements under the Bill only require a declaration with respect to tier 2 and tier 3 associations (in the form of a management committee declaration, which includes a declaration as to solvency, and a declaration that the financial reports have been prepared in accordance with the Act). This is also a much-needed change because it ensures that tier 1 associations can continue to use the cash method of accounting, under which it is technically impossible to produce a solvency declaration because assets and liabilities cannot be fully reported.¹⁶

4. Impact Analysis

There are approximately 17,542 incorporated associations in Western Australia. Given that financial information is not lodged with the Commissioner, and there is no other means of obtaining revenue figures for each of these associations, we are unable to calculate the precise spread of associations between the three tiers. However, based on statistics from other states, the Department estimates that the vast majority of associations, at least 90%, will fall within the tier 1 classification. Given the amount of rural associations in WA this is a conservative estimate, and may be closer to 95% in reality.

The balance of associations will fall within tiers 2 and 3. An accounting and auditing expert that specialises in the not-for-profit sector (including incorporated associations) has advised the Department that there may be more associations falling within tier 3 than tier 2. The Department estimates that 3% of associations will fall within tier 2 and 7% of associations within tier 3. One reason for the larger proportion in tier 3 than tier 2 is because the company limited by guarantee legal structure is used less in WA than in other states i.e. the company limited by guarantee structure under the Corporations Act being an alternative to incorporation under the Act.

Tier 1 associations

There will be no additional cost imposed on at least 90% of associations because the requirements for tier 1 associations under the Bill are similar to the Act i.e. basic accounts can be prepared and they will not be required to be reviewed or audited. This means that tier 1 associations that choose to have their financial statements prepared by non-qualified persons with knowledge of basic bookkeeping can continue to have their statements prepared in this manner and continue to keep reporting costs to a minimum.

¹⁴ This is a lower level of assurance (and sometimes cheaper than an audit) given that the scope of the work for a review (being a negative level of assurance) is narrower than an audit (being a positive level of assurance).

¹⁵ Page 20.

¹⁶ For example, cash accounting does not account for liabilities that are outstanding, but that have not yet been fully paid such as overdue amounts to suppliers, or accrued wages and salaries or other employee entitlements.

Given that there is no additional cost imposed on tier 1 associations, the focus of this analysis is on tier 2 and tier 3 associations.

Tier 2 and tier 3 associations

There are four main types of reporting to government agencies by not-for-profits, including tier 2 and tier 3 incorporated associations, depending on the nature of their activities¹⁷:

- a) financial reporting associated with the legal structure under which they are incorporated – in Western Australia this means the requirements of the *Associations Incorporation Act 1987*, under which 17,542 associations are currently incorporated (and going forward, under the *Associations Incorporation Act 2014* (WA);
- b) requirements of fundraising legislation – in Western Australia this means the *Charitable Collections Act 1946* (WA) (“Charitable Collections Act”), of which 720¹⁸ of the 1,206 licensees (60%) are incorporated associations;
- c) information required for endorsement for concessional tax treatment – at the Commonwealth level this is determined by the Australian Taxation Office. One important tax concession for not-for-profits is deductible gift recipient status (“DGR”). The Department understands that the number of associations with DGR status is estimated to be around 2,919¹⁹. These associations also fall under the jurisdiction of the *Australian Charities & Not-for-Profits Commission Act 2012* (Cth) (“ACNC Act”); and
- d) financial, governance and performance information required for obtaining or acquitting government funding (such as grants) or government funded service delivery contracts - the Department does not have access to the data regarding the number of associations with Commonwealth and state government grants or contracts. However, it is likely to be a significant proportion, given the nature of activities undertaken by incorporated associations. For example, sporting associations often receive grants and some associations enter into contracts with government agencies for the delivery of social services etc.

In addition, an incorporated association may prepare financial reports as a requirement under its rules, as a matter of best practice and/or for marketing purposes (e.g. for release on its website).

BENEFITS

(A) Promote harmonisation and minimise reporting burden

The 2010 Productivity Commission report *Contribution of the Not-for-Profit Sector* (page 116) noted that “NFPs’ compliance costs are minimised when they have to face a single clear set of requirements ... with common reporting standards and requirements, and where one report satisfies most, if not all, obligations ...” The challenge is to provide a regulatory system that offers these advantages, but that is proportionate to the risks posed by different types of NFPs”.

The proposed financial reporting requirements promote harmonisation with other reporting regimes and therefore minimise reporting burden because they require tier 2 and tier 3 associations to prepare financial reports that: a) are consistent with, or less onerous than, requirements under other legislation, such as the *Charitable Collections Act* and the *ACNC Act* and b) being in a “standardised form” that complies with accounting standards can satisfy reporting requirements outside of legislation (e.g. required by grants, contracts, marketing

¹⁷ Productivity Commission report *Contribution of the Not-for-Sector* (2010, page 129)

¹⁸ Note that some of these are incorporated under associations legislation in other states and territories.

¹⁹ According to figures provided to the Department in the process of the Department’s consultation with the Commonwealth and States and Territories regarding reducing regulatory duplication under the *ACNC Act* and regulations. We understand these figures to be derived from the ATO.

purposes etc).

Charitable Collections Act

The Charitable Collections Act requires all licensees to prepare audited financial statements and lodge these with the Commissioner for Consumer Protection i.e. with the Department. The Bill only requires tier 3 associations to have their financial statements audited, and there is no requirement that the reports of any associations are lodged – the Bill retains the status quo of the Act in terms of self-reporting to members only, rather than lodging with the Commissioner.

As incorporated associations are member-driven organisations, it is considered appropriate that reporting on the financial situation of an association be to its members rather than the Commissioner. The association's membership is best placed to assess the financial situation of the association. Associations have expressed a very strong preference to continue with the current arrangement of reporting to members only. However, the Bill will introduce a provision to require associations to provide an annual statement to the Commissioner which will act to verify an association's continued eligibility for incorporation under the Act, and this will include basic financial information (such as revenue). Further, the Commissioner will have the power to request financial information from an incorporated association in addition to the Commissioner's general investigation and enforcement powers.

ACNC Act and Corporations Act (re companies limited by guarantee)

The Bill's financial reporting requirements are almost synonymous with the ACNC Act²⁰. This is because both the requirements under the Bill and the ACNC Act are based on the requirements for companies limited by guarantee under the Corporations Act. The Department based the three-tiered reporting requirements under the Bill on the requirements for companies limited by guarantee because companies limited by guarantee are similar in nature to associations, and are an alternative legal structure for associations (and in fact associations can transfer their incorporation under the Bill to the Corporations Act and become companies limited by guarantee) and because the companies limited by guarantee requirements are considered to be a model for other jurisdictions in promoting harmonisation between jurisdictions (Productivity Commission report).

Although it is desirable for harmonisation between the Bill and the ACNC Act (because some associations report under the ACNC Act) a repeal of the ACNC Act would not change the Department's financial reporting proposals in the Bill because the Bill's provisions are based on the provisions of the Corporations Act for companies limited by guarantee.

The only significant difference between the requirements under the Bill and the ACNC Act²¹/Corporations Act is that the regulations under the Bill will allow an audit to be conducted by a member of a professional accounting body holding a public practice certificate, being a less onerous requirement than the ACNC Act and Corporations Act which require an audit to be conducted by a registered company auditor. This difference is driven largely by stakeholder concerns, supported by expert advice, that there is a shortage of registered company auditors in WA, particularly in rural areas.

Other reporting regimes

The Bill requires tier 2 and tier 3 associations to prepare "standardised" reports i.e. they are in a form that complies with Australian accounting standards, which are a benchmark for financial reporting in Australia. This means that the reports can often satisfy the reporting obligations under other regimes. For example, many associations receive government grants from Commonwealth and state government agencies. In the case of grants administered by Commonwealth agencies subject to the *Financial Management and Accountability Act 1997*

²⁰ Note that some of the financial reporting requirements are found in the regulations to the ACNC Act.

²¹ The ACNC Act incorporates the Corporations Act requirements re audit by reference.

(Cth) ("FMAA"), associations reporting on grants received must comply with the National Standard Chart of Accounts²² ("SCOA") when providing financial information to the agencies. As the SCOA is based on the Australian accounting standards, associations that report to Commonwealth agencies using SCOA can use the same information in reporting to members under the new financial reporting provisions in the Bill.

In the case of reporting to state government agencies, these requirements differ from agency to agency. Similarly, requirements under contracts may differ from contract to contract. The Department cannot comment on such requirements. However, by way of example, the Department has received advice that the financial reporting requirements for associations that provide Home and Community Care ("HACC") in WA are more onerous than those in the Bill.

(B) Meets the standards of accountability demanded by stakeholders

A three-tier system of financial reporting was overwhelmingly supported by stakeholders who provided submissions to the Green Bill. Further, stakeholders have shown strong support for the current three-tier system in the current Bill, including CPA Australia which is a leading professional accounting body.

The proposed financial reporting requirements under the Bill balance the need for associations to discharge their financial accountability to members and other stakeholders, with the need to minimise the costs of compliance and regulatory duplication. Stakeholders providing feedback to the Green Bill demanded accountability by larger associations, but also wanted to minimise accountability for smaller associations.

The Bill's three-tiered system of reporting maintains the status quo for smaller associations, whilst ensuring that associations with greater funds at risk are able to meet higher standards of financial accountability demanded from the public, and evidenced in the large proportion of complaints received by the Department about inadequate financial reporting to members, allegations of financial mismanagement and concerns about the insolvency of associations.

The continued approach of reporting to members, rather than the Commissioner will also ensure that costs are minimised, both for associations (e.g. in not paying a lodgement fee) and also for the Department, who would be required to process and assess 17,542 financial reports if lodgement was required.

The three-tier system, particularly the review and audit requirements of tier 2 and tier 3 associations respectively is a marked improvement on the current Act. It is expected to alleviate member concerns about inadequate reporting, financial mismanagement and fraud, given that reviews and audits provide a level of assurance to members and other stakeholders that the association's reports have been properly prepared and give a true and fair view of the financial position and performance of the association.

Given the sources of associations' funding (members, the public, State & Commonwealth government, service recipients) and the activities they perform which provide significant community benefit (e.g. sport and leisure activities, charitable activities, health and community care, retirement living etc) it is important to ensure that community resources are being employed in worthwhile areas and the funds are being adequately controlled and managed. As indicated above, the Not-for-Profit Fraud Survey 2014 reveals that fraud is a real issue for not-for-profits, and the risk of fraud increases as the entity's size increases. The three tier system is best aligned to addressing this issue by requiring greater transparency and accountability as the association's size increases.

In the process of preparing the management committee's declaration, committee members of

²² SCOA is an agreed list of account categories and data dictionary for Australian governments to use when requesting financial information from not-for-profit (NFP) organisations. Its objective is to simplify and improve consistency of financial reporting by NFP organisations to Commonwealth, State and Territory government agencies" (Australian Government, Department of Finance and Deregulation – Circular 2011/03).

tier 2 and tier 3 associations will be required to make an assessment of the solvency of the association. The accountants and auditors also make such an assessment in preparing and auditing the financial reports. Information about the solvency of the association is important, because it can assist committee members in preventing the association from trading whilst insolvent (which is an offence under the Act) and enable the management to take remedial action to save the association. Further, it will prevent the association from unnecessarily wasting assets and incurring liabilities prior to winding up.

COSTS

Tier 2 and tier 3 associations that do not currently prepare financial reports similar to those required by the Bill for other purposes will incur some additional costs. However, the number of these associations is likely to be low, being a small subset of the 3% (i.e. less than 526) of tier 2 associations.

Tier 3 associations

It is expected that tier 3 associations, as a bare minimum, would already be preparing financial reports that would be compliant with the Bill, including being independently audited by a qualified professional. In addition to all the above mentioned sources of financial reporting requirements, these associations have significant resources under their control, and face accountability to stakeholders regardless of statutory requirements. Examples of tier 3 associations who already prepare audited financial reports are as follows:

- St John of God Healthcare (Inc)– \$1.07 billion revenue²³
- RACWA (Inc) – \$560 million revenue
- Ocean Gardens (Inc) - \$8.15 million revenue.

Tier 2 associations

It is some of the tier 2 associations that, because of their size, may not already be preparing financial reports in accordance with the requirements under the Bill. However, the proportion of the 3% of tier 2 associations (i.e. less than 526) that would not already be reporting in this manner would be low because an association would have to not be subject to **any** of the following for this to be the case:

- does not hold a charities licence under the Charitable Collections Act (which requires the audit of the financial reports, being a higher requirement than the Bill's tier 2 requirements);
- is not registered under the ACNC Act (which requires the preparation of financial statements that comply with accounting standards and a review of the reports, being the same requirement as the ACNC);
- does not receive any state or Commonwealth grants (for which the reporting requirements vary, except for grants received from Commonwealth agencies falling within the FMAA, who must adopt SCOA, which is based on accounting standards and therefore similar to the Bill's tier 2 requirements);
- does not have a contract with a state or Commonwealth government body for the delivery of services (the reporting requirements vary from agency to agency, but for example, associations providing Home and Community Care ("HACC") in WA are subject to more onerous reporting than under the Bill;
- does not, as a matter of best practice, have a requirement in its rules that it prepare

²³ In all three cases, for the year ended 30 June 2013.

financial reports that comply with accounting standards and are reviewed or audited (bearing in mind that many associations require reports that are reviewed or audited, including smaller associations); and

- does not prepare financial reports for marketing purposes (e.g. on its website).

In short, although exact numbers cannot be provided, it is estimated that a very small proportion of the tier 2 associations will incur any costs in complying with the Bill's reporting requirements. Further, the cost of a review is low, and for a small tier 2 association, the cost could be as little as \$2,000 (an audit of a tier 3 association is estimated at \$5,000, although this could vary significantly based on the size and nature of the association's operations). These are not significant amounts when compared to the total revenue of the relevant associations, and in light of the size of funds, or assets that could be lost, or debt incurred, if an association continues to operate while insolvent.

The Department has received advice from an accounting and auditing expert (specialising in the not-for-profit sector, including incorporated associations) that the financial reporting provisions **would not** be a significant cost to tier 2 and tier 3 associations given the other reporting regimes (either in legislation or elsewhere).

5. Consultation

The Green Bill was made available for public comment for a period of five months from November 2006 to April 2007. Some 316 submissions were received during the consultation period and these submissions were taken into account in further iterations of the Bill, including the current Bill. As indicated in section 3 above, the report Your Views in Summary report revealed:

- strong support for a three-tiered system with reporting and auditing requirements that increase with the size of the association;
- strong resistance to public accountability from small incorporated associations; and
- suggestions that the \$100 000 threshold for tier 1 associations should be increased.

The current Bill addresses all of the above concerns.

Given the previous extensive public consultation on the Green Bill, the Department has undertaken a more targeted approach to consultation on the current Bill. In 2013, the Department held a series of meetings with a number of key stakeholders, representing a wide range of associations. These include, but are not limited to, the Western Australian Council of Social Services, Clubs WA, Sports Federation of WA, Basketball WA, Triathlon WA, WA Wildlife Rehabilitation Council and Mr Noel Harding, representative for the religious and charitable sector. The Department has also consulted with the Department of Sport and Recreation, given that many associations are formed for the purpose of sporting activities.

The Department regularly engages with these stakeholders via written correspondence to keep them abreast of the developments in the Bill. The input received by the Department to date from its stakeholders indicates strong support for the key provisions of the Bill, including the financial reporting provisions.

During the formulation of the policy, and the drafting of, the financial reporting provisions, the Department worked closely with two experts who specialise in accounting and auditing of not-for-profit entities, including charities and incorporated associations ("Accountants Working Party"). The provisions were also released to CPA Australia (i.e. a leading professional accounting body) for comment, as well as the Australian Institute for Company Directors. Where appropriate, this feedback has been incorporated into the Bill.

The Department has also sought comment on the proposals from the Law Society of WA, the Consumer Advisory Committee, the Property Industries Advisory Committee and the Motor Vehicle Industry Advisory Committee. The Department has also provided an update of the key aspects of the Bill (including the financial reporting requirements) to stakeholders via the Department's website. The Department has continued to receive stakeholder support for its proposals and has not received any adverse feedback on the financial reporting requirements.

6. Preferred Option

In considering all the available information, including the benefits and costs of the proposed financial reporting requirements, the Department does not believe that the financial reporting provisions impose a significant cost burden on incorporated associations. As indicated above, the vast majority of associations are tier 1, for which the reporting requirements under the Bill maintain the status quo of the current Act. Of the anticipated 526 associations that are tier 2, it is very likely that these associations would already be reporting in some capacity as a result of their activities. Given the size of tier 3 associations (i.e. revenue of more than \$1 000 000) the Department considers it would amount to regulatory failure not to require the basic level of reporting required under the Bill.

7. Implementation and Evaluation Strategy

The financial reporting requirements apply in respect of each financial year of an incorporated association that commences on or after 1 July 2016 so that the first financial statements that comply with the new Act are prepared for the financial year ending in 2017.

For example, associations with a financial year that runs 1 July to 30 June would have to comply from 1 July 2016 and produce their first financial statements complying with the new Act for the year ended 30 June 2017. Associations with a financial year that runs 1 January to 31 December would have to comply from 1 January 2016 and produce their first financial statements complying with the new Act for the year ended 31 December 2017.

The Department has chosen to provide this significant lead time to ease associations into the new requirements, although many associations may already have their accounts in a form that allows them to comply immediately with the financial reporting requirements.

The Department intends to review the provisions in five years' time, and in particular whether the revenue thresholds for each of the three tiers is appropriate, given that the Bill enables the revenue thresholds to be modified by the regulations.

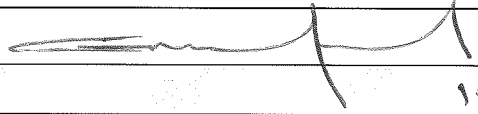
As part of the consultation process, the Department has already started to inform stakeholders of the proposed Bill, including the new financial reporting requirements. The Department has met with a number of stakeholder groups, such as the Western Australian Council of Social Service (i.e. the peak body for the social service sector in WA, representing a large number of incorporated associations) and Clubs WA (i.e. the peak body for clubs in WA, including many sports associations) and has provided updates on the proposed legislation. The Department will continue to inform such representative groups of the reforms, because these groups disseminate information to member associations.

The Department's education strategy is multi-faceted. Associations will be informed about the financial reporting and other requirements of the Bill through: direct mail correspondence; regular updates on the Department's website and information sessions.

Certification

By certifying this form, you are agreeing that,

- this RIS has been prepared in compliance with the Western Australian Government's requirement for Regulatory Impact Assessment and to facilitate consultation and decision making effectively.
- to the best of your ability, all information provided within this document is true and correct.

	Certified By	
Name	Gerry Milford	17/6/14
Position	Manager, Legislation & Policy	
Phone Number	92820682	
Email	gerry.milford@commerce.wa.gov.au	

Attachment A – Comparison of financial reporting between Western Australia and other jurisdictions

	WA BILL (2014) ¹	VIC (2012) ²	NSW (2009) ³	NT (2003) ⁴	ACT (1991) ⁵	CTH (ACNC) (2012) ⁶	CTH (CA) (2001) ⁷	SA (1985) ⁸	QLD (1981) ⁹	TAS (1976) ¹⁰	WA ACT (1987) <i>Current</i> ¹¹
Tiered reporting based on size	✓	✓	✓	✓	✓	✓	✓	✓	✓	✗	✗
Accounting standards (at least for larger tiers)	✓	✓	✓	✓	✓	✓	✓	✗	✗	✗	✗
Review or audit	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✗

¹ Associations Incorporation Bill 2014

² Associations Incorporation Reform Act 2012 (Vic)

³ Associations Incorporation Act 2009 (NSW)

⁴ Associations Act 2003 (NT)

⁵ Associations Incorporation Act 1991 (ACT)

⁶ Australian Charities and Not-for-profits Commission Act 2012 (Cth) and Australian Charities and Not-for-profits Commission Regulations 2013 (Cth)

⁷ Corporations Act 2001 (Cth) and Corporations Regulations 2001 (Cth)

⁸ Associations Incorporation Act 1985 (SA)

⁹ Associations Incorporation Act 1981 (Qld)

¹⁰ Associations Incorporation Act 1976 (TAS)

¹¹ Associations Incorporation Act 1987 (WA)