

SUPPLEMENTARY GUIDANCE ON THE CONTROL & SECURITY OF FUNDS

Control and security of funds disbursed by Australian NGDOs to third parties – Supplementary Guidance to Code of Conduct clause 2.8

This paper should be read in conjunction with ACFID Code of Conduct clause 2.8 and the related Guidance. This paper does not form part of the ACFID Code of Conduct or the Code Guidance Document.

*Approved by the ACFID Code of Conduct Committee on 21 May 2009.
Approved by the ACFID Executive Committee on 17 June 2009.*

1. **Introduction**

This paper sets out a range of issues for consideration by Australian Non-governmental Development Organisations (NGDOs) which are relevant to the control and security of funds transferred to third parties.

This paper does not attempt to address the specific regulatory or internal controls that may affect individual organisational structures and their application in specific scenarios. Each organisation must take into account the regulatory framework within which it operates, the affiliate/partnership network to which it belongs as well as the contractual requirements it has in place with donors and its stewardship responsibilities towards its supporters.

2. **Factors influencing control of funds transfer**

The following section sets out some of the existing regulations and arrangements that may drive or shape the funds transfer control and security mechanisms of organisations.¹

2.1 **Corporate Body Requirements**

Most Australian NGDOs are public companies limited by guarantee.

Examination of relevant law leads to the conclusion that the funds raised by a company limited by guarantee for charitable purposes are the property of the company (or assets) that should remain under the control² of the company until:

- disbursed or utilised for the appropriate charitable purpose; or
- otherwise used by the company in accordance with its constitution and law.

¹ Please note that the general commentary on legal issues set out below does not constitute legal advice or a legal opinion and should not be relied upon. The commentary has been provided for discussion purposes only.

² Control in this context would include appropriate contractual arrangements with a third party (such as a global affiliate) holding or managing the funds on behalf of the Australian company.

It follows that funds transferred by Australian NGDOs which are companies to third parties (such as an international affiliate) for further disbursement to beneficiaries should be held and managed by the third party in accordance with the instructions of the Australian NGDO. The Australian NGDO should remain in control of funds.

2.2 Duties of directors' of a company limited by guarantee

Directors have a duty to act in good faith for the benefit of the company as a whole. This duty would extend to ensuring that funds raised by the company are managed appropriately for the benefit of the company (noting that the benefit of the company in this context would include use for the relevant charitable purpose).³

2.3 State fundraising legislation

In at least two states in Australia (WA and NSW) charitable collections legislation requires that funds not being immediately applied to the purpose or object of an appeal must be held or invested in a manner allowed for a trust fund. This has the effect of requiring those responsible for holding or investing the funds (i.e. the directors of the Australian company) to act as if they were trustees of such funds.⁴

2.4 Tax legislation

In general, organisations eligible for tax concessions on the basis of their status as a charity must pursue the charitable purpose for which they have been established.

If an organisation operates a gift fund endorsed by the Australian Taxation Office as to be a deductible gift fund (for example, an Overseas Aid Gift Fund) then funds flow into and out of the fund must be monitored through the separate recording of:⁵

- all gifts and contributions, through a bank account or other cash management system for money, and a register for property;
- transfers from the gift fund, whether as payments, disbursements or for use by the fund, authority or institution; and
- investment returns on money or property that have been transferred out.

Money or property of a gift fund should not be mixed with other money or property of the organisation.

2.5 Anti-money laundering and counter-terrorism financing legislation

Relevant Commonwealth legislation includes:

- Financial Transaction Reports Act 1998;
- Anti-Money Laundering and Counter-Terrorism Financing Act 2006;
- Charter of the United Nations Act; and
- Part 5.3 of the Criminal Code Act (as amended by the Security Legislation Amendment (Terrorism) Act 2002.

³ It is worth noting however that, if, following due consideration, the directors of the company reasonably decide that it is in the best interests of the company (and in accordance with its constitution) to transfer funds to a global affiliate for the global affiliate to use as it determines this would not constitute a breach of the directors' fiduciary duties – although it may have implications for tax status and donor promise obligations (see below).

⁴ Relevant duties of trustees include a duty to protect and preserve trust property; to exercise a power of investment with, at a minimum, the care, diligence and skill that a prudent person would exercise in managing the affairs of other persons. In fulfilling these obligations a range of factors needs to be taken into account including: the need to maintain the real value of the capital or income; the risk of capital or income loss or depreciation; the potential for capital appreciation; and the likelihood of inflation affecting the value of the proposed investment or other trust property.

⁵ Gift fund requirements, Fact sheet for deductible gift recipients (Non-profit), on the ATO website at: http://ato.gov.au/content/downloads/NPC_00013269_n3194.pdf

Australian organisations must take account of the impact of the above legislation on their activities in Australia when: accepting money and goods from supporters; paying vendors; and funding its domestic programs. Organisations must also take account of the legislation in their field facing activities including when sending money to global affiliates or directly to programs.

Reporting obligations under the Financial Transaction Reports Act are limited to the mandatory reporting of cash transfers of more than \$10,000 or more into or out of Australia (cash or coin – not electronic transfer). From December 2008, the reporting requirements under the FTRA will be replaced by equivalent obligations under the Anti-Money Laundering and Counter-Terrorism Financing Act. This change in legislative underpinning does not change the underlying obligation to report cash transfers of \$10,000 or more.

Australian organisations are prohibited by the Charter of the United Nations Act from dealing with persons, or assets owned or controlled by persons, proscribed by DFAT and/or the AG's Department as having a connection with terrorism. This includes directly or indirectly making an asset (including money) available to a proscribed person or entity, without permission from DFAT and/or the AG's Department.

In addition, Part 5.3 the Criminal Code Act makes it a criminal offence to:

- intentionally get funds to or from a terrorist organisation, knowing that it was a terrorist organisation or being reckless as to whether the organisation was a terrorist organisation (section 102.6); or
- intentionally provides support to an organisation to undertake a terrorist act, knowing that, or being reckless⁶ as to whether, the organisation was a terrorist organisation.

The DFAT and AG's lists of proscribed organisations can be found at www.dfat.gov.au (site index/Counter Terrorism/What Australians and Australian Businesses need to know/Consolidated List) and www.ag.gov.au (National security and counter terrorism/terrorist organisations/Which organisations have been listed?) respectively.

2.6 Contractual arrangements

Contractual arrangements may be established with third parties to whom Australian organisations transfer funds to recognise and establish responsibilities, control, duties and obligations.

Project Agreements and Funding Agreements should contain provisions dealing with the following:

- how much funding will be provided (and whether in tranches);
- when funding will be made;
- how funding will be effected (bank accounts or perhaps through internal accounting mechanisms of the international network); and
- funds must be used for the specific project to which the contract relates.

In addition to the above matters, which deal with the “mechanics” of funding, contractual arrangements can establish good stewardship practices. For example, contracts should also:

- require return of surplus funds;

⁶ “Recklessness” includes not having a system in place to check the source and end use of funds.

- require reimbursement or indemnification if any funds were not used for the specific project to which the contract relates;
- require any interest that may be earned to be applied also towards the project; and
- require any exchange rate gains to be applied also towards the project.

2.7 Donor promise

Failure to meet donor promise invariably has a detrimental impact upon the reputation and standing of an organisation.

While not a formal legal obligation, satisfaction of an organisation’s donor promise should provide impetus for an organisation to establish appropriate controls and procedures to achieve at least the following:

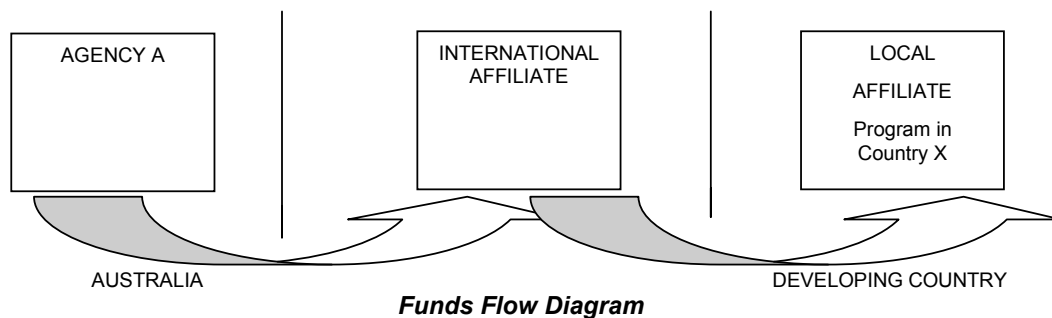
- ensure that funds are applied in the manner agreed (e.g. that the funds are actually disbursed to a specific program for which they have been donated or provided in the first place); and
- manage and invest funds well to protect the value of the funds which have been donated or provided to the organisation.

It may be worth considering the extent to which concepts of good stewardship are implied in the donor promise of an organisation – perhaps adding extra weight to the need for organisations to ensure funds reach the appropriate target.

3. Example scenarios:

The following example scenarios demonstrate possible practical application of the control mechanisms referred to in this paper in order for NGDOs to be compliant, legal and legitimate with regards to funds transfer. Scenario 3.1 provides a step-by-step example of where control mechanisms referred to in Section 2 may be applied at the various stages funds are transferred for international affiliates. Scenario 3.2 provides guiding principles for transfer of funds to independent third parties (i.e. non international affiliates or partners).

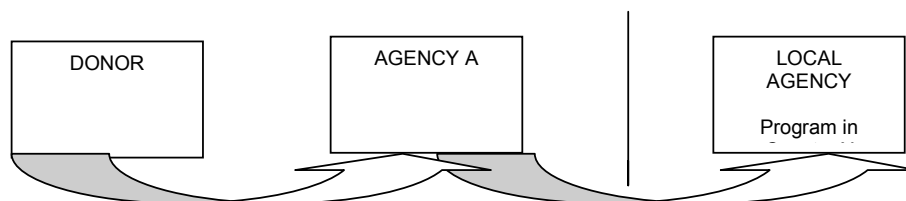
3.1 Funds transferred to an International Affiliate



- **Agency A is a company limited by guarantee and maintains a deductible gift fund. Agency A is a member of an international affiliation.**
- **Agency A receives a donation eligible to be applied to its Overseas Aid Fund for an approved program in Country X and deposits funds in OAF bank account.**

- *Controls influenced by director's duties, tax requirements, state fundraising legislation (if applicable).*
- **Funds are allocated by Agency A to program in Country X. The allocation decision is made following internal process taking into consideration strategic fit and financial and budgetary analysis of the program. Program is to be delivered by Local Affiliate of Agency A in Country X, where Agency A is involved in all stages of the Program Management Cycle.**
- *Contractual arrangement entered into between Agency A and Local Affiliate, which incorporates the guidance in the Explanatory Notes of the Guidance Document for Clause 2.8 (for all organisations), and adheres to the Financial Systems and Risk Management criteria set out in section E of the AusAID Full Accreditation Criteria (for all organisations accredited with AusAID).*
- *Although this is not an ANCP funded program, the notes in the AusAID Full Accreditation Criteria can be applied to demonstrate control of funds. AusAID accreditation criteria can be found at: www.ausaid.gov.au/ngos/accreditation.cfm*
- **Funds are transferred from Agency A to International Affiliate.**
- *Controls influenced by FTR and AML/CTF legislation and donor promise.*
- *Foreign exchange purchase (if required) regulated by contract.*
- *Relationship between Agency A and International Affiliate regulated by contract which establishes the obligations of the International Affiliate with respect to the management of the transferred funds. International Agency may only transfer funds to Local Affiliate in Country X on instruction from Agency A (note that this may be a standing instruction). International Affiliate provides reports on status of transferred funds to Agency A upon request and/or at cyclical intervals. Transfers made by International Affiliate must be in accordance with relevant AML/anti-terrorism laws and any additional agreed internal processes and safeguards.*
- **Upon instruction from Agency A, International Affiliate transfers funds to Local Affiliate.**
- *Funds are transferred in accordance with the contractual requirements relevant to management and security of funds transfer.*
- **Local Affiliate receives funds and implements project.**
- *Agency A receives regular financial statements, program reports and evaluations from Local Affiliate for the program in accordance with contractual arrangements.*

3.2 Funds transferred from Donor to Local Agency (non-affiliate) via NGDO



Funds Flow Diagram

- **The Donor is a private company or individual.**
 - **Agency A is a company limited by guarantee and maintains a deductible gift fund. Agency A is not part of an international affiliation or partnership.**
 - **The Donor wishes to provide funding to support program in Country X administered by Local Agency.**
 - **The Donor approaches Agency A with a proposal to donate funds to support a program in Country X administered by Local Agency. Agency A has no connection with and has never worked with Local Agency.**
 - **In addition to funds specified for Local Agency, the Donor proposes to contribute an amount to cover Agency A's administrative costs. The Donor asks if Agency A is able to provide it with a tax-deductible receipt for the full amount.**
- *What controls should Agency A adopt to enable it to agree to this arrangement?*
- I. *Agency A should advise the Donor that Agency A is only able to transfer funds to an overseas program which it has approved taking into consideration strategic fit, compliance with ACFID Code standards, and the ability to exercise the appropriate level of control and monitoring of the program. Agency A should advise the Donor that it has the ability to withdraw funding from the program if at any time the program breaches contractual arrangements. If the Donor is happy to proceed, the next steps should be actioned.*
 - II. *Agency A should conduct appropriate due diligence on the Local Agency (due diligence enquiries may include such things as checking that the Local Agency is appropriately registered and bona fide, the type of programs or work it conducts, track record, standing in the sector, etc.).*
 - III. *Agency A should ensure the program is consistent with its strategic plan.*
 - IV. *Agency A should establish a contractual arrangement with Local Agency which includes:*
 - *the matters referred to in Section 2.6 above;*
 - *necessary clauses to ensure Agency A complies with legislation outlined in Section 2.5;*
 - *provides Agency A with mechanisms to ensure that it has knowledge of the program and receives ongoing relevant information (such as financial reports, progress and evaluation reports, etc.);*
 - *enables Agency A to influence program direction; and*
 - *gives Agency A the ability to withdraw funding where the program is not aligned with Agency A's priorities, including ACFID Code requirements.*
 - V. *Agency A should establish contractual arrangement with the Donor.*
 - VI. *Agency A will need to determine (in accordance with tax regulations) whether it is able to issue a tax-deductible receipt to the Donor.*