



ROCpod episode 26 – Do you know who your related parties are?

Speaker Key

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DC Hello and welcome back to *ROCpod*. My name is Declan Clifford and I'm the Executive Officer to the Registered Organisations Commissioner. Today's episode is about related parties ... who is a related party of a registered organisation and what are the compliance requirements around dealing with related parties. To help me explore this topic, I am joined by my colleague Kristina Menzies. Kristina is Senior Advisor in the ROC's Education and Reporting Team.

Thanks for your time Kristina

KM You're welcome, Declan – thanks for having me! Now the topic of related parties is an interesting one. It can get technical so I'll try to simplify the legislation and accounting standards as best as I can, so they're easier to understand.



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DC Great now, first things first: what does the term "related party" actually mean?

KM That's probably the best place to start.

Basically, a related party is a person or an entity that has links with an organisation and might be able to influence the decision-making of the organisation or benefit from those decisions.



So an example we see is a training company being run by an organisation. There's an obvious connection between registered organisations and any companies or entities that they own. They share a common purpose, and there can be links between them, like people and property.

Officers and senior managers make decisions on behalf of the organisation they belong to, so they'll be related parties too. But then, those officers can be influenced by their families... So it's important to realise, certain individuals can also be related parties of a registered organisation because they, too, can influence decisions and benefit from them.



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DC Okay, that's quite a list... so before we talk further about these definitions, maybe we should start with 'why'.

Why do registered organisations need to know whether a person or a company is a related party?

KM It's important for transparency and managing risk. You need to know who your related parties are because when you make decisions that include them, it can raise issues around conflicts of interest.

There are some legal requirements you won't be able to comply with *unless* you know who your related parties are.

DC Okay, so there are two types of compliance requirements with related parties. The first is about not making decisions that impact your own interests or your related parties' interests. The second compliance requirement is about disclosing certain transactions to members. We'll look at these one at a time.

Let's start with how related parties can affect decision-making. Kristina, why shouldn't an officer be involved in decisions that can affect their related parties' interests?

KM Well, Declan, because related parties can be in a position to influence outcomes, and transactions with related parties raise issues around possible conflicts of interest.

And sometimes that influence can be hard to spot.

It might mean the best decision isn't being made for the organisation or it could be that it *looks* like the best decision isn't being made. That can affect trust in the organisation.

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DC Do you have an example of this?

KM Sure. Let's just say you're on a committee of management and the committee is deciding who to award a cleaning contract to. And one of the companies is owned by your son.

You could be drawn to vote for your son's company, even though objectively, it's not the best for the organisation. Or maybe you won't be influenced, but it *looks* like you might be influenced or *could* influence others. Members might not trust that awarding the contract to your son was the best decision.

So the *Fair Work (Registered Organisations) Act* (what we call the RO Act) has restrictions that stop you from being involved in decisions like that.

DC We covered this in our earlier good governance episode about conflicts of interest. So if you want more details – such as what to do if you have a conflict – you can go back and listen to episode 17.

In today's episode about related parties we'll focus on the disclosure requirements.

Could you explain why certain related party transactions must be disclosed?

KM The RO Act and the Accounting Standards don't prevent related party transactions from taking place but, to minimise the risks, they require some things to be disclosed to members of the organisation. And we'll discuss that further in this episode. And that way members *know* what's been going on in their organisation and who has benefited from any decisions.

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DC So what does a related party transaction look like?

KM It can look like lots of things! A related party transaction can occur between an organisation and a relative of an officer. And even a transaction with a company that is *owned by an officer* of an organisation.

Now I have to say, there's nothing intrinsically bad about a related party. Dealing with them can be convenient and commercially beneficial to organisations.

For example, using somebody related to an officer to repair something in the office might be a quick and cost effective way to get the job done... in which case it might be ok so long as any conflicts of interests are disclosed and the decision is made for the right reasons. We also know some registered organisations generate income through companies like training organisations, and their profits are used for initiatives that benefit members.



But to manage the risks there are disclosure requirements for some transactions.

DC The *Corporations Act* has similar requirements for companies around related party transactions, doesn't it?

KM Yes, it does. Disclosing related party transactions isn't something that only registered organisations have to do. It's also accepted in the government and corporate sectors that related party transactions are regulated and disclosed.



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DC So related party transactions are permitted, but there are important policy reasons behind the regulation of them. In what areas of compliance do registered organisations need to disclose related party transactions?

KM So there are two areas where related party transactions must be disclosed in our jurisdiction:

Firstly, we see it in financial reporting.

And secondly the RO Act has other disclosure requirements for organisations, including the officer and related party disclosure statement (or what we call the ORP statement).

DC So do these two areas have the same disclosure requirements?

KM No they don't.

A financial report and ORP statement are two different compliance obligations.

A related party transaction might appear in an ORP statement, but not in a financial report of the same registered organisation, even though both of these documents require the disclosure of related party transactions.

The reason is that the Australian Accounting Standards regulate related party transactions for financial reporting while the ORP statement is a requirement under the RO Act. The definitions and requirements unfortunately aren't the same.

So you'll need to be across the requirements of both when you're preparing these documents.



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DC Okay that's interesting, but might be a bit confusing, especially if you're new to compliance work... so let's separate the issues and we'll start with the General Purpose Financial Report.



Now the Australian Accounting Standards Board (or AASB) develops financial reporting standards, setting out how financial reports have to be prepared. What kind of related parties should be included in financial reports?

KM Well, Declan, we're not going to deal with all the different related parties here, just the main types that we see all the time. I think that might be the best approach. A related party is a person or an entity if they have control or joint control of the reporting unit, significant influence over it, or if they are a member of the management of the reporting unit or of a parent organisation of the reporting unit.

DC What you've just described is from the accounting standard AASB 124 *Related Party Disclosures*. This was drafted for financial professionals. But not everybody is an accountant...I'm certainly not. So maybe you can explain who this definition typically includes for a registered organisation?

KM So the definition of a related party for financial reporting could include officers of registered organisations and their spouses and de facto partners, and any of their children or dependants.

It's an 'open' definition and its broad. Its reach can expand to other close family members who could influence, or be influenced, by that person in their dealings with the organisation.



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DC So influence is a relevant factor. Are there any other groups of people that might fall under the definition?

KM Yes, where an entity is part of the same reporting unit or is controlled by officers or their relatives.

For example, some registered organisations have interests in subsidiary companies, training organisations like I mentioned earlier, and trusts. Employee benefit funds are another example. Or let's say an officer owns a business, or their spouse does. These things are all likely to be related parties for financial reporting.

DC Okay, so it's about influence and control. What does a reporting unit need to disclose in their financial report?

KM So reporting units must disclose all related party transactions, and that includes the amounts and any outstanding balances.

But a related party transaction can occur regardless of whether a price is charged. AASB 124 requires the disclosure of all relationships between the reporting unit and its subsidiaries, even if no transactions have taken place.

And payments to key people in management – like directors responsible for controlling the entity's activities – they must be disclosed in the financial report too.



And this can include *employees* and not just officers, if they have significant influence.



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DC Okay, let's talk through some examples.

So let's say the reporting unit paid the secretary's legal costs to defend a matter before a court. Would this need to be disclosed?

KM Yes, so as the secretary is a member of the key management personnel, they would be considered a related party of the reporting unit. So yes, that would need to be disclosed in the financial report.

DC What about the example we spoke about earlier with the officer's son's company. So let's presume the officer did the right thing and removed himself from voting, and the committee of management gave the cleaning contract to the son's company anyway?

KM That's probably likely to be a related party transaction. The officer is a related party and the son is a member of their family who you would think could be expected to influence or be influenced. Also, the son probably owns the cleaning company, so he controls it. And that control makes him a related party. It should be disclosed in the report, and if you've got special rates for the contract because of the relationship, that to must also go in the report.

Of course, if you have any doubt about whether a transaction is a related party transaction, organisations should seek independent accounting advice.



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DC You've told us about the Australian Accounting Standards, and in the ROC's jurisdiction we also have the Commissioner's Reporting Guidelines. The Reporting Guidelines are issued under section 255 of the RO Act. They require additional disclosures in the financial reports of registered organisations.

So what do the Commissioner's Guidelines say about related party transactions?

KM Reporting units must disclose payments made during the reporting period to a former related party of the reporting unit, where the event relevant to that payment occurred when a related party relationship existed. The transaction must be disclosed as though the relationship existed at the date the payment is made.

DC What does that mean... Could you perhaps give us an example of that?

KM Yes sure. An example could be a reimbursement to a former officer. Even though the person was no longer an officer when they received the payment, the reporting guidelines require that the amount must be disclosed in the financial report.

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DC Okay, so you've told us about related party disclosures in financial reports ... now let's now talk about the practical lessons. So what can an organisation do to stay on top of this?

KM So there are a few very easy practical steps.

Officers must be transparent about when they see a related party involved in the organisation. If you see a decision being made to give a contract to your son's company you must tell the organisation about the relationship and not participate in the decision making process. Organisations can also help officers by having guides that explain who a related party is and keeping a register of related parties. Our conflict of interest podcast has lots of good tips to help officers navigate those kinds of issues.

And I can't emphasise how important it is to keep records! You must disclose these transactions, so you need to know the details of them, who is a related party, how are they a related party, what are the details of the transaction? Those kinds of records.

DC And having a speak up culture can also help protect the organisation. You can refresh yourself on how to build a speak up culture in podcast episode 20. And you can also refer directly to the Australian Accounting Standards, which are published on the website of the Australian Accounting Standards Board (www.aasb.gov.au).

So are there any other resources to help organisations to disclose related party transactions in financial statements?

KM Yes, I'd recommend reporting units also look at the latest edition of the ROC's Model Financial Statements. You can find them on our website.

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DC Fantastic, thank you for that tip! We'll provide a link to the model financial statements for 2021 on the webpage of this podcast episode on our website.

Now let's move to the officer and related party disclosure statement ...as you said we call this the ORP statement.

So the RO Act requires every registered organisation and branch must lodge an ORP statement with the ROC within six months of the end of *their* financial year.

Now Kristina, you mentioned earlier that the ORP statement is not the same as the financial report. While they are sometimes prepared at similar times, the ORP statement isn't audited, and unlike the financial report (which is a requirement of reporting units), every registered organisation and branch needs to lodge an ORP statement.



So there are differences with financial reports and ORP statements, including the disclosure requirements for related party transactions.

What is the purpose of the ORP statement, and what information is reported in it?

KM So the ORP statement gives greater transparency to members of organisations about certain payments. We publish them online and organisations must also provide a copy to members. Every organisation and branch is required to lodge an ORP statement – even if they are exempt from lodging a financial report.

Now if you're familiar with what the ROC's ORP Statement template looks like, you'll know there are two tables to it. Organisations and branches aren't required to use the ROC template, but most do, and they tell us that it helps with compliance.

On the first table of the template, organisations and branches disclose payments to the top five rankings of officers who receive payments. This includes salaries and other non-cash benefits (like the use of a car), a fee or honorarium received because they are an officer, and any payments to officers by related parties. Any related party payments to the officer disclosed on the ORP statement are those made in connection to their position as an office-holder. So in other words, *because* they are an officer they have received the benefit.



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DC So that's the first part of the ORP statement. There's a second table in the template isn't there?

KM Yes there is. So the second table is where you disclose payments required under section 293G of the RO Act. This includes payments made by the organisation or branch to a related party or to a declared person or body.

DC That's a quick summary of what's disclosed in the ORP statement. Let's now talk about who may be a related party of an organisation or branch under the RO Act. The RO Act provides a definition doesn't it, Kristina?

KM Yes, section 9B defines who is a related party of a registered organisation or branch.

Essentially any entity controlled by an organisation is a related party of the organisation. Now I won't go into great detail about the meaning of 'control', but it's about applying practical influence and determining the outcomes of decisions.

But this definition is narrowed by a few exceptions. So it excludes a branch, it excludes a sub-branch, a division or a sub-division of an organisation, and it also excludes a state-based association. So if your organisation has control of an entity registered under a State or Territory law and your organisation is its Federal counterpart, the state-based entity is not a related party.

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DC So the concept of control is relevant, but branches and state-based associations are excluded.

There's more to this definition, isn't there? Who else might be a related party of a registered organisation or branch under the RO Act?

KM Yes there is. We spoke earlier about the open definition under the Accounting Standards. The RO Act is different – it names certain relatives of officers as related parties.

The RO Act definition includes officers of an organisation and their spouses and relatives. "Relative" is defined to include people like grandparents and parents, children, grandchildren, siblings and even some step-relatives. The definition also includes the officer's spouse and any of *their* relatives – so it's quite a broad list.

And we also need to take this group of extended family members and include any entities that are controlled by any of them – they're related parties under the RO Act, too.

So it could include an officer's brother-in-law's construction company. And a family trust, even if the officer is not a trustee but their parents are. I guess the point I'm trying to make here is that the definition can capture a wide net of people as related parties of the organisation.

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DC The timing of relationships is also relevant, isn't it? Can you explain the relevance of timing to the definition of a 'related party'?

KM Yes, that's right Declan. The RO Act has provisions for looking-back and looking-forward under section 9B.

So an entity will be a related party if they were a related party at any time in the previous 6 months. Like, an officer who has recently left the organisation.

And transactions with potential future related parties must also be disclosed. So if it's reasonable to believe a person or company is likely to become a related party in the future, payments to them must be reported in the ORP statement.

DC What kind of transactions can be captured here? There's no time limit to this part of the definition, is that right?

KM Yes, that's right. So one example is where an organisation is in the process of purchasing a company... or even where an *officer* of the organisation is in the



process of purchasing a company. The organisation's transactions with the company may need to be disclosed. As you've said though, there's no time limit so it will depend on the circumstances. Like, how foreseeable is it that they will be a related party in the future?

I think it might help if I give you an example:

So let's say an officer buys a company. And three months before it's settled, they convince the organisation to buy an office building owned by the company for their new national office. Even though the officer doesn't control the company yet, it is already causing a possible conflict of interest. Members deserve to know about this transaction, and the RO Act requires it to be disclosed in the ORP statement.

Now I spoke earlier about record-keeping and governance systems. It's essential for organisations to encourage a culture of ongoing reporting. We know some organisations open their meetings with an invitation for officers to make disclosures. And processes like this can help identify related parties and help organisations openly disclose transactions with them.



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DC We've covered the common types of related parties. But there are more, and listeners can refer to section 9B of the RO Act for the full definition.

Here's a quick question for you, we know related parties are important to the second table about payments to related parties, but are related parties relevant to the first table about officer remuneration?

KM Yes they are! If an officer receives a payment from one of the organisation's related parties because of their role as an officer, they must disclose it to the organisation or branch. And the amount is added to their other remuneration and they might be in the first table if they're ranked in the 5 top officers by payment.

So if for example it's irrelevant if an officer earns money on the side from working in a second job ... that doesn't need to be disclosed in an ORP statement because it has nothing to do with their role as an officer of the organisation

The disclosure of related party payments to officers on the ORP statement is limited to payments from related parties of the organisation. A typical example is where they receive payments for representing the organisation on another body.

DC Back to that second table of the ORP statement ... What about payments made by the organisation or branch to related parties of the organisation. What kind of transactions are disclosed here?

KM Well there are those paid to related parties and others that follow the declaration by officers of material personal interests. These arrangements *can* potentially capture a wide group of officers' relatives.

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- DC** Can you give us an example where money is paid by an organisation to a related party?
- KM** So the example we discussed earlier, to bring it back to the cleaning company owned by the officer's son. That may need to be disclosed on the ORP statement because the organisation is paying money to a related party.
- DC** What about an example of payments to a declared person or body?
- KM** Sure. Let's say the Treasurer's wife is a bookkeeper and owns part of the bookkeeping business. The Treasurer declares a material personal interest in the business as they are required to do. because the wife's company does some work for the organisation. Payments to the bookkeeping business may need to be disclosed on the ORP statement as a transaction to a declared body.
- DC** Okay, in this episode we've spoken about the disclosure requirements of the ORP statement. But there are exemptions in section 293G of the RO Act. So that means not all related party transactions are disclosed on the ORP statement. Kristina, could you tell us more about the exemptions?
- KM** Yes, there are five exemptions to the disclosure of related party transactions in the ORP statement.
- One exemption for related parties is what we call 'arms length' transactions. So this is where the transaction is made freely between the two parties without undue pressure.
- For example, if the terms under a contract are made after a tender process or at publicly available competitive rates, it's at 'arms length'.
- Of course, we would recommend that organisations lean towards transparency of related party transactions whenever there is any doubt about the disclosure.

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- DC** You said there were five exemptions. Before we finish today's episode could you tell us about another?
- KM** Sure Declan. Another exemption relates to salary payments to employees of the organisation, or reimbursements to officers for reasonable work-related expenses.
- If you want to find out more about those exemptions and the full list of five, we've summarised them in our guidance note GN014. And the guidance note also provides more information about the disclosure requirements of organisations and branches under the RO Act including a lot of the content we spoke about today.



DC We'll provide a link to the guidance note on the webpage of this episode on the ROC website. Thank you for joining me for today's episode, Kristina. You said earlier that you'd have a go at simplifying some of those legal and accounting concepts and I think you've done exactly that.

KM Thank you Declan. You're welcome, thanks for having me.

DC Please join us again next month for another episode of ROCpod. We'll be back with another instalment of our good governance in practice series. Stay safe.

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