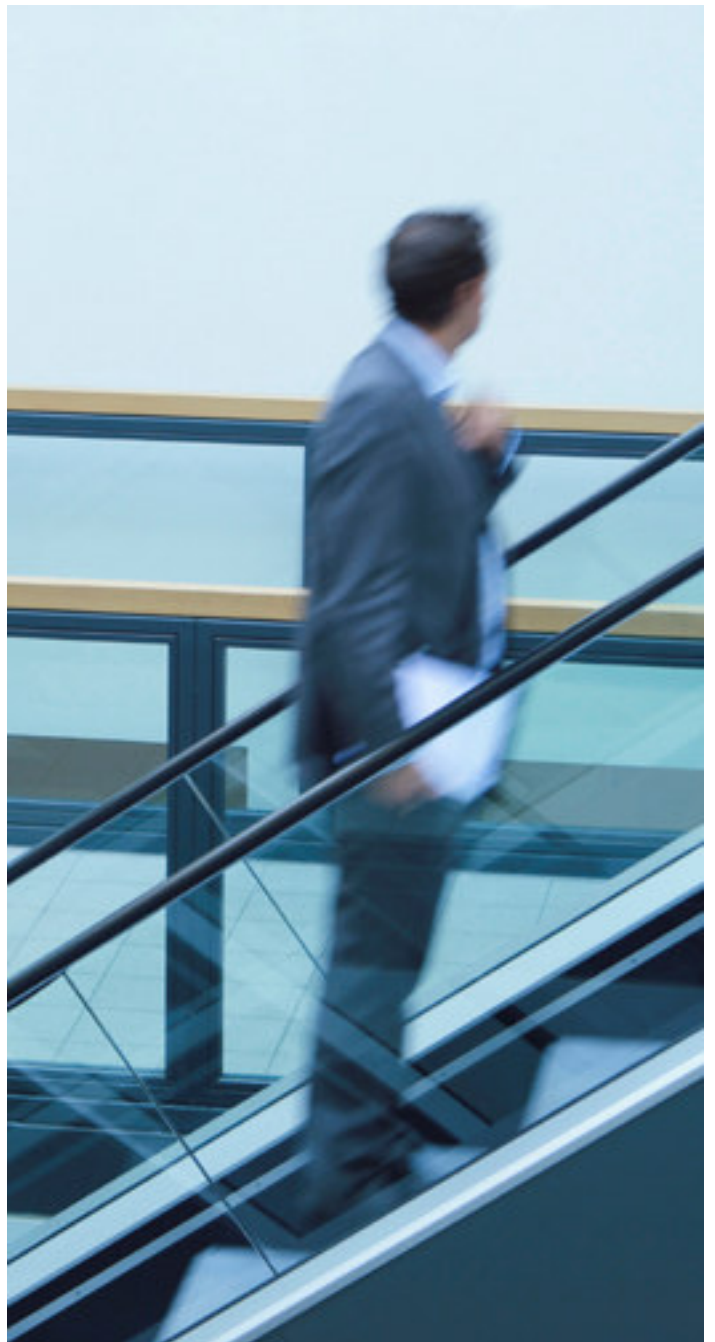


Briefing Note

Charities

Charities Act 2006—where are we now?



The Charities Act 2006 has created the most significant change in this part of English law for perhaps four hundred years. It has taken a considerable time to prepare the Act and put it through Parliament. Many provisions were implemented during 2007 and early 2008 but we still await some changes.

David Blunkett has commented that the government's stated aim is to "enable the sector to operate in a dynamic and innovative fashion and preserve and build on the very considerable trust and esteem in which the public hold the sector".

The two sides of the government's aim, as expressed above, are reflected quite clearly in the Charities Act 2006. Much of the Act seeks to give charities greater freedom, while other parts strengthen charity regulation and reinforce the role of the Charity Commission.

From the outset, the Charity Commission's aim was to untie some of the 'red tape' charities had to cut through in the past and establish "a set of changes to make life simpler for trustees, modernise the definition of charity, and provide new safeguards to uphold public trust in the charitable sector".

Brief Overview

Briefly the Act aims to provide trustees with more "flexibility and less bureaucracy". It seeks to modernise the definition of charitable purposes and ensures that the test of public benefit remains a cornerstone of charity, underlining that all charities must be for the benefit of the public. It also ensures that public trust is protected by strengthening the charity sector's accountability and transparency.

The new list of charitable purposes

From 1st April 2008, the definition of 'charity' in the Charities Act 2006 became law. The Act defines a charity as a 'body or trust, which is for a charitable purpose that provides benefit to the public'. It lists 13 charitable purposes, and any charity must have purposes fitting within that list.

This part of the Act also sets out principles that must be used by the Charity Commission when deciding whether any organisation that is, or wishes to become, a registered charity in England and Wales provides "public benefit". The Act removes the assumption that there will be public benefit in relation to activities for the relief of poverty, the advancement of religion and the advancement of education.

We have previously published guidance on 'public benefit' and the advancement of education. Please visit our website for a copy of our briefing note entitled 'Fee Paying Schools and Public Benefit Re-Assessed'.

Registration of charities

Under the old law, there was a requirement that a charity with an annual income above £1,000 must register. This requirement is now gone. The purpose of this is to save time and money for several thousand small charities by releasing them from the duties of registration.

The Charities Act 2006 states that only charities with an annual income above £5,000 must register. If they have an annual income under £5,000 they are no longer subject to compulsory registration. This provision came into force on 23 April 2007.

The Act also changes the registration requirements for 'exempt' and 'excepted' charities. This will include provisions for ending exception, which will make it compulsory for charities with an annual income over £100,000 to register. The Government believes that there is no longer any justification for keeping the classes of charity that are currently excepted outside registration with the Commission.

Initially the types of organisation that are likely to be affected include some parochial church councils and armed forces charities. There are plans to reduce the threshold in due course, which will ultimately catch many more currently excepted charities in the net.

This provision will be implemented from 1 October 2008 onwards.

The Charity Commission and the Charity Tribunal

One of the real anomalies of the regulatory framework under the 1960 Act has been the existence of certain types of charity that have, for historic reasons, been shielded from the sector's regulator. The Act rises to the challenge of dealing with these inconsistencies by implementing a new Commission and a Charity Tribunal.

The 2006 Act abolishes the office of Charity Commissioner and transfers the Charity Commissioners' function to the Commission (a corporate body), itself with specific new regulatory objectives relating to public trust and confidence, increasing compliance by charity trustees, maximising charities social and economic impact and enhancing accountability of charities to donors, beneficiaries and the general public.

The 2006 Act sets out the Commission's statutory functions, which include determining whether an institution is or is not charitable, encouraging and facilitating better administration of charities, and identifying and investigating apparent misconduct or mismanagement of charities.

On the 18 March 2008, provisions in the Act established a further avenue of appeal for trustees wishing to challenge a legal decision of the Commission - The Charity Tribunal. The tribunal has authority to hear and determine appeals against Charity Commission decisions and actions in certain circumstances.

Phil Hope, Minister for the Third Sector said the Charity Tribunal will "create an affordable recourse for charities to challenge legal decisions of the Charity Commission and will strengthen the legal framework for charities by building case law which has been seriously lacking because charities simply could not afford to bring cases before the high court."

Some examples of the types of appeals, which may be brought before the Tribunal are as follows:

- Decisions to enter or not to enter an organisation in the register of charities;
- Decisions to remove or not to remove an organisation from the register of charities;
- A decision requiring the name of a charity to be changed;
- A decision to launch an inquiry into a charity; and
- Orders in relation to the removal or appointment of trustees.

The Tribunal is a significant step in the right direction and will provide a court of first instance for a number of appeals.

However, as a note of caution, appeals will be permitted on a point of law only and no financial assistance will be available for appellants. The Tribunal will have powers to award costs against the Charity Commission where it has acted unreasonably, but no power to award compensation over and above this.

Nevertheless, it is hoped that the Tribunal will increase the Commission's accountability and provide further transparency.

Trustees

A range of changes affect the trustees, the main areas being removal from office and liability indemnity insurance.

The Act introduces statutory powers to pay an individual trustee to provide a service to a charity (outside their duties as a trustee) if they reasonably believe it to be in the charity's interests to do so. However, the Act also includes safeguards to prevent abuse of this power by limiting the amount of trustees that are eligible to receive payment and limiting the amount that individual trustees can receive by way of payment. The Act does not allow trustees to be paid simply for being trustees or to entitle trustees to be appointed to any salaried position within the charity.

In relation to the above, the Act contains five conditions. In summary, they are:

- The amount or maximum amount of the payment must be set out in writing;
- The payment must not exceed what is reasonable in the circumstances;
- It is in the best interests of the charity for the services to be provided by the trustee for the amount or maximum amount of payment set out in writing;
- Only a minority of the trustees of the charity can receive payment; and
- The trusts of the charity do not prohibit such payment.

The above provisions came into force earlier this year. Trustees who are in any doubt as to whether they are entitled to payment should seek legal advice.

The Act also gives charity trustees a power to apply to the Charity Commission as well as to the High Court for relief from personal liability for breach of trust where they have acted honestly and reasonably. The Government believes the inclusion of this provision will benefit some trustees who fear personal liability. It is also hoped that this will encourage new people to become charity trustees who may have been put off by the risk of personal liability.

However, it is important to note that the Charity Commission and the courts will still take deliberate breaches of trust very seriously.

On a practical level, this new provision will also make life easier for trustees who wish to purchase insurance as they no longer require approval from the Commission or from their governing document. They can simply go ahead and purchase such insurance themselves.

Mergers and restructuring

There are a range of provisions that relax current restrictions and provide new and easier procedures for charities to merge or otherwise restructure.

A technical problem for charities that merge is possible uncertainty over what to do with legacies and other gifts intended for charities that have 'disappeared' as a result of the merger.

To overcome this problem, the Commission will keep a public register of mergers, and charities may notify the Commission of the merger after any transfer of property assets. Mergers that occur before these new rules came in force can also be registered.

A significant effect of registration is that any gift to the transferring charity, which takes effect after the date of registration, will automatically be treated as a gift to the merged charity. This will even apply to a gift that is made before the new rules come into force but which does not take effect until after the new rules are in place.

Charity assets and property (small unincorporated charities)

In relation to small unincorporated charities with an annual income under £10,000 the Commission state that there will be "greater freedom for the courts and the Charity Commission to take account of current social and economic circumstances when such charities seek their permission for the re-assignment of charitable funds that cannot be used for their original purpose".

In simple terms, the Act will make it easier for you to update your charitable purposes. Provided that the new purposes are similar to the original purpose, you do not need to ask the Commission to make a 'scheme' to change them.

The Commission give the example of a charity initially set up to relieve sickness could update its purposes to take part in a health promotion scheme to promote healthy living.

In addition, trustees of smaller charities will be able to transfer property to another charity with consistent objects provided the new objects remain consistent with what the charity was originally set up to do.

Trustees should consider the need to take legal advice on any changes they wish to make to the purpose of their charity.

Legal forms and altering charity constitutions

The Act introduces the charitable incorporated organisation (CIO), which is a new option for charities that want a corporate structure. It provides a legal identity separate from the members of the organisation. The CIO will help charities to obtain the benefits of incorporation without having to undergo dual registration and regulation. The charity will be able to hold property and enter into contracts in the charity's name, rather than the names of individual trustees and will have limited liability.

CIOs will only be regulated by the Charity Commission and will not be regulated by Companies House. This will avoid the dual responsibilities and inherent cost of complying with charity law and company law, as is the case for existing corporate charities.

The basic framework for the CIO is set out in the Act, while the technical provisions, which might need amendment, will follow in secondary legislation.

The CIO will be particularly attractive for existing trusts and unincorporated associations wishing to benefit from limited liability, existing charitable companies wishing to escape dual reporting requirements, and new charitable organisations. It should speed up and simplify the process of registering an incorporated charity and may well encourage the establishment of new charities where economy of administration is a priority for the donor.

Under the new law there will also be fewer occasions on which advance Charity Commission consent will be needed for alterations to the memorandum and articles of a charitable company.

New accounting and audit rules

A modified system for compulsory audit of charity accounts applies to financial years beginning on or after 1 April 2008. This results in compulsory audit for any charity that has annual income of £500,000 or more (whether that charity is a charitable company or unincorporated). This in turn means that most charities with an annual income below £500,000 will not need to have their accounts professionally audited.

Under previous law, trustees were committing an offence if they failed to submit an annual return. The new Act provides that all registered charities that have to submit annual returns to the Commission must do so within 10 months of the end of the charity's financial year. Trustees will not be committing an offence if they can prove that they have taken all 'reasonable steps' to meet the deadline.

Conclusion

It's clear that the Act strengthens the Commission's role in encouraging the better administration of charities. This will hopefully prevent charities getting into difficulties in the first place and allows the Commission to help them uphold principles and good governance.

It has yet to be seen how successful the Charities Act 2006 will be. Some argue that the Act doesn't go far enough in making the necessary changes and are asking about missed opportunities. Commentators have expressed the view that the existing Charity law should have been codified. Helena Kennedy* argues that some areas of the law remain "outdated" and it lags "behind modern social realities". However, in view of the effort and time spent, the 2006 Act in final form is a welcome to many in the charity sector.

Full implementation of the Act should be completed by October 2008.

* Journalist for the Independent Newspaper.

This note does not constitute legal advice but is intended as general guidance only

If you would like further information on this or any other related matter please e-mail us at charities@druces.com or telephone us on 020 7638 9271 and ask for Richard Monkcom