The Kubernesis Partnership

The Kubernesis Partnership LLP • Charity Consultants • York

Tel: 01904 788885 www.kubernesis.uk

The Charities (Protection & Social Investment) Act 2016

Substantial new changes to charity law in England & Wales

The Charities (Protection & Social Investment) Act 2016 is the first substantive new piece of charity-specific legislation in England and Wales for ten years – since the Charities Act 2006. (The Charities Act 2011 was a "consolidation act" – it did an excellent job in tidying up the presentation of the law but it did not make any fundamental changes).

The Charities (Protection and Social Investment) Bill completed its passage through both Houses of Parliament on 2 February 2016 and it will therefore become law in the next few days as the **Charities (Protection and Social Investment) Act 2016**.

Originally the Bill was intended purely to enhance the powers of the Charity Commission, but other provisions have been added relating to social investment and fundraising. All provisions are specific to England and Wales but it is possible that similar updates to charity law in Scotland and Northern Ireland could follow in the Scottish Parliament and Northern Ireland Assembly.

This Bulletin offers a brief summary of the main issues which the Act addresses.

(1) Increased Powers for the Charity Commission

The Charity Commission for England and Wales (CCEW) has faced parliamentary criticism for not taking more action against wrongdoing by charities. In response, the CCEW has said that its existing powers under the Charities Act 2011 were often too limited.

Sections 1 to 12 of he 2016 Act make a number of amendments to the Charities Act 2011 to give stronger powers to CCEW - in particular in terms of disqualifying and suspending trustees. The CCEW is also given more explicit powers to direct a charity to wind-up or transfer its assets to another charity or to direct a charity *not* to do something.

More controversially the CCEW is also given a new power to issue an official warning to a charity, which it can publicise – and although the Act requires the Commission to give advance notice of such a warning so the charity can make representations before it 'goes live' there is no right of appeal to the Charity Tribunal against these new official warnings.

Our view

At one level these new powers should make no difference to the vast majority of well-run charities. But in any situation where a charity finds itself in a disagreement with the CCEW, where the Commission is tempted to use these powers, the consequences could be dire.

Although some of these provisions make sense, we are concerned that much of what is proposed has been justified by the Government's anti-terrorist agenda – as Gareth Morgan argued back in November 2014 when giving evidence in Parliament on the Draft Bill which led to this Act.

Giving the CCEW more power does not address its lack of resources. An under-resourced Commission could easily be tempted to take over-the-top actions, particularly in a situation where it was under criticism from MPs or the press. We anticipate more potential difficulties, for example, if a charity invites a controversial speaker who is critical of UK foreign policy in regions with high levels of terrorism – or a grant-making charity supporting controversial projects – it could be too easy for CCEW to leap in and use its new powers.

There are also many more circumstances in which people can now be disqualified as charity trustees, so forms where new trustees declare that they are not disqualified will need updating once the Act comes into force.

We would therefore recommend charities to spend time understanding the CCEW's new powers, when they might be used, and the mechanisms for making representations and lodging appeals.

(2) Regulation of Fundraising and New Requirements in Trustees' Reports

Follow the scandals in 2015 regarding some large charities engaging agencies who used inappropriate methods of fundraising, the Government was determined to strengthen the regulation of charity fundraising.

However, extensive powers *already* exist in the Charities Act 1992 and Charities Act 2006 allowing the regulation of charity fundraising, most of which have never been implemented, because the Government was keen to see a self-regulatory approach through the Fundraising Standards Board (FRSB).

Following the Etherington review in summer 2015, the Government has agreed that there should be a new much more powerful body called the *Fundraising Regulator* which is now established (chaired by Lord Grade) and due to become fully operational in the coming months. In due course, the FRSB will hand over to the Fundraising Regulator which will also take over the fundraising codes of conduct from professional bodies

Whilst the Government still hopes the Fundraising Regulator will work on a self-regulatory approach, section 14 of the 2016 Act includes provisions that could compel charities to sign up and pay fees to support its work.

Alongside this, section 13 amends the rules in the Charities Act 1992 regarding the use of professional fundraisers and commercial participators (a commercial participator is a business which sells products with a promise that part of the price will go to charity). The written agreements which are already required between a charity and a professional fundraiser/commercial participator now have to include specific provisions to protect vulnerable people and to ensure that the public are not subject to "unreasonably persistent approaches".

Section 13 also requires charities over the audit threshold (in most cases this means those over £1M income) to include six additional issues in their Trustees' Annual Report (TAR) (alongside the accounts) explaining varous aspects of the charity's practices on protecting prospective donors/supporters and the numbers of fundraising complaints received.

Our view

Although we are broadly supportive of the recommendations in the Etherington review (though more work is needed on certain aspects) we feel that the Fundraising Standards Board has been reasonably effective in improving practices in fundraising. But the main limitation of the FRSB has been what to do about charities which are not members of the FRSB, or which simply ignore its recommendations and rulings.

So, some kind of compulsory mechanism is needed – but the 2016 Act does not deliver that explicitly. It simply gives more explicit powers to Ministers to make regulations if they consider it necessary – but that power was pretty much there in any case in the Charities Act 2006. The Government hopes that the threat of compulsory registration with the new Fundraising Regulator will be enough to persuade virtually all fundraising charities – at least those over a certain size – to sign up.

In the meantime, we would encourage all charities which have *any* income at all from individual donors, grant-making trusts or from businesses to sign up to the FRSB if they have not done so – see www.frsb.org.uk. This is not just about charities with big fundraising departments – any income other than from public sector sources is covered. It is almost certain that membership of the FRSB will be carried over to the new Fundraising Regulator, but it is probably much cheaper to join the FRSB as it stands. It includes charities of all kinds.

We feel the additional requirements for TARs generally make sense though this could have been added simply by updating the Charities (Accounts and Reports) Regulations 2008. These regulations are already in urgent need of updating for the 2015 SORPs, so there was no real need to include this in the 2016 Act. In any case it is already a requirement for larger charities to explain their fundraising methods so this only clarifies an existing requirement. However, as with other material in TARs, there is a risk that charities will just include 'boilerplate' wordings suggested by their accountants, rather than a proper analysis of their fundraising ethics.

(3) Social Investment

Section 15 of the new Act inserts some new provisions in the Charities Act 2011 which makes it explicit that charities have the power to make social investments as a means of advancing their charitable aims.

A social investment is defined as an investment or commitment made by a charity where it expects to achieve some financial return (so not a pure grant) as well as advancing its charitable aims. Common examples including providing loans at low rates of interest or interest-free in order to support beneficiaries, or 'soft loans' which only have to be repaid under certain circumstances. They could also include charities taking shares in non-charitable social enterprises, even if such shares would not generally be a prudent investment for a charity, provided the trustees consider that the investment will deliver social outcomes that further the charity's objects. Giving loan guarantees on behalf of beneficiaries can also be a means of social investment.

Many charities have, of course, been making social investments for many years but there have been suggestions that, at least in some charities, trustees making social investments may have been in breach of duties to manage their investments in ways that would directly maximise the financial return for their beneficiaries. The changes made by the 2016 Act make it clear that non-financial returns can be considered.

These changes were recommended by the Law Commission in their review of charity law in helping to avoid uncertainty in this issue, and have generally been welcomed by those of all parties.

However, the Act also includes a whole list of conditions that must be met in relation to social investments:

- The new provisions do *not* generally apply to permanent endowment unless the trustees can show that the social investment would not breach any rules on the expenditure of the permanent endowment. So, charities with permanent endowment funds will not, in most cases be able to use these provisions to make social investments (as at present, specific Charity Commission authorisation, usually through a Scheme, would be needed for social investment of permanent endowment).
- The social investment provisions do *not* apply to charities established by legislation or by Royal Charter. This rules out many of the major churches, universities, professional bodies, many scout and guide groups etc. The provisions only apply to charities that have the power to change their own govering documents.
- Trustees must consider a wide range of issues (and in most cases they will need to take professional advice) *before* making social investments. The social outcome must be linked to the charity's purposes.

Our view

We believe many charities that are keen to make social investments are already doing so under the existing understanding of charity law, and we do not anticipate that these provisions will unlock huge amounts of new social investments by charities. Also, as explained above, many funds will be excluded.

However, where a social investment is clearly an appropriate use of charitable funds, these new provisions may well be helpful in confirming that trustees have the relevant powers.

Implementation Timescales

As with the majority of new legislation, most of the Act will only come into force when the Minister makes the appropriate orders (in this case, the Minister for the Cabinet Office, or in practice the Minister for Civil Society, Rob Wilson MP).

Hopefully the Minister will make a statement on timescales in the near future. Clearly the CCEW will want its new powers as soon as possible, but other provisions, in particular section 14 on the compulsory regulation of fundraising, may *never* be implemented if the Government is happy that the new Fundraising Regulator is working effectively on a self-regulatory basis. Some provisions will definitely be delayed – in particular, because of concerns from charities working with former offenders, it has been agreed that the new automatic disqualification of trustees who have certain convictions (much wider than at present) will not be implemented for at least 12 months to allow time for the CCEW to work with charities in this field and agree when exceptions to disqualifications should be permitted. The new provisions on social investment are not controversial, but the Minister will probably want to wait for CCEW to revise its guidance before they are commenced.

So, it is difficult to predict exact timescales, but we would encourage charities to prepare for these changes as soon as possible. In terms of the additional information needed in TARs regarding fundraising practices, we suggest many charities may want to start including this information immediately – as a sign of good practice – rather than waiting for section 13(4) of the 2016 Act to be formally brought into effect.

FURTHER HELP: *The Kubernesis Partnership LLP offers a range of seminars on issues concerning charity regulation and accounting. See www.kubernesis.uk/seminars.*

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Partners (members of the LLP): **Gareth G Morgan** MA BA PhD FAIA(Acad) FBCS MInstF(Dip) FCIE **Sharon L Morgan** BA CertTh
Professional services since 1979 ● *E-mail:* info@kubernesis.uk ● *Website:* www.kubernesis.uk