

Milestones

Managing key events in the life of a charity

Contents

	Page
Introduction	1
Executive summary	2
Starting up	6
Registering as a charity	6
The role of the governing document	7
Incorporation	8
Planning ahead	11
Extent of planning	11
Accuracy of expectations	12
Funding	14
Independence	14
Sustainability	15
Contract funding	16
Grant funding	18
Grant making charities	19
Managing fundraising	20
Raising funds through appeals	21
Raising funds through trading	22
Managing change	25
Updating the governing document	25
Developing capacity	25
Employment	26
Balancing responsibilities between trustees and employees	27
Acquisition and disposal of land	29
Winding up	32
Alternatives to winding up	33
Annex A - Questions to ask at each stage	35
Annex B - Survey findings	40
Annex C - Glossary of terms	48
Annex D - Resources for trustees	50
Annex E - Bibliography	55
Acknowledgements	57

Introduction

There are over 180,000 registered charities in England and Wales. Each charity is different and their diversity is one of the defining characteristics of a vibrant civil society. Charities share many common events or milestones as they develop, grow and change. The lessons learnt by one charity can be of benefit to other charities by helping them to avoid common pitfalls and take advantage of best practice experience.

Society is increasingly turning to charities to provide and deliver key services and amenities, with an expectation that these services will be delivered in a well organised, effective and accountable way. This report aims to play a part in supporting new and developing charities by exploring, from the charity regulator's perspective, some of the issues charities can expect to encounter. It aims to disseminate the information gained from charities' experience of milestone events and illustrate some best practice ways of preparing for and dealing with them. To complement our casework experience, the report also presents findings from a survey which gathers, for the first time, the feedback of recently registered charities.¹

¹ The surveyed charities were all registered in 1995, either for the first time or subsequently as a charitable company.

Executive summary

A 'milestone' is defined as a significant change that has repercussions for many aspects of a charity's role and activities. It may have implications for the charity's governance arrangements, the roles individuals play, potential liabilities and so on. The characteristic of a milestone is that many changes have to be considered at the same time and the demands on trustees and staff increase significantly.

The report is structured around issues and phases of development rather than strictly by milestone because many of the issues covered by the report are relevant to more than one milestone. Typical milestones in the life of a charity are illustrated below, with the section of the report that deals with the related key issues shown in brackets.

The milestones that charities commonly encounter as they develop are:

- establishing themselves as a formal legal entity (*Starting up*);
- employing staff for the first time (*Managing change*);
- planning future activities (*Planning ahead*);
- encountering changes in their funding arrangements such as getting a grant, entering into a contract to deliver services or setting up a trading subsidiary (*Funding*);
- making changes in their governance or organisational structure (*Managing change*);
- acquiring, repairing or selling property (*Managing change*); and
- winding up or changing direction (*Managing change*).

Annex A provides a list of questions that trustees may find useful to ask themselves at various stages of their charity's development.

There are many milestones in the life of any one charity. This report concentrates on those for which the Charity Commission's regulatory experience adds a particular perspective and value. It is not a manual; it does not give detailed instructions on what to do when each milestone is met. Instead it draws attention to the main issues that the Charity Commission sees and of which charity trustees need to be aware.

Each milestone can be a springboard if well managed but cause problems otherwise. In some cases the Charity Commission will become involved because our authority or advice is needed or because the charity becomes a cause for concern which may lead to an investigation. More generally, the Commission has a statutory duty of "promoting the effective use of charitable resources".² In our experience, resources are used most effectively in a charity that manages its transitional stages well. This is more likely to happen in a charity which takes a long-term, informed perspective.

Our casework shows that charities often experience milestones or transitional events as crisis points rather than as anticipated stages in a process. The milestones listed above are identifiable because new and developing charities regularly meet the same events as those before them without the benefit of learning from others' experience. Experience is passed on through umbrella and advisory bodies but they report that charities often do too little, too late. All too often, charities seek support and advice when they hit a transitional period rather than in preparation for it. The evidence also suggests that charities' response is often to implement a short-term solution rather than to adapt their organisational structure to ensure that the charity has the capacity to continue to function efficiently and effectively in its new situation.

² Section 1(3) Charities Act 1993.

Executive summary

This can be explained, in part, by a lack of adequate planning. Only 49% of the charities surveyed produce a yearly or longer term plan. Charities can only deal with milestone events successfully in the context of a proper risk management strategy. A long-term perspective and awareness of the context within which the charity is operating are essential to a proper assessment of risk. If trustees are to manage charities effectively, they need a working plan, appropriate to their size and needs, based on an awareness of the probable direction of their charity's development, an understanding of the social and economic factors that are likely to impact upon them and an awareness of the evolving needs of their beneficiaries.

Charity Commission casework experience indicates that trustees are not always accurate in their expectations for their charity. This is confirmed by our survey: 21% of charities had underestimated expenditure or overestimated income in their early years; 39% had underestimated the time required to run the charity; and 18% had underestimated the complexity of accounting involved.

A large number (59%) of charities with staff and/or volunteers do not have a long-term or yearly plan that ensures they are able to meet their commitments as employers. Only 58% are confident that they are up to date in their understanding of employment legislation.

The conditions in which a charity operates can have an effect on their ability to plan ahead. Short-term and restricted funding have the most significant impact in this respect. 69% of grant funded charities surveyed reported that relying on short-term grant funding had compromised their ability to plan their development.

There is scope for trustees to be more proactive in ensuring that the organisational capacity of their charity keeps pace with its growth. 69% of surveyed charities stated that they had never made changes to their management or governance structure.

The Charity Commission's evidence shows that, perhaps understandably, charity trustees and employees tend to focus their attention and resources more heavily on their beneficiaries than on their organisational structure. 22% of surveyed charities reported that the daily running of the charity took up most of their available resources, which does not leave much scope for the development of internal systems and structures. As identified by the Active Community Directorate, the long-term interests of beneficiaries are better served by robust organisations with the capacity to use funds efficiently.

On the whole, charities do not currently communicate or co-operate with each other to a very high degree.³ However, the evidence suggests that smaller charities are more likely to look up from their daily work and take a more strategic perspective when they have secure funding in place. Evidence supports the findings of the Government's recent Cross Cutting Review, *The Role of the Voluntary Sector in Public Service Delivery*.

The main message of this report is that planning should be central to a charity's governance and, to inform the planning process, trustees should make use of the experience and lessons learned by other charities. Sound planning and a proper assessment of risks by charities, of their governance, finance and activities, will promote efficiency, sustainability and growth in the sector.

³ See Charity Commission publication **Collaborative Working and Mergers (RS4)**.

Executive summary

Charity Commission casework experience and consultation within the sector show that successful charities:

- have a governing document which matches the reality of what they want to do;
- have governance arrangements which keep pace with change;
- take stock to ensure that they have the skills and experience/knowledge for the nature of their activities, especially when getting into complex situations such as contract negotiations or setting up a trading subsidiary;
- confront difficult or emotionally charged issues such as whether to wind up their charity or transfer activities;
- are financially stable and have:
 - secured sufficient, or sufficiently diverse, income,
 - properly costed their activities and contained their expenditure, and
 - paid sufficient attention to financial planning and risk management.

Research for this report involved detailed analysis of our bank of casework and other data held within the Charity Commission, a survey of all charities registered in 1995 (either for the first time or subsequently as a charitable company) and consultation with charities, umbrella and advisory bodies.

Recommendations

Below are some recommendations which we believe will help charities anticipate and successfully deal with the milestones in their development.

- As good practice, trustees should:
 - develop a business plan and risk management strategy, however simple, to establish the projected future activities and financial and organisational situation of the charity and determine how these will be managed.
- As part of that process, trustees should:
 - ensure that they fully understand their governing document, refer to it on a regular basis and act within its terms;
 - ensure that the governing document they adopt is appropriate, comprehensive and contains provision for amendment to meet the evolving needs of their charity;
 - be proactive in sharing experience, use all available sources of information and network with other charities to develop realistic projections of income, expenditure and time commitment;
 - weigh up both the potential benefits and costs of incorporation when considering whether to register as a charitable company;
 - maintain a realistic understanding of the extent of their liability for any losses incurred by their charity;
 - scrutinise the conditions attached to grant funding and contracts to ensure that the independence of their charity is not compromised;
 - ensure that the terms of any contract they enter into safeguard the interests of their charity and its users;
 - ensure that fundraising is actively managed, even when it is contracted out, and that it complies with all relevant legal requirements;

Executive summary

- ensure that their own roles and those of the charity's managers and employees are clearly defined so that all parties understand the scope of their responsibilities;
 - seek the appropriate level of legal advice before entering into a property transaction;
 - give regular consideration to whether or not their charity has a viable future and a good reason to continue.
- Grant makers should seek to ensure that any administrative and monitoring requirements accompanying funding are proportionate to the size of the grant.
 - Umbrella and professional bodies should:
 - encourage charities to use model and standard governing documents which contain the provisions that they are likely to need;
 - provide guidance on trustees' personal liability and on the extent to which incorporation can provide some protection against this liability.
 - The Active Community Directorate, as part of its strategy for encouraging capacity building, should promote business planning and predictive skills by charities.

The Charity Commission produces an extensive range of guidance that sets out our position and the main points of consideration for charities in relation to each issue. Where such guidance is available, it is sign-posted in the report. The Charity Commission will incorporate the experience gained from this research into its wider range of publications.

Starting up

One of the early decisions for an organisation planning to register as a charity is to choose an appropriate legal form and a suitable governing document. Another is to draw up a plan outlining the first few years' activities and anticipated income and expenditure. The Charity Commission's regulatory experience indicates that charities which get it 'right' at registration tend to run into fewer difficulties as they grow or change.

Registering as a charity

Registering as a charity is a key event for any organisation because of the opportunities it presents. Charities with an income greater than £1,000 per annum are currently legally required to register with

the Charity Commission.⁴ A previous survey undertaken by the Charity Commission shows that the main reasons for which charities register, other than the legal requirement, are to secure funding, to obtain tax relief and to achieve wider recognition. Registration is also seen as conferring public confidence in the charity, its trustees, staff and volunteers.⁵

"Before [we were registered as a charity], when we went anywhere for donations, the first thing they would ask is whether or not we were a charity. When I said no they said sorry, but they couldn't help us."

Charity representative

This case illustrates the positive impact that registration as a charity can have on an organisation.

A village hall was able to apply for grant funding after raising enough funds to become registered as a charity.

Charitable status allowed the hall to apply for a grant that would otherwise have been inaccessible to it. The grant was awarded, enabling the hall to modernise its facilities and increase the range of events that it is able to run.

The charity's new charitable status gained press attention which raised its profile and publicised its events and facilities.

⁴ There are some exceptions to this, see **Exempt Charities (CC23)**. The Strategy Unit review makes the recommendation that the proposed Charities Bill include a raised registration threshold of £5000 but allow for voluntary registration below that figure, and that the Bill should also include changes to the rules regarding exempt and charity charities. See *Charities and Not-for-Profits: A Modern Legal Framework - The Government's response to 'Private Action, Public Benefit'* on the Home Office website.

⁵ Findings from a Charity Commission review of its charitable status function (2002).

The role of the governing document

Registering a charity under a suitable, comprehensive governing document helps

to avoid the potential stumbling points that charities can encounter as they develop.

This case illustrates what can happen when a charity's governing document does not make provision for actions it might have to take.

A charity ran into difficulties when it discovered that its governing document did not contain the means by which it could remove trustees whose behaviour was damaging the charity.

A dispute developed between some of the trustees and the management body of the charity, during which the former prevented the managers and chief executive from carrying out their work. The other trustees contacted the Charity Commission to request a copy of the charity's governing document in order to determine what action to take. It did not contain a clause stating the conditions under which a trustee could be removed from office. The Charity Commission became involved when allegations of misappropriation of funds were made. The Charity Commission held several meetings to establish what had happened to the funds in question and tried to effect a compromise between the parties.

A special meeting was eventually held to insert the necessary clause in the charity's governing document. This was not an easy process because all the trustees needed to be present but they were in dispute. The dispute was finally resolved by the removal of those trustees that had been causing the disruption and the charity was able to continue its work.

The trustees and management body of the charity were clearly not aware of the full details of their governing document and, when drafting it, had not ensured that it contained all clauses that might prove necessary. The dispute and the protracted arrangements required to remove the disruptive trustees took up time and resources that should have been directed toward meeting the charity's purposes.

The governing document is a *legal* document containing a charity's objects (what the charity is set up to do) and powers (how it will achieve those objects). If a charity acts outside the scope of its objects and powers, that will constitute a breach of trust and could have serious consequences for both the trustees and the charity.

Recognition of the importance of the governing document at the outset establishes a culture of best practice in

terms of trustees' attitude toward it; the governing document should play a central role in all future governance decisions. However, Charity Commission casework and findings from our review visits programme indicate that a large number of trustees do not make reference to their governing document when directing the activity of their charity. Consequently, charities often 'outgrow' their governing document as they evolve.

Starting up

In addition, of the charities surveyed for an earlier regulatory report, **Trustee Recruitment, Selection and Induction (RS1)** some 45% did not provide new trustees with a copy of the charity's governing document. Trustees who do not direct the activities of their charity with reference to its governing document are leaving themselves and their charity open to risk.

- Wherever possible, umbrella bodies should encourage charities to use model and standard governing documents which contain the provisions that they are likely to need.
- Trustees should ensure that they fully understand their governing document, refer to it on a regular basis and act within its terms.
- Trustees should ensure that the governing document they adopt is appropriate, comprehensive and contains provision for amendment to meet the evolving needs of their charity.

Related Charity Commission Guidance:

Registering as a Charity (CC21) provides information and guidelines with which founding trustees ought to familiarise themselves before beginning an application for charitable status.

Choosing and Preparing a Governing Document (CC22) gives full details of Charity Commission recommendations on what trustees should consider in relation to their governing document, including a checklist of standard provisions which we would normally expect to see included. It also contains details of what it means to be a charitable company and the circumstances in which incorporation might be appropriate.

The Charity Commission provides model governing documents which can be adapted by most charities. A list of other organisations for which a standard governing document has been agreed can be found on the Charity Commission website.

Incorporation

Incorporation (ie establishing a company) is one of the constitutional forms available to a charity. Our survey confirmed anecdotal evidence of a growing trend toward incorporation among charities. In total, 14% of charities surveyed for this report are registered as charitable companies but that figure rises to 27% for surveyed charities established since 1995.

The trend toward incorporation appears to be largely based on fears about trustee liability and the risks associated with a charity's income sources and activities. 60% of surveyed charities that had incorporated had done so to protect their current trustees and 22% had incorporated to help with the recruitment of trustees. 33% incorporated because they employed staff and 26% because they were working with vulnerable people. 59% of surveyed

Starting up

charities with a main income from contracts, and 36% with a main income from a trading subsidiary, were incorporated.

76% of charitable companies surveyed have a yearly or longer term plan in place, compared to 47% of unincorporated charities, which suggests that incorporation can bring a more professional approach. Many surveyed charities noted this as a reason for incorporating.

49% of incorporated charities had done so on advice from a solicitor and 30% on advice from an umbrella or advisory body. However, there is evidence to indicate that trustees are not always confident that incorporation is the best option for their charity. Only 34% of the incorporated charities surveyed had carried out an assessment of whether incorporation was the most appropriate legal form. 15% of surveyed charities that had incorporated stated that they did not know whether it has been the right choice. 19% of unincorporated charities did not know whether it would be suitable for them.

Incorporating can waste resources if it results in charities operating within a structure that is overly complex. There is also an opportunity cost involved because the process of incorporation can disrupt a charity's work. On the other hand, failing to incorporate when it is appropriate to do so can be damaging to a charity and leave its trustees open to unnecessary risk.

Our experience and research show a high degree of misconception among trustees about what trusteeship entails, the level of risk that trustees face and the extent to which incorporation will mitigate that risk. Some survey respondents reported that a significant event for their charity had been losing trustees who had found the responsibility too great.

"[We] found out that we were the trustees of the school."

Survey response to question: "Please provide details of the [unexpected] situation."

"I'm not a trustee, I'm on the committee."

Charity trustee.

The creation of a corporate identity gives trustees a certain amount of protection from personal liability when their charity is engaged in high risk activities such as entering into contracts, employing staff or working with vulnerable people. But, if trustees fail to act with due diligence, the corporate identity of the charity may not protect them from personal liability for costs incurred. The directors of a charitable company have certain fiduciary duties to the company and may be personally liable for any breach in those duties.⁶

⁶ The governing body of a company are effectively the trustees of the charity as defined by section 97 of the Charities Act 1993 as 'the persons having the general control and management of the administration of a charity'.

Starting up

Trustees should not overestimate the level of risk that their position brings. Equally, they should not become complacent when a corporate identity has been established. Many of the advisory bodies consulted in research for this report expressed concern that charities perceive incorporation to offer more protection than it actually does and that charities are often pressured into incorporation by the national body of which they are a member or by the need to reassure existing or potential trustees.

"Being unincorporated keeps trustees on their toes."

Chief executive of an incorporated charity.

Trustees should consider carefully the advantages and disadvantages of incorporating as a company and may need to take professional advice. Smaller charities may find that incorporation is a more significant milestone than it is for larger charities, which find it easier to absorb the costs associated with dual registration, financial administration, winding up the unincorporated charity and

so on. The additional work and costs involved in incorporation should be factored in to charities' plans.

Part VII of the Charities Act 1993 allows for the incorporation of an existing trustee body. The trustee body can be incorporated without having to go through the process of winding up the charity. This may be more suitable for some charities and trustees should seek advice. The liability of the individual trustees is unaffected by this form of incorporation.

- Trustees should weigh up both the potential benefits and costs of incorporation when considering whether to register as a charitable company.
- Trustees should maintain a realistic understanding of the extent of their liability for any losses incurred by their charity.
- Umbrella and professional bodies should, as good practice, provide guidance on trustees' personal liability and on the extent to which incorporation can provide some protection against this liability.

Related Charity Commission Guidance:

The Essential Trustee: What you need to know (CC3) outlines the role of trustees.

Trustee Recruitment, Selection and Induction (RS1) provides information on best practice in recruiting new trustees.

Incorporation of Charity Trustees (CC43) provides details of how to incorporate the trustee body. See also operational guidance **Corporate Trustees (OG38)** available on the Charity Commission website.

Trustee Indemnity Insurance (OG100) sets out our policy on trustees purchasing insurance which protects them against the risk of personal liability arising from certain breaches of trust.

Planning ahead

Extent of planning

"In the beginning I had no fixed idea of what I was doing."

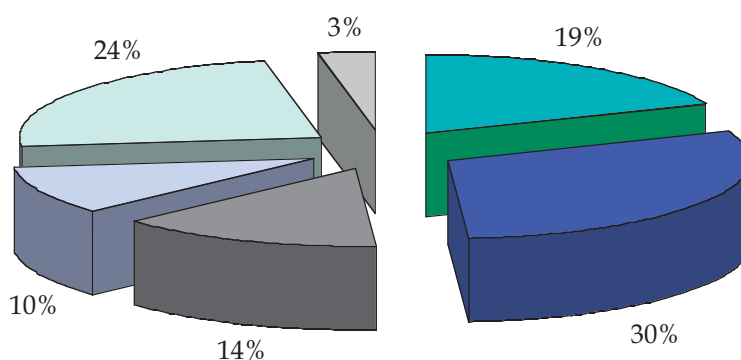
Charity founder.

Our casework experience shows that charities which plan for their future are more likely to use their resources effectively than those which do not. Less than half (49%) of surveyed charities have either a long-term or a yearly plan directing their activities. It may be entirely appropriate for some charities to have minimal planning but many of the surveyed charities had no long-term plan despite being involved in activities that warrant a strategic perspective.

Risk management is an important element of trustees' responsibility. Charities can only deal with milestone events successfully in the context of a proper risk management strategy. A long-term perspective and awareness of the context within which the charity is operating are essential to trustees' assessment of risk.

The survey showed that charities with a yearly or longer term plan are consistently more likely to be accurate in their expectations of income, expenditure, time commitment and legislative requirements than charities without.

Level of planning undertaken by responding charities



 We have a yearly and a long-term plan (eg 3-5 years) in place (19%)

 We plan 1 year at a time (30%)

 We make plans on an ad hoc basis (14%)

 We respond to events as they occur (10%)

 We see no need for a strategic plan (24%)

 Other (3%)

Accuracy of expectations

This case illustrates what can happen when a charity is established with unrealistic expectations.

A charity established with a large amount of statutory grant funding to run a public attraction had difficulties almost immediately because the charity's estimated visitor numbers proved extremely ambitious. The charity received further funding to broaden its activities in an attempt to attract greater public interest but this was unsuccessful. A Review Visit to the charity revealed that the charity was well-run. Its problems were entirely due to the fact that it was founded with the expectation of significantly more income than it actually received. The nature of the building and location of the charity meant that efforts to revive its fortunes also failed and the charity was forced to close down and sell its property to pay off its creditors.

The grant making bodies in this case were extremely 'hands off', even when approached by the trustees of the charity for advice. Money was wasted because the charity and the grant makers did not take sufficient care when setting up the charity to ensure that their plans were realistic.

Charities can find it difficult to predict future activities and finances. Survey and Charity Commission data show that charities' expectations are not always accurate, especially in newer charities. A significant proportion of surveyed charities had underestimated:

- the time required to run the charity (39%);
- the time required from trustees (25%); and
- the complexity of accounting involved (18%).

21% of surveyed charities had either underestimated expenditure or overestimated income during their early years. In addition, of the charities that registered with the Charity Commission in 2002 with an *estimated* first year income on their application form:

- only 1 in 4 had an *actual* year end income within 20% of their estimate;
- 19% had an actual year end income of less than 80% of their estimate;
- 11% of charities had an actual income of 300-500% of their estimate.⁷

As income or expenditure reach various thresholds, charities are required to prepare and submit increasingly detailed accounts and reports. The requirement to have accounts independently verified also becomes more comprehensive as charities reach higher income/expenditure thresholds. Charities planning a substantial increase in income through, for example, a grant application often fail to take into consideration the additional resources that may have to be devoted to their accounts as they cross these thresholds.

⁷ Newly established organisations that have not been operational long enough to have actual income figures are required to provide an estimate on their application form.

Planning ahead

Casework experience shows that charities are more likely to be successful if their founders have considered all of their expectations and done some research to ensure that they are realistic.

Networking with other charities and using professional and advisory bodies can help trustees to build a realistic picture of how their charity can expect to change. All charities' accounts and governing documents are available from the Charity Commission. Looking at those of similar charities can be a useful exercise for founders who want to gain an accurate perspective and prepare a governing document suitable to their needs.

Some of the problems charities experience will be beyond their control but others are avoidable with minimal forward planning. Most of the 'significant events' that charities described in the survey related to services they had been able to provide to their

beneficiaries. This focus on outputs, while understandable, needs to be balanced by a corresponding internal focus and long-term perspective if resources are to be applied to the greatest public benefit.

- Trustees should use all available sources of information and network with other charities to develop realistic projections of income, expenditure and time commitment.
- Trustees of all charities should develop a business plan, however simple, to establish the projected future activities and financial and organisational situation of the charity.
- The Active Community Directorate, as part of its strategy for encouraging capacity building, should promote business planning and predictive skills by charities.

Related Charity Commission Guidance:

The Register of Charities: Information and Services Available (CC45) provides details of the information that the Charity Commission makes available to the public.

Charities and Risk Management, available on the Charity Commission website on www.charitycommission.gov.uk, provides guidance designed to help trustees set a framework which allows them to: identify the major risks that apply to their charity; make decisions about how to respond to the risks they face; and make an appropriate statement regarding risk management in the Annual Report.

Funding

The source of a charity's income is fundamental to the way it operates because it determines the amount of time and resources that will be devoted to managing funding streams and the extent to which a charity can be pro-active in driving the direction of its activities. The terms attached to grant and contract funding in particular can drive a charity in certain directions.

The most common sources of income among the charities surveyed were:

- donors (56%);
- members (39%); and
- grants (37%).

There are many other means by which charities can fund their activities - through fees, rent, borrowing, sponsorship, investment. This report focuses mainly on grants, contracts, trading and property because these are the funding methods in which the Charity Commission is most likely to have any regulatory involvement.

Independence

"We have to be a chameleon and constantly change our colours to get funding."

A charity representative.

Independence of governance is of paramount importance for charities. Over-dependence on restricted grant or contract funding can be limiting for charities because, under trust law, charities have a duty to apply restricted funds in line with the reason for which they were given. 22%

of the grant funded charities surveyed for this report said that they had directed their charity's activities in a certain way in order to be eligible for funding and 12% said that their independence had been compromised by the terms of a grant.

69% of grant funded charities surveyed indicated that dependence on short-term funding had compromised their ability to plan as thoroughly as they would like. 15% said that they had had difficulty responding to external changes in circumstances because of grants being tightly allocated or unavailable for what they wanted to do. 12% of surveyed charities reported that they had had grant applications turned down because their reserves level was 'too high'.

It is good practice to diversify income streams in order to limit the risks posed by one source drying up and to boost sustainability and independence. The survey showed a high degree of diversity in the income streams for most charities.

Charities can become over focused on getting grant funding and fail to ensure that it fits with their objects or their plans. There is a balance to be struck. Maximising a charity's ability to attract funding is vital but this needs to fit with the charity's overall plans and be consistent with the terms of the charity's governing document (see **The role of the governing document** on page 7).

"Trying to adhere to everyone else's requirements is moving us away from what we were set up to do."

Chief executive of a grant funded charity.

Funding

Grant makers sometimes seek a charge over some or all of a charity's assets in return for grant funding. In these cases, the charity must get Charity Commission authority to go ahead with the agreement.⁸ Charities should ensure that the extent of the agreed charge is proportionate to the size of the grant and that the terms of the agreement do not put the charity at undue risk.

- Trustees should scrutinise the conditions attached to grant funding and contracts to ensure that the independence of their charity is not compromised.

Related Charity Commission Guidance:

The Independence of Charities from the State (RR7) and **Local Authorities and Trustees (OG56)** explore independence in more detail.

Charity Reserves (RS3) examines in more detail the issues surrounding reserves and restricted funding.

Sustainability

A sufficient level of planning is important to ensure that charitable resources are not wasted in running a charity that has no viable future.

Consultants and feasibility studies can help a charity to explore new ways of funding their charity and also help them to develop

their business strategy and internal systems, structures and skills base. However, only 8% of surveyed charities had requested funding for either consultancy fees or feasibility studies.

This case illustrates how a charity overcame initial problems resulting from grant dependence.

A charity that was founded and sustained through grant funding had been slowly expanding and enhancing its services in response to increased demand. The building that the charity leased came up for sale and the trustees felt that owning the property would be a boost to their independence. However, the bank would not lend them the money because of the short-term nature of their funding and their related inability to provide a long-term business plan.

The charity secured a donation of consultancy advice which helped them to take a strategic view and develop alternative funding methods such as charging fees for some of their services. On the basis of the new strategic plan, the charity was able to raise match funding to gain a grant to buy premises. Ownership of the property has allowed the charity to develop its services with greater independence. The charity still relies on grant funding for many of its projects but has diversified its income sufficiently to allow the trustees and chief executive to be selective about the funding they take and to plan and control the way in which the charity moves forward.

⁸ Section 38(1) Charities Act 1993.

Contract funding

Charities are increasingly entering into contracts with public bodies to provide services on their behalf and this trend looks likely to continue. 10% of surveyed charities reported that they are currently contract funded.⁹

Whilst change is underway following the outcome of the Treasury's Cross Cutting Review, short-term contracts and deficit funding are currently still the norms that contract funded charities can expect.¹⁰ Deficit funding is awarded subject to the charity demonstrating that it has achieved certain pre-agreed outcomes. The balance of risk is weighted heavily toward the charity because it must spend on a project before receiving funding for it. Only a very small number of surveyed charities had had deficit funding withheld because of failure to meet outcomes. Nevertheless, it is a potential problem of which trustees should be aware.

Smaller charities are more adversely affected by outcome based funding. They lack the resources to undertake sophisticated analysis of the impact of their work. They are also less able to absorb the additional overheads that grants bring but do not cover.

10% of grant or contract funded charities surveyed reported that they had experienced problems meeting the costs of delivering deficit funded projects. Some charities use grant income received for other projects to cover the cash flow for deficit funded projects. Trustees should be careful about using restricted funding in this way in case the accounts do not balance, for example where outcomes are not met and funding is withheld. In that eventuality they could be in breach of trust.

Trustees should assess the risks involved in accepting a deficit funding agreement and make sure that the terms of the contract are clear about factors such as the conditions on which the funding will be given and how achievement of outcomes will be determined. They should also ensure that they have the capability to measure their outcomes. Where trustees are unhappy about the terms of any contract they should try to re-negotiate and, if the situation does not improve, reject the funding wherever possible.

Charity Commission cases include situations in which charities have got into difficulties because they either had no formal contract or their contract did not cover them for all eventualities.

⁹ The Charity Law Association's paper 'Charities and Local Authority Contracts', available via their website, highlights some of the issues encountered in forming and maintaining contracts and shows how charity law affects a charity's ability to make contracts.

¹⁰ HM Treasury's Cross Cutting Review, *The Role of the Voluntary and Community Sector in Service Delivery*, promises full implementation of the Compact and makes several recommendations for improvements in the way the government interacts with the voluntary sector, including a move away from one-year and end-loaded contracts.

This case illustrates what can happen when trustees do not ensure that they are sufficiently covered by the terms of a contract.

A number of charities came to the attention of the Charity Commission because they had run into difficulties when their local authority suddenly pulled its funding. Some of the charities employed staff and were obliged to pay redundancy. There was no agreement in the charities' contracts with the local authority to cover such costs and many of the charities had no funds in reserve due to the restricted nature of their funding up to that point. These charities were forced to wind up their activities as a consequence.

The trustees of these charities put charitable funds at risk by entering into contracts that did not protect their long-term interests.

A local government authority can decide not to renew a contract and charities are often affected by the priorities of their local authority. The Charity Commission has seen many cases in which charities have struggled or been forced to wind up because of funding being cut at short notice.

Delay in releasing funding is another potential problem faced by charities contracted to provide public services. Many of the charities consulted during our research stated that delayed funding had

caused them cash flow problems. The Charity Commission is aware of cases in which funds have been paid so late that they have arrived close to the deadline by which they have to be applied. Trustees are then forced to rush their spending decisions or face losing the money. That does not represent sufficiently independent governance.

- Trustees should ensure that the terms of any contract they enter into safeguard the interests of their charity and its users.

Related Charity Commission Guidance:

Charities and Public Service Delivery: An introduction and overview (CC37) gives advice and guidance to trustees and staff of charities thinking of entering into contracts with public bodies to provide services in return for payment.

Grant funding

A significant number of charities depend upon grant funding for some or all of their income. 41% of surveyed charities had received grant funding and 25% were in receipt of grant funding at the time of the survey. For 15% of respondents, grant funding was their main source of income.

Grant funded charities face similar issues to contract funded charities. Receipt of a grant can be a significant positive milestone for a charity. However, the restricted nature of most grant funding can compromise trustees' independence of governance and restrict their ability to develop as they would like.

The survey showed that the problems charities experienced in relation to grants included having difficulty securing core costs (34%), charities' requirements not being reflected in funders' priorities (15%) and funders putting an excessive administrative burden on charities (40%).

"During the first few years, managing our grants took up about a third of my time."

Chief executive of a rapidly growing charity.

Whilst charities exist in a challenging funding environment, they should not seek grants that are rigidly prescriptive about how income is to be applied, especially if they do not have recourse to other sources of income. The Charity Commission sees cases where charities experience difficulties because their funding cannot be channelled into related areas not specified in their grant application. For example, some grant makers give funding for a salary while others will fund a post. In the latter situation the money can be used to fund re-recruitment costs if the original staff member moves on, whereas this is not possible if the grant maker specifies that the funding is for salary costs only.

Charity Commission casework experience shows that charities which make well-informed grant applications are better able to manage the funding they receive. The cases in which charities have run into difficulties often involve funding for projects that are too complex for the charity to comfortably deliver. Again, many of these grant-related problems can be attributed to inadequate planning that fails to take account of such things as the resources required to deliver the project and cover its administration.

This case illustrates what can happen when a charity makes a grant application without sufficient preparation.

A dispute between trustees of a village hall came to the attention of the Charity Commission when one group made a complaint about the other. The dispute centred upon an application for grant funding to build a new hall which one group did not want. A complicating factor in the dispute was ambiguity in the governing document which was unclear about various issues including who the trustees were.

Charity Commission staff held meetings with the disputing groups and were able to effect a compromise and prevent the matter from going to court. A Scheme of the Commission was produced which regularised the issue of trusteeship and other areas of confusion.

The trustees who made the grant application did not have the agreement of the community as a whole or a clear understanding of the legal basis of their charity and their role within it. It was almost inevitable that this would lead to a dispute that could not be resolved by reference to their governing document.

Grant making charities

Grant making charities are subject to the same strictures as all charities and must ensure that their grant making policy fulfils their objects. A grant making charity should ensure, to the best of its ability, that its funds are applied in the most effective manner in line with the terms of its

governing document. As part of that duty, administration, both for the grant maker and the funded charities, should be proportional to the size of the grant. Equally, the personal preferences of trustees must not dictate where grants are awarded.

This case illustrates the need for trustees of grant making charities to apply their funds in keeping with their governing document and not their personal preference.

A grant making charity had a level of reserves that triggered the Charity Commission's monitoring system. The trustees of the charity said that they couldn't find anywhere to spend the money. On examining the charity's governing document it was discovered that the charity's objects referred to a much larger geographical area than the trustees had been considering. It was merely their personal desire to limit the area of benefit that was causing the money to accumulate. The Charity Commission insisted that the charity spend its money in keeping with the area of benefit detailed in its governing document. Monitoring shows that the charity has now applied its income appropriately.

Managing fundraising

Fundraising can be legally complex and time consuming. It requires active management and should form an integral part of a charity's strategic plan.

The Charity Commission usually only becomes actively involved in charities' fundraising practices when there is cause to believe that funds are being lost or wasted because of poor management or dishonest activity. The Charity Commission also has a role to play in promoting the effective use of charitable resources, including fundraising.¹¹

Fundraising is one of the highest public profile activities that a charity engages in. Managed well, it can be a major source of

income. Managed badly, it can undermine the public's confidence in the integrity of charity. Fundraising features highly in the inquiries and evaluations that the Charity Commission carries out (15%).¹² These often centre on the four fundamental elements of fundraising - legality, transparency, accountability and financial controls.

The Charity Commission will intervene if we have reason to believe that a charity's fundraising practices are damaging to their beneficiaries, stakeholders or the wider integrity of charities, or where trustees are in breach of legislation.

This case illustrates what can happen when fundraising is not properly managed

A charity began an appeal to fund the establishment of a clinic at a local hospital. During routine scrutiny of the charity's accounts, the Charity Commission became concerned about apparently high fundraising costs. A formal inquiry was opened.

The appeal initially received corporate funding and significant income from organised fundraising events. However, changing circumstances meant that corporate support dried up and organised fundraising events became very labour intensive, generating high income but low profit.

The appeal continued despite concerns raised about its long-term future and without a formal business plan in place. A new Appeals Director was recruited but at that time a number of trustees were coming to the end of their 3-year terms of office. As a result, the Appeals Director was not closely monitored for the first few months of his employment.

The fundraising objectives became unclear and working practices were in need of improvement. The new trustees dispensed with the services of the Appeals Director.

The clinic has been built and handed over to the local NHS Trust, the appeal is now closed. The present trustee body has adopted a more hands-on approach to the day to day running of the charity.

¹¹ Section 1(3) Charities Act 1993.

¹² The Charity Commission can open a formal inquiry into a charity under Section 8 of the Charities Act 1993. Details of these cases are published on our website. Evaluation cases are opened when there is cause for concern and to determine whether a formal inquiry is appropriate.

Funding

Trustees should familiarise themselves with the specific legal requirements relevant to the form of fundraising they are planning to undertake and ensure that they comply fully with them. The Institute of Fundraising provides comprehensive advice on legal requirements and best practice considerations relating to different types of fundraising ventures.

- Trustees should ensure that fundraising is actively managed, even when it is contracted out, and that it complies with all relevant legal requirements.

Related Charity Commission Guidance:

Charities and Fundraising (CC20) sets out a number of factors that should be considered in the planning process for fundraising.

Charities and Commercial Partners (RS2) provides a detailed examination of the issues involved in outsourcing fundraising.

Raising funds through appeals

Most appeals with a specified target raise either more or less than anticipated, and predicting anticipated funds is difficult. However, this is only problematic if trustees have not made provision for what they should do in this eventuality and have not included details in the appeal literature. Where funds are raised through a public

appeal, trustees of charities that exceed or fall short of a specified target must either try to return the money or seek permission to apply it 'cy-près', that is to purposes as near as possible to the original, unless the appeal specified what would happen to any unused money.

This case illustrates what can happen when a charity appeal is set up without provision for how to apply surplus funds.

A charity that was set up to help families in need after a large disaster was unable to distribute all of the funds raised. Charitable funds cannot be used to give individuals benefits above their needs. Response to the appeal was greater than anticipated and donations far exceeded the money required to meet the needs of the specified beneficiaries. The charity had not made provision for what it would do with excess funds. The result was bad feeling among stakeholders and trustees couldn't apply the funds as they had intended.

If greater care had been taken over the terms in which the appeal was originally set up, the charity could have simply put the excess funds to use for wider purposes within the community and the families would have been saved a great deal of distress.

Funding

Charities are often established with a specific target in mind - to build a community centre, for example - and reaching that target is a definite milestone. A well run charity will have clear plans to determine what their charity will do once its target has been reached and will ensure that their charity's governing document makes provision for these planned activities.

- Trustees should ensure that the terms of an appeal include details of how income will be applied if it exceeds or falls short of the target.

Related Charity Commission Guidance:

Disaster Appeals: Attorney General's Guidelines (CC40) sets out guidelines to help people setting up an appeal to avoid the problems commonly associated with them.

Raising funds through trading

Setting up a trading subsidiary is a key event for many charities because it represents a new source of income and involves significant structural changes within the organisation.

Two casework examples follow which illustrate common issues associated with charities and trading:

- the relationship between primary purpose activities, ancillary trading and trading in its own right; and
- the financial viability of trading subsidiaries.

Charities can engage in two main forms of trading. One is 'primary purpose' trading - trade that is necessary to fulfil the charity's reason for existence. The other form,

'ancillary trading', is that which is not the primary purpose of the charity, for example a café within a charitable museum.

Income from trading purely for fundraising, such as a charity shop, is not subject to the charity tax relief that applies to other charitable income, and should be placed in a non-charitable trading subsidiary so that it is clearly separated. This includes splitting the time of any staff employed by the charity who also undertake work for the trading subsidiary. The Charity Commission can offer assistance to ensure that the paperwork that accompanies this process is correct. The Inland Revenue's publication IR2001 offers an excellent explanation of tax-exempt trading.

This case demonstrates the need for trustees to take care when trading, ensure that their charity's activities are authorised by its governing document, and seek advice from the Charity Commission where there is any doubt.

A charity had a café on its premises that was correctly classed as ancillary trading. This was permitted by its governing document and there was no need to set up a trading subsidiary.

The charity then began to rent out the café for events that occurred when the venue was closed to the general public. The charity did not set up a trading subsidiary to facilitate this change and therefore did not pay the correct tax.

The trustees of the charity contacted the Charity Commission when the problem became apparent. We advised them to re-organise the charity so that money from trading would be directed through a trading subsidiary and taxable income could be accurately accounted.

The Inland Revenue insisted that the charity repay tax on all its trading activities, backdated over a number of years.

The trustees were deemed not to be liable for these costs because they had acted prudently by taking advice before expanding their use of the café, although that advice was poor. Repayment, therefore, came from the charity's resources. Had the charity not been financially robust, the trustees' failure to ensure that its activities were wholly charitable would have caused the charity to fold. Had the trustees acted without taking advice, they may have been deemed liable for the loss and forced to repay the Inland Revenue from their private resources.

Where trustees intend to finance a subsidiary company from the charity's own resources, they should make sure that:

- they have the power to do so; and
- have properly assessed the financial viability of the subsidiary trading company.

Professional advice might be required to assist in this process. Trustees must take all reasonable steps to minimise any loss to the charity if the venture fails and must be particularly careful in situations where the subsidiary trading company is operating at a loss and requires new capital.

This case illustrates how a charity can incur losses by failing to ensure that its trading subsidiary is properly set up and financially viable.

The Charity Commission's monitoring of annual returns and accounts highlighted some irregularities in the transactions made between a charity and its trading subsidiary. A formal inquiry was opened.

The trading company had been set up to raise funds for the charity through a lottery, under advice from a fundraising company. The charity had funded the trading subsidiary's start-up costs on the assumption that it would quickly become profitable but the trading subsidiary proved unsuccessful at raising funds. As a result, the charity provided additional financial support to the trading subsidiary. The support was described in the charity's accounts as 'loans' but no formal loan agreements were in place and no security was raised. Without the charity's support, the trading subsidiary would not have been viable.

The Charity Commission advises that charity funds should not be used to prop up an insolvent or failing trading subsidiary. The trustees in this case had not set a limit on the extent to which they would support the trading subsidiary and should have shut it down when it became apparent that the venture was not going to become financially viable.

The contract by which the trading subsidiary's activities were governed was between the commercial fundraising facilitator and the charity. Consequently, all the financial risks of the trading subsidiary remained with the charity, negating the protection from the risks of commercial trading that the trading subsidiary is set up to offer.

Following the Charity Commission investigation, the trading subsidiary was wound up and the trustees of the charity were authorised to write off loans totalling nearly £150,000. The investigation concluded that the trustees had not acted as prudently as they might have done but did not deem them liable for the loss because they had not acted in bad faith and had sought some professional advice.

Undertaking trading is a key milestone for a charity and trustees should ensure that:

- the affairs of a charity and its trading company are kept separate;
- a trading subsidiary is only created after a proper financial assessment; and
- monitoring procedures are in place to evaluate the trading subsidiary's success, with contingency plans should it prove unsuccessful.

Related Charity Commission Guidance:

Charities and Trading (CC35) explains when charities may engage in trading activities for fundraising purposes, and when a separate subsidiary trading company should be established to carry out those activities.

Internal Financial Controls for Charities (CC8) gives guidance on monitoring a charity's financial position and its investments.

Managing change

Charities change, like any organisation, under the influence of various factors - economic fluctuations, trends in donor giving and grant making policies, changes in beneficiaries' needs for example. As part of this change trustees need to ensure that the governance structure and capacity of the charity keep pace and remain appropriate to meet its purpose efficiently and effectively.

Updating the governing document

This report has already noted the importance to charities of working within a governing document that accommodates their activities and way of functioning. A governing document should also include provision for amendment as the charity evolves. The Charity Commission recognises the importance of a governing document that is fit for purpose. Of the guidance given to charities on governance or administration in 2002, 29% was in the form of alterations to objects or governing documents.

Related Charity Commission Guidance:

Amending Charities Governing Documents: Orders and Schemes (CC36) provides guidance to help trustees who need to apply to us for an Order or a Scheme. It sets out the circumstances in which trustees will need to approach us for help in changing the purposes of the charity or its administrative provisions. It describes the differences between an Order and a Scheme and how we make them. More detailed coverage of the issue can be found in Operational Guidance **Orders and Schemes (OG1)** available on our website.

Unincorporated charities: Amendments to Governing Documents (OG 45) and information sheet **Amending Governing Documents: Unincorporated charities (CSD-1342A)**, available on our website, provide guidance especially for smaller charities (ie those charities with an income of less than £10,000 per year).

Developing capacity

For a charity to remain efficient as its work expands, its ability to carry out that work needs to expand in step. This may include considering whether to take on staff and changing the charity's way of operating to accommodate more work and greater complexity. It may also involve re-evaluating the balance of skills on the charity's board and among its staff and volunteers to cope with increased administration of income and charitable activity.

Charity Commission casework, survey data and consultation with umbrella and advisory bodies all indicate that charities do not develop their organisational capacity to a sufficient extent. This is partly due to the fact that capacity building is simply not a consideration for some charities and partly due to an inability or failure to plan ahead - see **Planning**. Funding restrictions can also limit charities' ability to develop their capacity.

Managing change

The majority of charities surveyed stated that they had never made changes to their management/governance structure (69%) or to their trustee board (54%). Of those that had made changes to their management or governance structure, 71% had at least a yearly plan in place. Likewise, 58% of charities that had made changes to their trustee board had a yearly or longer term plan in place. Changes to the trustee board were equally as likely to be made in response to unforeseen factors as they were to be part of a strategic plan, while 64% of changes to the management or governance structure were part of a strategic plan and 36% in response to unforeseen factors.

Many of the rapidly growing charities consulted during research for this report said that, with hindsight, they would have developed more slowly to allow themselves to step back and take a more strategic perspective.

"It was like being on a runaway train. We needed to stop and take a breath."

Chief executive of a rapidly growing, grant funded charity.

This case illustrates a best practice way of using grant funding to expand organisational capacity.

Charity Commission staff met with a small charity which was growing quickly in response to heavy demand for its services and needed to amend its governing document accordingly. The charity was presented with the opportunity to apply for a large grant to continue to expand its services. The grant application did not form part of their business plan. The trustees and chief executive held a meeting and decided not to go forward with the application because they were already working to the limit of their capacity. Instead, they applied for an interim grant to help them to develop their organisational structure and systems and, having ensured that they were able to manage a large increase in income, and having adjusted their business plan accordingly, they applied for the large grant.

With hindsight, the trustees reported that their decision to delay was correct. The amount of work involved was, in fact, even greater than they had anticipated.

Employment

"One of the fundamental step changes in the life of a charity...is when they become an employer."

Chief executive of an advisory body.

Over one in five of the charities surveyed that provide a service or support are entirely trustee run. The evolution from a trustee run charity to a charity with paid employees can be a big cultural and organisational shift.

The charities and advisory bodies consulted for this report consistently cited employment as the most significant and potentially problematic issue that charities face. 41% of surveyed charities with paid staff do not have yearly or longer term plans that would enable them to manage this change effectively. 66% of survey respondents have staff or volunteers or both. 39% of these charities reported that they are not confident that they are up to date in their understanding of employment legislation.

Volunteers are also an invaluable asset to charities and over one in three of surveyed charities rely on the work of volunteers. However, trustees are often unaware that volunteers may have some of the same rights as paid staff and that, in some cases, the terms of a volunteer's involvement with a charity constitute a contract of employment.

Employment cases make up a relatively small proportion of the cases handled at the Charity Commission but they are often serious cases. Unanticipated costs associated with employment can cause charities to fold and failure to act prudently has the potential to leave trustees personally liable for losses incurred. Staffing issues that do not require Charity Commission intervention can still reduce efficiency and result in bad publicity that is damaging to the name of charity.

There are countless issues to consider when employing staff: employment contracts; working space and the regulations that apply to it; systems of management and reporting; funding of salaries, national insurance, pensions and so on; and additional or on-costs. There is an added dimension when charities are working in partnership with another organisation and share staff or have staff who also carry out work for their trading subsidiaries. Charity Commission staff have seen cases that range from charities that have taken on staff without any space to accommodate them to charities that have faced large, unexpected bills in order to comply with employment regulations.

Problems occur when charities fail to fully appreciate what employment entails. In an open survey question in which charities were asked to note an event that was unexpected or had unexpected consequences, 13% reported employment issues. This is lower than anecdotal evidence suggested but confirms that charities are not always prepared for the impact of employment. It also suggests that building skills in employing and retaining staff is perhaps an area which the Home Office and HM Treasury could focus on as part of their capacity building and infrastructure strategy if charities are to play a greater role in providing public services.¹³

Balancing responsibilities between trustees and employees

When charities take on staff there should, ideally, be a clear divide between governance - the role of the trustees (who are also directors if it is a charitable company) - and management - the role of the chief executive or management who direct the daily running of the charity. When there are only a few staff in place and trustees are still involved in the daily activity of the charity, the division of labour between governance and management can be difficult to maintain.

At the heart of a significant number of situations that result in a Charity Commission Section 8 inquiry is a trustee body that does not have an appropriate level of control. Commonly, a dominant trustee has remained too involved in the daily running of the charity once staff are in place or the chief executive has been allowed to run the charity unchecked and the trustees have become too removed.

¹³ See the proposals for a *futurebuilders* fund (July 2003) following the recommendations within the Treasury's Cross Cutting Review, *The Role of the Voluntary and Community Sector in Service Delivery* and the Home Office proposals for supporting the voluntary and community sector.

Managing change

Trustees who do not allow their charity to be managed by those appointed to do so often disrupt its running. When a charity becomes complex enough to require staff, the trustees cannot be personally involved in everything and trying to do so can result in maladministration.

Similarly, managers or chief executives who retain too much responsibility for the running of a charity and fail to sufficiently involve the trustees (in which case the trustees may also be at fault for accepting such a situation) or are selective about what they report to trustees are often the cause of maladministration. Many of the cases involving dishonesty that the Charity Commission sees have begun with small misdemeanours and escalated when the individual goes unchallenged.

The drive and energy exhibited by the founding individual(s) of many charities may not be the qualities that are needed when the charity is more established. Many charities struggle in their early years and the sort of person who can root out the

funding and work long hours getting the charity up and running often finds it difficult to step back when the charity is more stable and has more staff to share the workload.

Smaller charities can experience a loss of focus and morale when an individual who has been a strong, positive force within a charity leaves. The departure of a dominant individual is a good opportunity for existing trustees and staff to reassess their roles and instil a better balance of authority within the charity.

Whether it is a trustee, chief executive or other member of staff that resists the evolution of a charity, it can be extremely costly and is a common cause of maladministration. Internal relations can break down to the extent that a charity's work is disrupted, good staff can be lost and opportunities for development missed. Grant makers will sometimes withhold their funding if they are aware that there are disputes within a charity.

This case illustrates the dangers of allowing one trustee to take too much control.

The Charity Commission opened a Section 8 inquiry into a charity in which the founding trustee had been taking decisions without holding formal meetings and consulting his fellow trustees. One such decision was the termination of the contracts of two employees, which led to an industrial tribunal that ruled against the charity. The charity was forced to pay £2,000 compensation.

A previous inquiry had been opened into the charity because of inadequate financial controls - the finances of the charity were being handled almost exclusively by the founding trustee. Advice arising from that inquiry had been ignored.

A new trustee was appointed following the second investigation and the founder trustee resigned. Financial controls have now improved and all decisions are shared between the trustee body.

Managing change

Cases in which trustees have taken unauthorised benefit from their position are commonly the result of individuals considering themselves to be entitled to it on the basis of the amount of time they devote to running the charity.

- Trustees should ensure that their own roles and those of the charity's managers and employees are clearly defined so that all parties understand the scope of their responsibilities.

This case illustrates what can happen when the founders of a charity do not accept that they cannot maintain full control over a charity or take benefit from their position.

A charity was established by two parents in response to the death of their child. The couple were the only trustees and the only people running the charity. In spite of the fact that the charity's governing document prohibited the payment of trustees, both trustees received payment because they were working full time running the charity and felt that they needed to support themselves. Following a Charity Commission investigation, the trustees resigned, identified others to act as trustees and continued to work as employees of the charity. The new trustees came into constant dispute with the founding couple because they were not able to distance themselves personally from the work of the charity and could not allow others to run it for them. This culminated in an industrial tribunal case and a further Charity Commission investigation.

The charity had been functioning in a disorganised and unfocused manner due to the personal tensions within it and its financial administration was a cause for concern. Since the removal of the founding individuals, the charity has been able to function in a more organised, accountable and successful manner.

Acquisition and disposal of land

At any stage in a charities' lifecycle, acquiring and disposing of land are significant events.¹⁴ Responses to an open question about key events showed that 30% of surveyed charities listed property as a key event. This was the highest category for any single event (charities could list up to three).

Disposing of and acquiring land can have a significant positive impact on a charity when well managed. For example: buying office space can provide greater independence for charities that have previously paid rent and/or relied on grants for their accommodation; buying new facilities can allow a charity to expand the services it provides; selling land can provide a huge boost in income.

¹⁴ Disposal means sales, leases, grants of rights of way or other rights, exchanges of land, and all other transactions in which trustees part with or grant an interest in their land except for the release of a rent charge and the granting of a mortgage.

Managing change

When involved in a land transaction, effectively run charities will:

- properly plan and manage the transaction and its effects;
- ensure that it represents the best interests of the charity and its users;
- comply with the various statutory requirements; and
- engage good quality professional advice to assist in the process.

If a charity is to hold land it is advisable that it is constituted as a company or has an incorporated trustee body. A company constitutes a legal person and, as such, it

may hold property of all kinds in its corporate name. Trustees do not, therefore, have to hold the property in their own names and this limits the risk to them as individuals. Holding property in a corporate name also avoids the expense and inconvenience of transferring it when trustees are replaced.

Problems usually arise when charities are involved in acquiring land for the first time. Lack of experience, sometimes coupled with insufficient or inaccurate professional advice, result in oversights that can be extremely costly.

This case illustrates the difficulties that charities can face if they do not seek professional advice before entering into a property transaction.

A growing charity received funding to buy office space. The space had previously been used for other purposes and so required conversion. The trustees received a quote for the cost of the work and put in their bid for funding on that basis. However, the work quoted for did not take account of regulations that apply to working space. As this was the first time the charity had been involved in buying commercial property, the trustees were not fully aware of the regulations that they needed to meet. They received grant funding on the basis of the quote and went ahead with the conversion. However, an inspection by the Health and Safety Executive highlighted various regulatory breaches. The charity had to modify the building in order to adhere to standard requirements, which more than doubled its budgeted expenditure. The additional costs were met out of the charity's reserves.

The lack of awareness of health and safety regulations within this charity could have forced it to close. The purchase of office space should have been a progressive step for the charity but instead they are in a position of trying to rebuild their reserves.¹⁵

¹⁵ The Health and Safety Executive produces a free leaflet entitled '5 steps to Risk Assessment'. HSE Books produce a publication entitled 'Charity and voluntary workers, a guide to health and safety at work'. Unison produces a free downloadable guide to the 'six pack' of health and safety regulations that apply to the workplace as well as information relating to other health and safety matters.

Charities and the general public are often unaware that trustees cannot sell land at less than the best price, even if to do so would avoid selling to a purchaser that they or their local community find objectionable. They can reject an offer on the grounds that land will be used in a way that is directly contrary to the purposes of the charity or accept a lower offer if the new purpose for the land is compatible with the charity's trusts. It is sometimes permissible for a charity to sell or lease land to another charity for less than the full market value. Trustees should take advice on this.

Cases opened at the Charity Commission include situations in which trustees have either sold land below the market price and are therefore failing in a statutory requirement, or want advice because they are unhappy about selling to the highest bidder.

Some charity projects involving land arouse opposition which leads to media attention and phone calls to the Charity Commission because it is assumed that the charity can be selective about the buyer to which it sells. Trustees should make information about such a sale available to the public and, where appropriate, pursue a pro-active publicity campaign. The costs can be justified by the counteraction of a negative public profile which can damage the good name of charity and impact on income.

It may be necessary for a charity that receives a large amount of income from the sale of land to update their trusts. Trustees should contact the Charity Commission for advice.

This case is an example of a situation in which a charity needed to update its trusts after sale of land resulted in a large rise in its income.

A church charity received a considerable amount of income from the sale of land. The governing document of the charity stated that the vicar was entitled to a certain percentage of income from the land which meant that he was now entitled to a very large sum of money. The vicar and the charity approached the Charity Commission to update the trusts so that the money would remain within the charity.

Sometimes a charity's governing document stipulates that land should be used for a specific purpose. This does not bar the charity from selling the land as long as proceeds from the sale are used to purchase land that will be used for a similar purpose. An example of a case in which this happens is where a charity that owns a recreation ground sells it to a developer and buys alternative grounds to serve the same purpose, making a considerable profit. If the trustees do not wish to buy replacement property, they should contact the Charity Commission for advice before the sale proceeds.

If land forms part of a charity's permanent endowment, then the proceeds will also be permanent endowment and cannot normally be applied without an Order from the Charity Commission.

These are only some of the many issues that trustees should take into consideration and they illustrate the potential complexity of property transactions. The legal position on land is set out in Sections 36-40 of the Charities Act 1993.

- Trustees should seek the appropriate level of legal advice before entering into a property transaction.

Managing change

Related Charity Commission Guidance:

Charity Commission publications **Acquiring Land (CC33)** and **Disposing of Charity Land (CC28)** outline the areas that trustees should consider, the statutory requirements that they must meet and the points at which Charity Commission involvement is required.

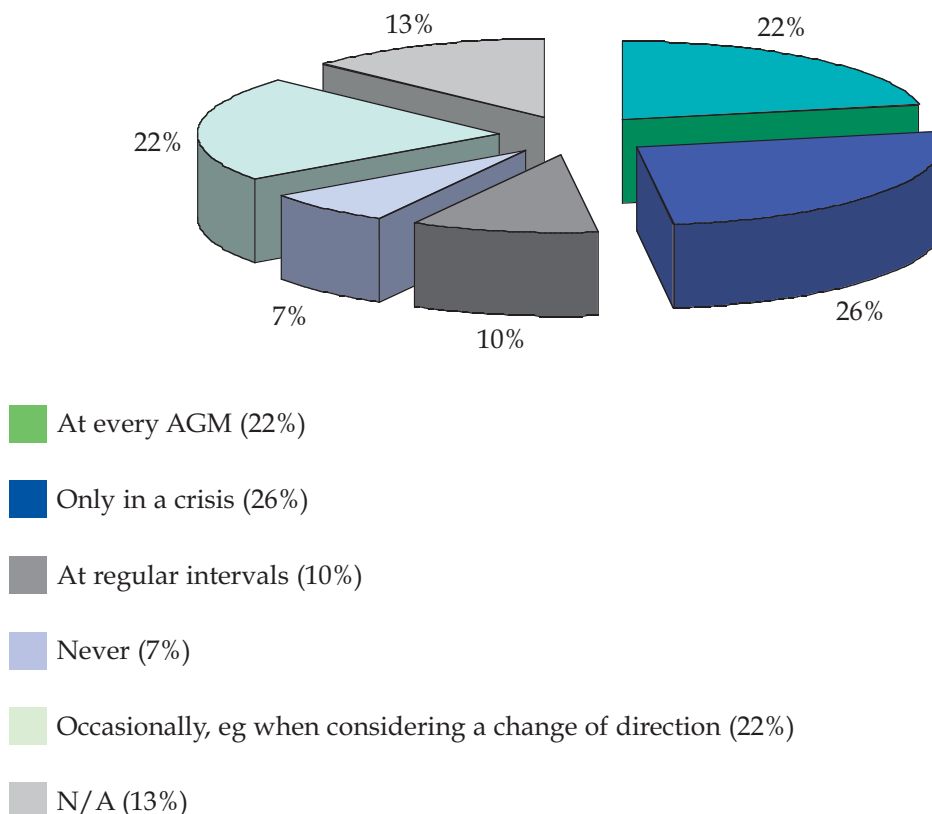
Guidance tailored specifically for small charities relating to the issues raised in this section: **Small Charities: Transfer of Property, Alteration of Trusts, Expenditure of Capital (CC44)**; Operational Guidance **Small Charities: Disposal of Charity Land and Buildings (OG204)**; and information sheet **Disposals of land and buildings with particular reference to recreation ground charities**.

Winding up

A charity that continues to operate without a viable future may be wasting funds that could be better used by winding up the charity and transferring its assets to another charity. Winding up a charity can

be a positive step to either acknowledge that the charity's mission is complete or obsolete or that charitable funds can no longer be effectively applied by that organisation.

How often does your charity assess if it should continue?



Managing change

Some charities have a clearly identifiable aim and wind up when it has been achieved. Others specify in their governing document the length of time for which they will be operational. In many cases charities peter out and do not wind up in an organised fashion. An emotional attachment to a charity and its cause often prevents trustees from winding up their charity when it becomes clear that it no

longer has a viable future. Dwindling interest from trustees, volunteers and donors is another cause of charities slowly unravelling rather than actively taking the decision to wind up. This is frequently linked to beneficiaries' needs being less immediate but, regardless of the level of demand for a charity's services, trustees should not allow charitable funds to be swallowed up by an ineffective organisation.

These cases illustrate good and bad practice in terms of assessing whether to continue with a charity's activities.

A charity that was set up to preserve a local historical site was wound up following a meeting in which trustees decided that the charity had served its purpose. Interest in the site had increased during the course of the charity's work so there was sufficient funding and support from other sources to ensure that the site would be preserved. The charity transferred its excess funds to charities with similar objects. The trustees had anticipated that the charity would not need to continue indefinitely and had made provision for winding up in its governing document. The Charity Commission removed the charity from its register when all final records and accounts were received.

A fee-charging educational charity which owned land and employed staff ran into difficulties when demand for its services slowed. The trustees continued to operate the charity on the belief that its position would improve but it did not. The trustees' belief that the situation would improve seemed to be largely based on an emotional attachment to the charity. The Charity Commission advised the trustees that they ran the risk of insolvency and the trustees finally recognised that it was inevitable that the charity would have to wind up. The Charity Commission facilitated the transfer of its assets to another charity with similar purposes and the failing charity was removed from the register. Had the trustees been more realistic the value of the assets it passed on would have been greater.

Trustees of an unincorporated charity can only be indemnified out of the assets of the charity if there are sufficient assets to cover their debts. Therefore, if a charity continues to incur costs to the extent that its liabilities outweigh its assets, the trustees may be personally liable for the charity's debts regardless of whether they have acted prudently. See **Incorporation**. Likewise, trustees of a charitable company should minimise their expenditure when it becomes apparent that insolvency is unavoidable, otherwise they can be forced to contribute toward the payment of the charity's debts. It is illegal for a company to

trade when it is insolvent so trustees must be aware of when the charity has reached this point.

Alternatives to winding up

It may not be necessary to wind up in order to secure a future for a charity that still has beneficiaries to serve. Joining forces with another charity, either by working collaboratively or merging, is another way in which charities can ensure that funds are put to best use.

This case illustrates how a charity ensured that services to its beneficiaries continued when local authority funding was cut.

A care centre run by a local charity faced closure when the County Council that funded it was unable to continue its commitment. The charity secured an emergency grant from another agency to continue its services in the short term. It also made contact with a national charity with similar objects to enquire if the national charity could take over the running of the centre. The larger charity decided, on the basis of a feasibility study, that it would be able to take over and continue to provide the service to beneficiaries. As a result, the people of the local area still have access to the service they need.

Trustees of charities set up with a specific target sometimes find that additional needs become apparent in the course of their work. For example, a charity with objects to provide hospital equipment may find that, once the equipment has been funded, the users of that equipment need transport. There are several ways of responding to this kind of situation. A charity's governing document should include a power of amendment, otherwise trustees of an unincorporated charity will have to seek Charity Commission authority to broaden its objects.

A charity with the power of amendment should ensure that new objects accord with their trusts. The beneficiaries are key; new objects should be to the advantage of

current beneficiaries and should not conflict with other objects. For example, the charity in the situation outlined above should not start providing transport if there is still an outstanding need for equipment.

Founding trustees should ensure that their governing document includes a power of dissolution which allows the trustees to wind up the charity and outlines how it will be done. For example, it should provide details of how any remaining funds will be applied.

- Trustees should give regular consideration to whether or not their charity has a viable future and a good reason to continue.

Related Charity Commission Guidance:

Charity Reserves (RS3) and Collaborative Working and Mergers (RS4).

Managing Financial Difficulties and Insolvency in Charities (CC12) provides guidance for charities that are in financial trouble and also advice about how to recognise when a charity is in danger of becoming insolvent.

Internal Financial Controls for Charities (CC8) also provides guidance on maintaining healthy finances and keeping up-to-date on the financial situation of a charity.

Small Charities: Dissolutions and Removal from the Register (OG202) and information sheet **Guidance for small charities winding up (CSD-1344A)** highlight the issues that small charities need to consider.

Annex A - Questions to ask at each stage

The following lists provide trustees with questions that they may find useful to ask themselves at various stages of their charity's development. The points covered have been drawn from our casework and from the responses to our survey. They are included here as a resource to help trustees as one part of their wider consideration of an issue. They should be regarded as a starting point and not the last word on a particular issue. Relevant Commission publications in which further guidance can be found appear in brackets.

Starting up

- Do we need to establish a new charity or is there another charity already trying to achieve the same aims in the same area? (See **The Register of Charities** on the Charity Commission website at www.charitycommission.gov.uk. See also **The Register of Charities: Information and services available (CC45)**.)
- Do we have to register with the Charity Commission? (With some exceptions, it is a legal requirement for charities with an income over £1,000 per annum to register with the Charity Commission. See **Registering as a Charity (CC21)** and **Exempt Charities (CC23)**.)
- Is there a model governing document that can be adapted for use by the charity? (These may be provided either from the Charity Commission or other large national parent charities. See the Charity Commission website.)
- Have we made sure the governing document contains the provisions that the charity will need as it grows and evolves - including a power of amendment and power of dissolution?
- Have we looked at the governing documents of other similar charities to get an idea of what it is necessary to include?
- Have we considered what will be the most appropriate form for the new charity ie trust, unincorporated association, charitable company? (See **Choosing and Preparing a Governing Document (CC22)**.)
- Do all of the founding trustees understand their role and the governing document? (See **The Essential Trustee: What you need to know (CC3)**.)
- Is there an umbrella organisation to go to for guidance and information?
- Have we made some initial plans and projections? For example, have we thought about:
 - time required to run the charity
 - time required from each trustee
 - complexity of the accountancy involved
 - anticipated expenditure
 - projected income
 - the actions that will be possible if the charity either exceeds or falls short of projections and targets?

Questions to ask at each stage

Keeping pace with change

- Do we have a written plan for the charity that covers both the immediate future and longer time periods?
- Do we have a mechanism for reviewing our plan on a regular basis?
- Do we review staff skills, the composition of the board and the suitability of the governing document to existing circumstances and those expected in the future?
- Do we need to restructure our organisation or develop its capacity before increasing income and activity?
- Will a significant increase in income require additional resource management (eg the requirements of a higher SORP threshold)?
- Do we network with other charities and utilise umbrella bodies to find out from others' experience what to expect as we develop?
- Have we sought funding for capacity building and feasibility studies where appropriate?

Funding

- Do we regularly explore new funding sources?
- Does our current funding structure compromise our independence? (See **The Independence of Charities from the State (RR7)** and **Local Authorities and Trustees (OG56)**.)
- What can be done to diversify our income?
- Is our charity's level of reserves properly accounted for and set out in a comprehensive reserves policy so that funders can understand it? (See **Charities' Reserves (CC19)** and **Charity Reserves (RS3)**.)
- Do we need Charity Commission authority to accept funding? (If your funder seeks a charge over your charity's assets in return for a grant, you must contact the Charity Commission for authority.)
- Before we accept deficit funding, can we cover the interim cash flow situation?
- Are the terms of any contract(s) we accept covered in our charity's risk assessment? (See **Charities and Public Service Delivery: An introduction and overview (CC37)** and **Charities and Risk Management** on the Charity Commission website.)
- If we are currently unincorporated, is it necessary to incorporate before accepting a contract?

Questions to ask at each stage

- Are we clear about what the funder expects to see for their money eg how outcomes will be measured?
- Does our funding application include all the costs we will incur eg administration and core costs?
- Does our charity have the capacity to deliver the level of complexity that the funded project requires or is there a risk that we may over stretch ourselves?
- Does our charity have enough staff resources to cope with any extra administration both to apply for grants and to manage and monitor the application of funds throughout the period of the grant and beyond?
- Are we applying to funding bodies that make the type and size of grant we need?
- Are we ensuring that our grant applications are in keeping with our objects?
- Are we getting feedback and advice if funding bids are rejected?
- Are our fundraising plans part of a wider business plan?
- Are we familiar with the laws surrounding the specific type of fundraising planned? (See **Charities and Fundraising (CC20)**.)
- Is our fundraising venture cost-effective?
- Have we made provisions for what we will do if we raise more or less funds than necessary for the stated purpose of an appeal? (There are rules about this. See **Disaster Appeals: Attorney General's Guidelines (CC40)**.)
- Have we put in place adequate controls for monitoring and reporting on fundraising activities, especially when they are contracted out? (See **Charities and Commercial Partners (RS2)**.)

Trading

- Are there any restrictions in our governing document prohibiting or restricting our ability to carry out trading activities? (See **Charities and Trading (CC35)**.)
- Have we planned anticipated income and expenditure from our trading subsidiary carefully and realistically?
- Do we need to take advice from the Charity Commission or a professional advisor regarding setting up a trading subsidiary?
- Are we complying with the necessary tax rules associated with charitable and non-charitable trading? (Contact HM Revenue & Customs for information).
- Are we reviewing our trading activities regularly and do we have contingency plans in place, including winding up the subsidiary if it should prove unsuccessful?

Questions to ask at each stage

Employment

- Do we have all the necessary policies and procedures in place and are we compliant with all relevant employment legislation?
- Are we familiar with employment legislation, including that which applies to volunteers, and do we need to take professional advice?
- Will there be any costs involved in complying with employment regulation and legislation eg adapting the workplace to meet health and safety regulations?
- Have we considered how an increase in staff numbers will impact on the management structure and culture of the organisation?
- Do we have a job description and arrangements for induction and support of the person appointed?
- Are roles clearly defined, including lines of management?
- Are we clear about what is to be delegated to employees and what the trustees will remain responsible for? (See **The Essential Trustee: What you need to know (CC3)**.)
- Have we considered all the 'domestics' of employment including workstations, additional cost such as telephone calls, electricity etc?
- Have we factored in costs such as National Insurance and pension arrangements to our longer-term plans?
- Have we considered outsourcing as an alternative to employment?

Property

- Does our governing document include a power to dispose of or purchase land or property, where required? (Charity Commission authority is not usually necessary except in circumstances relating to Permanent endowment. See **Acquiring Land (CC33)** and **Disposing of Charity Land (CC28)**.)
- Have we planned the transaction carefully, taking full account of relevant legislation?
- Have we complied fully with Section 36 of the Charities Act 1993 before commencing a sale, including seeking appropriate professional advice, ensuring that the full market price is sought, and giving due public notice of the sale where necessary? (Charity Commission authority is required if S36 of the Act cannot be complied with.)
- Is the proposition financially viable in both the short and long term?
- Does the purchase represent effective use of charitable funds?

Questions to ask at each stage

- Does the charity have enough resources to manage an investment in land?
- Are the potential land/ buildings to be purchased subject to planning or legal use restrictions?
- In whose name(s) will the new property be held? (This will depend on whether your charity is a company or whether your trustee body is incorporated or there are individuals as holding trustees.)
- Have we informed all interested stakeholders of our intentions to buy/sell and considered the impact of our decision on the profile of the charity?

Winding up

- Do we give regular consideration to the continued need for our charity to operate and to its ability to do so?
- Is it necessary, or would it be more effective, to work collaboratively or merge with another organisation? (See **Collaborative Working and Mergers (RS4)**.)
- Would it be appropriate to utilise the power of amendment in the governing document and re-focus the charity to a more relevant need? (Charity Commission authority will be necessary in this case. See **Amending Charities' Governing Documents: Orders and Schemes (CC36)** and **Small Charities: Transfer of Property, Alteration of Trusts, Expenditure of Capital (CC44)**.)
- Do we have a power of dissolution in our governing document and does it provide details of how remaining assets should be applied? (Where there is no power of dissolution, trustees may need to contact the Charity Commission for advice.)
- Have we taken stock of the charity's assets and liabilities and considered issues such as staff notice and redundancy payments? (See **Managing Financial Difficulties and Insolvency in Charities (CC12)** and **Internal Financial Controls for Charities (CC8)**.)
- Have we put mechanisms in place to ensure that any future legacies that may be received are still applied to those beneficiaries for whom the money was intended?

Annex B - Survey findings

Research techniques

The data used in this report was derived from the Charity Commission's records and extensive casework archive. Meetings with individual charities and umbrella bodies also informed the research. In addition, Martin Hamblin GfK, an independent research company, undertook a postal survey of over 4000 charities registered with the Charity Commission in 1995. The survey achieved a response rate of 35%.

Survey findings

Table 1: Year in which surveyed charities were established (not necessarily year registered).

Year established	Number of charities	%
Before 1900	40	3
1900-1970	321	20
1971-1980	145	9
1981-1990	281	17
1991-1995	626	38
1996-2002	80	5
Not answered	129	8
	Base: 1622	

Table 2: Current sources of income and sources that charities would like to develop.

Income source	% charities with each income source*	% charities with each as MAIN income source*	Sources charities would like to develop (%)*	Sources charities have ability to develop (%)*
Contract	10	5	7	5
Donors	56	24	24	15
Grants	37	15	26	14
Investments	18	7	4	3
Members	39	22	11	11
Trading subsidiary	4	1	4	3
Rent	1	1	0.2	0.2
Fees/sales	25	15	5	6
Sponsorship	1	0.2	0.2	0.2
Nothing	0.2	-	0.1	0.2
Others	-	-	-	-
Don't know	-	-	0.1	0.1
Not answered	4	11	51	64
Base: 1622				

* Columns may add up to more than 100% because respondents could give more than one answer

Survey findings

Table 3: Extent of grant funding.

	% of charities
Currently grant funded	25
Have been grant funded but not at present	16
Never been grant funded	55
Not answered	4
Base: 1622	

Table 4: What charities request and receive grant funding for.

	% charities requested*	% charities received*	% found it most difficult source to secure*
Project costs plus related core costs	46	41	17
Project costs only	39	41	5
General running costs	46	40	34
Feasibility study costs	8	7	2
Consultancy fees	8	7	1
Financial aid for transport	1	1	1
Building work/refurbishment	1	1	-
Equipment	1	1	-
Never had difficulty securing funding	-	-	11
Not answered	-	-	33
Base: 663			

* Columns may add up to more than 100% because respondents could give more than one answer

Survey findings

Table 5: Grant-related experience of charities.

Experience	% charities*
Directed charity's activities so as to be eligible for a grant	22
Felt that charity's independence was compromised by terms of a grant	12
Rejected grant funding to avoid loss of independence	3
Had difficulty responding to changes in circumstances because of grants being tightly allocated or not available	15
Had grant application turned down because of charity's reserves	12
Had difficulty with recruitment or retention of staff	20
Found that charity's capacity was insufficient to deliver a grant funded project	5
Had difficulty meeting costs of deficit funded project	10
Had deficit funding withheld because charity didn't meet outcomes	1
Had difficulty meeting additional costs incurred as a result of getting a grant	9
Felt that time spent completing grant application and monitoring forms was excessive in relation to charity's work	40
None of the above	34
Not answered	5
Base: 663	

* Columns may add up to more than 100% because respondents could give more than one answer

Table 6: Level of planning.

Level of planning	Total % of charities	% of charities with employees*
We have a yearly and a long-term plan (eg 3-5 years) in place	19	26
We plan 1 year at a time	30	33
We make plans on an ad hoc basis, as seems appropriate at the time	14	15
We respond to events as they occur	10	10
We see no need for a strategic plan because activity is fairly constant	24	19
Others	2	-
Not answered	1	-
Base: 1687		

* Columns may add up to more than 100% because respondents could give more than one answer

Survey findings

Table 7: Type of activity by level of planning.

Type of activity	Level of planning (as % of total for each activity)*						
	Total % for activity	Yearly and longer term	One year at a time	On an ad hoc basis	Respond as event occur	No need for a strategic plan	Others
Provision of financial assistance (eg grant awarding)	22	10	29	17	17	30	1
Provision of a service/ support direct to beneficiaries (eg care, aid, advice, education)	65	23	32	14	8	24	2
Acting as an umbrella or resource body	5	29	26	20	10	17	1
Sponsoring or undertaking research	1.3	24	33	19	5	14	-
Housing/ accommodation	0.4	14	29	14	-	29	14
Conservation	1	7	21	29	21	29	-
Arts/theatre/choral societies/visitor attractions	3	20	41	8	6	26	-
Not answered	4	16	26	10	14	35	-
Base: 1622							

* Rows may add up to more than 100% because respondents could give more than one answer

Table 8: Factors that compromise ability to plan.

	Total %*	% of grant funded charities*
The current level of planning is satisfactory	43	28
Volatility in income and/or expenditure	26	34
Dependence on short term grant funding	23	69
Daily running of the charity takes up all available resources	22	40
Uncertainty about beneficiaries' future needs	9	9
Inability to get funding for feasibility studies or consultation work	6	12
Lack of specialist knowledge within charity	6	6
Inability to borrow money	4	9
Insufficient volunteer help	1	1
Base: 1622		

* Columns may add up to more than 100% because respondents could give more than one answer

Survey findings

Table 9: Charities that had made changes to management/governance structure or trustee board, by level of planning.

Level of Planning	% of those that had made changes to management/governance structure*	% of those that had made changes to trustee board*
Yearly and longer term plan in place	40	26
Plan one year at a time	31	32
Plan on an ad hoc basis	11	14
Respond to events as they occur	7	10
No need for a strategic plan	12	19
Others	2	2
Base: 1622		

* Columns may add up to more than 100% because respondents could give more than one answer

Table 10: Factors charities under and over estimated during their development.

	%				
	Under estimated	Accurate	Over estimated	Don't know	Not answered
Income	15	69	7	7	2
Expenditure	14	75	3	5	3
Complexity of accounting	18	69	2	6	5
Time required to manage the charity	39	52	1	5	3
Time required from trustees	25	61	2	7	5
Extent of regulatory and legislative requirements	34	45	1	16	4
Base: 1622					

Table 11: Events experienced that were unexpected or had unexpected consequences (open question).

Unexpected event	% charities that have experienced it
Change in government/council policy or legislation	25
Funding: failure to obtain/reduction/need for sudden increase	39
Changing costs of rent/insurance/maintenance of premises	16
Staff shortages/problems	13
Others	7
Base: 261	

Survey findings

Table 12: Most significant key events for charity (open question).

Milestone event	% charities that reported it*
Acquiring/repairing/planning/leasing/selling property	30
Securing grant/contract	25
Setting up as a charity/registration/registration as a charitable company	19
Employing/losing staff/problems with staff	12
Setting/exceeding financial targets/thresholds	8
Base: 1622	

* Charities could give up to 3 responses

Table 13: Number of charities incorporated, by year established.

	% established in each time frame						
	Total %	Before 1900	1900-1970	1971-1980	1981-1990	1991-1995	1996-2002
Charity is not a company	84	82	91	88	79	83	66
Charity is a company and was a company when originally registered	9	5	2	3	9	13	23
Charity is a company but originally registered as an unincorporated and later re-registered as a charitable company	5	11	5	7	10	3	4
Not answered	2	2	2	2	2	1	7
Base	1622	38	321	145	281	626	80

Table 14: Main income source, by whether incorporated.

	% charities with each main income source						
	Contract	Donors	Grants	Investments	Members	Trading subsidiary	Other
Charity is incorporated	59	11	31	9	3	36	8
Charity is not incorporated	40	88	68	88	94	64	90
Not answered	1	1	1	3	3	0	2
Base	85	392	245	109	349	14	260

Survey findings

Table 15: Level of planning, by whether incorporated.

	% with each level of planning*					
	Yearly and longer term plan	Plan one year at a time	Plan on an ad hoc basis	Respond as event occur	No need for a strategic plan	Others
Charity is incorporated (base 224)	53	23	11	4	10	2
Charity is not incorporated (base 1358)	15	32	15	12	28	1

* Rows may add up to more than 100% because some charities gave more than one answer

Table 16: Reasons given for becoming a charitable company.

Reason	% charities*
To protect the current trustees	60
On advice from a solicitor	49
On the basis of a risk assessment	34
Because the charity employs staff	33
On advice from an umbrella body or advisory body	30
Because the charity deals with vulnerable people or expects to in the future	26
To assist in the recruitment of trustees	22
Because the charity is complex or is likely to be so in the near future	17
To create a corporate identity for holding contracts	15
To create a corporate identity for holding land and/or shares	13
Don't know	6
Best way to manage the charity	3
For trading purposes - charging for services/rents	1
Not answered	2
Base: 224	

* Column may add up to more than 100% because respondents could give more than one answer

Table 17: Whether charities think incorporation was the right choice.

	% charities			
	Yes	No	Don't know	Not answered
Charitable companies	79	3	15	3
Base: 224				

Survey findings

Table 18: Charities with staff and/or volunteers, by awareness of current legislation.

% charities confident that there is an up-to-date understanding of employment legislation within the charity					
	Total %	Yes	No	Don't know	NA
Charities with paid staff and/or volunteers	66	58	18	21	3
Base: 1068					

Table 19: Charities that have made changes to their management/governance structure or trustee board.

Changes made to management/governance structure	% charities	Changes made to trustee board	% charities
Yes, as part of a strategic plan	14	Yes, as part of a strategic plan	18
Yes, in response to unforeseen factors	8	Yes, in response to unforeseen factors	19
No changes made	69	No changes made	54
Don't know	3	Don't know	3
Not answered	6	Not answered	6
Base: 1622		Base: 1622	

Table 20: Consideration of winding up.

How often does your charity conduct an assessment of whether its activities should continue?	% charities
At every AGM	22
Only in a crisis	26
At regular intervals	10
Never	7
Occasionally, eg when considering a change of direction	22
Not answered	13
Base: 1622	

Annex C - Glossary of terms

Capacity building is the development of structures, systems, skills, knowledge and resources so that charities are better able to achieve their objectives and realise their full potential.

Charitable company means a company:

- formed and registered under the Companies Act 1985; or
- to which the provisions of the 1985 Act apply as they apply to a company so formed and registered;

and

- which is established for **exclusively** charitable purposes.

A **governing document** is any document which sets out the charity's purposes and, usually, how it is to be administered. It may be a trust deed, constitution, memorandum and articles of association, conveyance, will, Royal Charter, Scheme of the Commission, or other formal document.

Insolvency. Charitable companies are 'legal persons', can incur liabilities, and can become 'insolvent'. Such a charity can be deemed insolvent either:

- when it is unable to pay its debts as they fall due; or
- when the value of its assets is less than the amount of its liabilities taking into account its possible and prospective liabilities.

These two tests have a legal basis for **charitable companies**, as they are aspects of the definition of inability to pay debts in s.123 of the Insolvency Act.

Unincorporated charities are not 'legal persons' and cannot technically incur liabilities, which are instead incurred by their trustees, acting on their behalf. Unincorporated charities cannot, therefore, technically become insolvent. However, a charity may reach the financial state where the value of the assets in the trust, which are available to the trustees to settle their liabilities, are insufficient. In the context of unincorporated charities 'insolvency' is used to describe this situation.

Permanent endowment means property of the charity (ie land, buildings, investments or cash) which the trustees may not spend as if it were income. It must be held permanently, sometimes to be used in furthering the charity's purposes, sometimes to produce an income for the charity. Trustees cannot normally expend permanent endowment without our authority.

Primary purpose trading is a trade exercised by a charity in the course of the actual carrying out of its primary purpose. The following are examples of what might be regarded as trading in this manner:

- The provision of educational services by a school or college in return for course fees.
- The provision of residential accommodation by a resident care charity in return for payment.
- A trade in which a primary purpose of the charity is carried out by beneficiaries.

Glossary of terms

Scheme. A Scheme is a legal document which amends, replaces or amplifies the trusts of a charity. It may be:

- a fully regulating Scheme which deals with all aspects of a charity's administration and becomes the governing document of the charity; or
- a non-regulating Scheme dealing with some particular aspect of the charity's purposes or administration by amending or amplifying the charity's governing document, or by authorising a particular action prohibited by the trusts of the charity.

Subsidiary trading company means any non-charitable trading company owned by one or more charities to carry out trading activities on behalf of the charity(ies) with a view to raising funds in a tax efficient manner.

Charity trustees are the people responsible under the charity's governing document for controlling the management and administration of the charity (s.97(1) of the 1993 Act). They may be called trustees, managing trustees, committee members, governors, or directors, or they may be referred to by some other title. In the case of an unincorporated association, the members of the executive or management committee are its charity trustees; in the case of a charitable company it is the directors.

Trustee board. We use the word 'board' to refer to a charity's governing body.

Unincorporated charity means a charitable trust (other than a CIF or a common deposit fund) or a charitable unincorporated association, and for present purposes includes any other charity whose property is held on a trust (eg a company incorporated by Royal Charter).

Must is used to refer to actions that trustees, or their agents or employees, are obliged to take by law.

Should is used to suggest actions which we consider to be good practice and which we expect trustees to follow.

Annex D - Resources for trustees

There are many resources which charity trustees can tap into to help them manage their organisation. Whilst this is not a definitive list of all the sources of information available it does offer a useful starting point. The publications listed in Annex E may also be useful.

Organisations

■ *The Charity Commission for England and Wales*

Further information can be obtained from the Commission:

- by visiting our website www.charitycommission.gov.uk;
- or by contacting Charity Commission Direct.

Telephone: 0845 300 0218

Typetalk: 0845 300 0219

Email: enquiries@charitycommission.gsi.gov.uk

Or write to:

Charity Commission Direct

PO Box 1227

Liverpool

L69 3UG

■ *Association of Chief Executives of Voluntary Organisations (acevo)*

acevo provides good practice resources and information on sector issues.

1 New Oxford Street

London

WC1A 1NY

Tel: 0845 345 8481

www.acevo.org.uk

■ *Association of Charitable Foundations (ACF)*

ACF promotes and supports the work of charitable grant-making trusts and foundations.

Central House

14 Upper Woburn Place

London

WC1H 0AE

Tel: 020 7255 4499

www.acf.org.uk

Resources for trustees

■ *Charities Aid Foundation (CAF)*

CAF helps non-profit organisations in the UK and overseas to increase, manage and administer their resources.

25 Kings Hill Avenue
Kings Hill
West Malling
Kent
ME19 4TA

Tel: 01732 520000
Website: www.cafonline.org

■ *Charity Finance Directors' Group (CFDG)*

CFDG provides information for its members and others on a range of issues and specialises in helping charities to manage their accounting, taxation, audit and other finance related functions. Benefits of membership include regular members' meetings, monthly mailings and access to information and services.

3rd Floor
Downstream Building
1 London Bridge
London
SE1 9BG

Tel: 0845 345 3192
E-mail: info@cfdg.org.uk
Website: www.cfdg.org.uk

■ *Directory of Social Change (DSC)*

The Directory promotes positive social change and provides a wide range of resources for trustees.

London
24 Stephenson Way
London
NW1 2DP

Liverpool
Federation House
Hope Street
Liverpool
L1 9BW

Tel (books): 08450 77 77 77
Tel (training and events): London 020 7391 4800 & Liverpool 0151 708 0117
Website: www.dsc.org.uk

Resources for trustees

■ *HM Revenue & Customs*

For information on tax issues relating to charities.

St John's House
Merton Road
Bootle
Merseyside
L69 9BB

Tel: 0845 010 9000
Website: www.hmrc.gov.uk

■ *Institute of Fundraising*

The Institute of Fundraising aims to promote the highest standards of fund-raising practice.

Park Place
12 Lawn Lane
London
SW8 1UD

Tel: 020 7840 1000
E-mail: enquiries@institute-of-fundraising.org.uk
Website: www.institute-of-fundraising.org.uk

■ *National Association for Voluntary Service and Community Action (NAVCA)*

The NAVCA network provides a wide range of information and support for charities through its local CVSs.

NAVCA
The Tower
2 Furnival Square
Sheffield
S1 4QL

Tel: 0114 278 6636
E-mail: navca@navca.org.uk
Website: www.navca.org.uk

Resources for trustees

■ *National Council for Voluntary Organisations (NCVO)*

NCVO provides information on fund-raising and governance issues and a range of general support services.

National Council for Voluntary Organisations
Regent's Wharf
8 All Saints Street
London
N1 9RL

Tel: 0800 279 8798
E-mail: helpdesk@askncvo.org.uk
Website: www.ncvo-vol.org.uk, www.askncvo.org.uk

■ *VolResource*

This internet only resource for charities offers quick links to useful organisations concerned with the effective running of charities.

E-mail: info@volresource.org.uk
Website: www.volresource.org.uk

■ *Wales Council for Voluntary Action (WCVA)*

WCVA supports charities and the voluntary sector in Wales.

Baltic House
Mount Stuart Square
Cardiff Bay
Cardiff
CF10 5FH

Tel: 029 2043 1700
Helpline: 0870 607 1666
E-mail: help@wcva.org.uk
Website: www.wcva.org.uk

Journals, magazines and newspapers

■ *Charity Finance*

3 Rectory Grove
London
SW4 0DX

Subscriptions - Tel: 020 7819 1204
E-mail: sshabiolegbe@charityfinance.co.uk
Website: www.charityfinance.co.uk

■ *Charities Management*

Subscriptions - Tel: 020 7729 6644

■ *Charity Times*

Subscriptions - Tel: 020 7426 0636
Website: www.charitytimes.com

■ *The Guardian/Society*

The *Society* section in Wednesday's edition of The Guardian is particularly relevant.

Website: www.SocietyGuardian.co.uk

■ *The Times/Public Agenda*

The Public Agenda section in Tuesday's edition of The Times is particularly relevant.

Website: www.timesonline.co.uk

■ *Third Sector*

Subscriptions - Tel: 020 8606 7500
E-mail: subscriptions@haynet.com
Website: www.thirdsector.co.uk

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Acknowledgements

We would like to thank everyone who has co-operated in the production of this report, especially the charities that gave their time to speak to our staff.

Special thanks also to Mike Hudson of Compass Partnership for his advice and support.