Private Client law

Briefing

MACFARLANES

An introduction to being a charity trustee

What is a charity trustee?

Charity trustees are the people who are legally responsible for the day-to-day management and decision-making in a charity.

Every charity has charity trustees, although not every charity is a trust. In the case of a charitable company, the charity trustees are its directors. In the case of an unincorporated association with charitable status, the charity trustees are the individuals who make up the governing body or council. Charitable Incorporated Organisations (CIOs)[1] will likewise have charity trustees when these entities are introduced.

Whilst being a charity trustee can be interesting and rewarding, it can also be challenging. It is important to be aware before taking it on of the responsibilities that accompany such a role. This note is intended to provide an overview of the duties of a charity trustee.

Who can be a charity trustee?

By law, you cannot be a charity trustee if you:

- have previously been removed as a charity trustee;
- have been disqualified from acting as a company director;
- have been convicted of an offence of dishonesty or deception; or
- are an undischarged bankrupt.

In addition, the charity's governing documents may impose restrictions on who may act.

Subject to these qualifications, you will be permitted to act provided that you are aged 16 or over (if the charity is a company) or aged 18 or over (for any other kind of charity).[2]

It is worth pointing out that no-one should take on the role unless they will have the time, motivation and abilities to discharge their duties as a trustee effectively. Involvement in the governance of a charity can require business acumen as well as commitment to the causes which the charity has been set up to further.

Duties of a charity trustee

Technically, the duties owed by a charity trustee differ slightly depending on the legal form of the charity (whether it is a trust, company, CIO, etc). However, in practice all charity trustees have the same fundamental responsibilities, known as fiduciary duties.

Generally, these duties are enforced by the Charity Commission, which has extensive powers to obtain information about charities and to investigate possible misconduct. Where misconduct is found, charity trustees can be sued for any loss incurred by the charity. They can also be removed from office and (in the case of criminal misconduct) prosecuted.

Charities may also be subject to investigation by HM Revenue & Customs. In certain situations (outlined below), HMRC has the power to deprive a charity of tax relief to which it would otherwise be entitled. Where tax has to be paid by a charity, and the charity trustees are to blame for this, they may be held to account by the Charity Commission (i.e. sued) for the liability incurred by the charity.

The core duties of charity trustees are as follows.

Promotion of charitable purposes

This is arguably the most fundamental of all duties of a charity trustee. He or she must ensure that the charity advances the charitable purposes set out in its governing documents and does not engage in activities which do not advance those purposes.

[1] For more information on these, see our note "The Charities Act 2006: saying ciao to CIOs".
[2] In fact, at the time of writing, you can be the director of a charitable company at any age. However, it is expected that the position will change in 2008 and that, from then on, any director of a charitable company will need to be at least 16.

If the charity's funds are expended on non-charitable activities, the charity trustees could be sued by the Charity Commission for breach of duty, and/or the charity could be deprived of valuable tax relief by HM Revenue & Customs.

It's important to note that administration, marketing and fund-raising aren't charitable activities, although in practice it is permissible for a modest proportion of the charity's funds to be expended on these items. The excessive use of charitable funds for non-charitable expenses such as administration and fund-raising is a common trigger for Commission investigations.

Best interests of the charity

Another fundamental duty of a charity trustee is to act in the best interests of the charity. Prior to the making of any decision, the charity trustees must consider the possible ramifications of the proposed course of action and whether, in the round, this course of action is likely to enhance the financial position of the charity and/or its ability to promote its charitable purposes effectively, both in the short term and over a longer timeframe.

This duty has application in a wide range of situations, including investment policy, commercial transactions and how the charity presents itself to the public. For example, before embarking on a controversial, shocking campaign on a particular topic, charity trustees should consider whether the advantages of this in terms of awareness-raising might be outweighed by longer-term damage to the charity's image or reputation.

Care and skill

The law imposes a duty of care on all charity trustees. They must exercise such care and skill as is reasonable in the circumstances, whenever they are making decisions in relation to the charity. If a trustee has any special knowledge or experience, or if his or her business or profession means that he or she can reasonably be expected to have special knowledge or experience, a higher standard of care and skill is expected.

If the trustees lack expertise in a particular field, they may be expected to obtain professional advice in order to fulfil their duties. As discussed below, this comes up particularly frequently in relation to the investment of a charity's funds.

Avoidance of conflicts of interest

Charity trustees must always regard the best interests of the charity as paramount and must not allow their personal interests to override this.

A personal interest in a particular transaction will always need to be disclosed, and generally a charity trustee with a personal interest will be disqualified from voting on the decision to enter into the transaction. He may even be required to leave the trustees' meeting. This depends to some extent on the charity's governing documents.

As a charity trustee, you will need to be alive at all times to the possibility that you might have a personal interest in a proposed transaction or some matter under consideration. Recently, some of the charity trustees of an august and famous institution suffered the very public ignominy of a Charity Commission investigation after they had paid scant attention to these rules.

Avoidance of personal benefits

As a general principle, a charity trustee is not permitted to benefit in any way from his charity; he will be expected to perform his role pro bono publico and without remuneration in any form.

However, there are exceptions to this. A charity trustee may receive remuneration for goods or services provided to or for the benefit of the charity if:

- this is authorised by the charity's governing documents; or
- the Charity Commission has sanctioned the receipt of remuneration.

It is very rare for a majority of the trustees of a charity to be remunerated on either basis.

Provisions contained in the Charities Act 2006 (expected to come into force in early 2008) will relax this position somewhat so that trustees can be remunerated even if the charity's governing documents do not explicitly allow it, and the consent of the Commission has not been obtained. However, this will be subject to strict conditions.[3]

In addition, recently enacted provisions of the Charities Act 2006 allow trustees to purchase personal indemnity insurance out of the charity's funds[4]. This is another exception to the general prohibition on charity trustees receiving any benefit from their charity.

Compliance with legal requirements

Charity trustees must ensure that they / the charity comply with:

- the provisions of the charity's governing documents;
- the general law of charities, as interpreted and enforced by the Charity Commission; and
- all other legal requirements which may apply to the charity, which will depend on its legal form and its activities.

The main statutory sources of charity law are the Charities Act 1993 and the Charities Act 2006. The Charities Act 1992 applies to charities that engage in fund-raising from the public. Case law continues to be relevant, for example in relation to the categories of charitable purposes.

Directors of corporate charities need to ensure that they comply with the Companies Act 2006[5] and also (to the extent that it is still in force) the Companies Act 1985.

In addition, there are many other areas of law which may have relevance to a charity, depending on the activities that it is undertaking. Examples are:

- employment law, where a charity has employees;
- health and safety law and disability legislation, where a charity has employees and/or has premises which are open to the public;
- landlord and tenant law, if the charity has land which is let as an investment (or indeed occupies land as a tenant); and
- child protection law, if the charity has involvement with children.

It is also worth noting that a charity engaging in fund-raising from the public will need to comply with detailed rules in the Charities Acts of 1992 and 2006, and that there are particular rules which a charity must comply with if it is proposing to sell or otherwise dispose of any land, as set out in the Charities Act 1993.

Professional advice should be obtained, where necessary, to ensure that the charity trustees are aware of all their compliance responsibilities. If in doubt, seek advice.

Specific areas of responsibility/ governance

Meetings and decision-making

Charity trustees should generally meet on a regular basis to make decisions, delegate tasks and formulate strategy and policies to ensure that the charity is advancing the purposes set out in its governing documents in the most effective way.

Requirements for meetings may be set out in the charity's governing documents. Under current law, any charitable company must hold an annual general meeting of its members (who are not necessarily the same people as the directors) on a broadly annual basis.

3 For more information, see our note "The Charities Act 2006: the big picture for the third sector".
4 This is subject to certain conditions. For more information, see the section of this note entitled "Liabilities of charity trustees".
5 For more information on this, see our note "Charities caught in the Act: the Companies Act 2006 and the implications for the third sector".

Charity trustees are collectively responsible for any decisions which are made, and all decisions should be made collectively. However, decisions need not be unanimous; a majority decision should suffice (unless the governing documents state otherwise).

Charity trustees are free to delegate powers to others (subject to any restrictions set out in the governing documents of the charity). However, they will always bear ultimate responsibility for actions taken by such delegates on behalf of the charity.

Accounting and reporting

A further duty of charity trustees is to ensure that they comply with the statutory requirements for the preparation of accounts and the filing of accounts and annual returns. The details of these requirements are beyond the scope of this note.[6]

Trustees of unincorporated charities (trusts, unincorporated associations) only need to comply with the requirements in relation to accounts and returns in the Charities Act 1993. However, directors of charitable companies also need to comply with companies legislation, and filings need to be made to Companies House as well as the Charity Commission.

If a charity's annual income is over £10,000, an annual return needs to be submitted to the Charity Commission. This provides the charity trustees with an opportunity to summarise the main activities and achievements of the charity and to explain how the charity's money has been raised and spent that year.

It is worth noting that the reporting burden for many charity trustees is likely to get weightier when the new rules on public benefit (contained in the Charities Act 2006) are brought into force. Trustees will be expected to include information in annual returns explaining how the charity has been providing a benefit to the public. Of course, some charities already go to some lengths to show in their annual returns and other publications that public benefit is being provided.

Financial management

Regardless of a charity's size, good financial management will be crucial to its success and its ability to pursue its charitable purposes. The charity trustees must ensure that:

- the charity remains solvent (i.e. has positive net assets, taking all liabilities into account, and is able to pay its debts as they fall due);
- cash flow is managed carefully and the charity has funds available to cover contingencies (for example, a humanitarian charity should have funds which it can access immediately in the event of sudden disaster);
- appropriate arrangements are in place for the custody and control of the charity's assets, to protect against fraud or other loss (for example, only charity trustees and trusted employees should be able to procure payments from the charity's bank account, and payments above a certain amount should require multiple signatures);
- appropriate arrangements are made for the protection of any physical assets of the charity (for example, buildings should be fully insured against all normal risks);
- risks faced by the charity are covered where cover can be obtained at a reasonable cost (insurance may be obtained to cover employee fraud, potential liability to visitors to the charity's premises, potential liability for medical negligence, etc.); and
- all investments of the charity are suitable (see below).

All of these requirements are simply an extension of a charity trustee's duty of care and duty to act in the best interests of the charity.

[6] But see the Charity Commission publication "Charity accounts: the framework 2007". This is available from the Commission's website.

Investments

Money not needed for expenditure in the near term should be invested. The aim is to secure the best possible return on the charity's assets without subjecting those assets to undue risk.

Charity trustees who are proposing to purchase a particular investment should ensure that the governing documents of the charity provide a power to do so. If an investment of a particular type is not expressly authorised by the governing documents, it may, if the charity is a trust or unincorporated association, be authorised by the Trustee Act 2000. Where trustees are in doubt about their investment powers they should seek advice.

The Trustee Act 2000 sets out quite detailed rules on the selection and review of investments. Strictly speaking, these rules do not apply to charitable companies. However, the Charity Commission takes the view that such rules should be followed by all charity trustees, who may be breaching their fiduciary duties if they disregard them.

Charity trustees must consider which types of investment are most suitable for the charity, bearing in mind their risk/return characteristics, and should have regard to the need for diversification of investments, so far as is appropriate for the charity. In addition, they must review the charity's investments periodically to ensure that they remain suitable for the charity's needs.

There is a duty to obtain advice when selecting new investments and reviewing current ones, unless it is reasonable in all the circumstances not to do so. Normally it is necessary to obtain advice from an investment professional (e.g. an independent financial advisor). However, a non-professional with knowledge and practical experience of financial matters may be consulted by the charity trustees instead, where this is appropriate. There may be such an individual among the charity trustees, who is willing to give advice to the trustees as a whole. Any such individual should note the risk of personal liability if his advice gives rise to loss for the charity and he is considered to have been negligent in giving it.

Given these obligations, charity trustees may wish to hand responsibility for selection of the charity's investments to an investment manager with a discretionary mandate (so that decisions to buy and sell are taken by the manager, not the trustees). They should check that they have a power to do this under the governing documents of the charity.

Under the Trustee Act 2000, trustees of a charitable trust are only permitted to give a manager a discretionary mandate if they have prepared a written policy statement giving the manager guidance on the exercise of its functions. This should be reviewed periodically and revised where necessary (for example, if the charity's financial position changes significantly). In relation to a charitable company, the preparation of a policy statement is, at least, best practice.

Even if the charity trustees wish to make investment decisions themselves, it is recommended that they draw up an investment policy, for their own benefit, considering the charity's needs as to both income and capital in the short, medium and long term, and how these needs will be satisfied by the charity's portfolio.

One last, obvious point on this topic: invest in haste and you may rue at leisure. It is important that all investment decisions are taken with care, and that the charity trustees' thought processes are summarised in minutes of the trustee meeting, which can be relied on later to show that there was a rationale for a particular investment decision.

Payments to other organisations

One of the most fundamental duties of a charity trustee is to ensure that the charity's funds are applied for the purposes set out in its governing document (and are not expended for other purposes). Therefore, as a general rule, a charity can only make a grant to another organisation if the grant will be used by that organisation for the purposes of the charity.

This applies to grants to other charities as well as grants to non-charitable organisations. So, for example, a charity established for the relief of financial hardship cannot make a grant to another charity if the other charity's purposes do not include the relief of financial hardship. In addition, if the other charity has a variety of charitable purposes, one of which is the relief of financial hardship, a payment can be made to that charity only if it is subject to a condition that requires it to be used solely for relieving financial hardship.

It is important to note that a non-UK organisation cannot be a charity for the purposes of English law, even if it is considered charitable under the law of the country in which it is registered or based. It follows that if the trustees of a charity wish to make grants to a non-UK organisation, they must take appropriate steps to ensure that the grants will be applied for purposes which are charitable under English law (and within the charitable purposes of the charity), even if the organisation is registered as a charity where it is based.

In this scenario, a funding agreement should be entered into between the charity and the overseas organisation. Such an agreement should stipulate the purpose(s) for which the proposed payment must be used and should impose reporting obligations on the receiving organisation, i.e. obligations to provide the charity with accounts, receipts and other evidence that the payment has been used solely for the stipulated purpose(s). The agreement should also include clawback provisions so that, in the event of a breach by the recipient organisation, the charity will be able to demand immediate repayment of the grant (and will be entitled to withhold further funding).

If the trustees are ever in doubt whether or not they have authority to make a particular payment, the Charity Commission has a power, under section 29 of the Charities Act 1993, to give formal advice. If the trustees act in accordance with that advice, they will be protected from personal liability for breach of trust in relation to that particular action.

Avoidance of tax

Some charity trustees are slightly shocked to learn that they are under a duty to avoid tax.

However, this follows from their duty to act in the best interests of the charity. Tax liabilities incurred by a charity will of course reduce the funds available to be used for charitable purposes. The Charity Commission confirm this duty in some of their publications – and that they may seek to hold charity trustees to account (i.e. sue them) where tax liabilities have been incurred unnecessarily because of mismanagement by the trustees.

Generally, charities pay no income tax, capital gains tax or corporation tax. However, tax liabilities may be incurred by a charity if:

- the charity purchases an investment which is not authorised by the income tax legislation (although this is not always strictly enforced);
- the charity makes a payment to a non-UK body without taking reasonable steps to ensure that the payment will be used for charitable purposes;
- the charity enters into a transaction with a substantial donor (unless there is an exemption under the substantial donor rules);[7]
- the charity receives income from a trade which is not carried out in pursuance of its charitable purposes (such income will not usually be exempt from tax);[8] or

[7] See our note "Charities and Trojan horses: an introduction to the 2006 substantial donor rules".
[8] See our note "A complicated business: charities and trading".

- the charity enters into a transaction concerned with the purchase or sale of land for the purpose of development.

This list is not exhaustive.

It goes without saying (or should do) that, while there is an obligation to avoid tax for the charity where possible, there is also an obligation to ensure that any tax liabilities incurred by the charity are disclosed to HM Revenue & Customs and duly paid.

Liabilities of charity trustees

Liability to third parties

Most charities need to enter into contracts with third parties in order to carry out their work. Whether or not the trustees are personally responsible for liabilities arising under the terms of a contract depends on whether the charity is incorporated (a charitable company or CIO) or unincorporated (a trust or unincorporated association).

A corporate charity is a legal entity in its own right and so third parties are able to contract with the charity itself rather than the trustees. This means that, provided the contracts are entered into with proper authorisation, the trustees are not personally liable under them.

On the other hand, since trusts and unincorporated associations have no independent legal personality, it is the individual trustees rather than the charity who are party to any contracts made on behalf of the charity. As a result, the charity trustees are personally responsible for the obligations which arise under these contracts. However, provided that they act properly in entering into the contract, the trustees are entitled to use the charity's assets to meet these obligations.

It is of course possible that an unincorporated charity will have insufficient resources to cover liabilities incurred by the trustees. In such a case, they may find themselves personally liable even though they have acted perfectly properly. Therefore, it is quite common for trustees to purchase insurance out of the charity's funds against liabilities to third parties incurred in the running of the charity. Technically, this is a different type of insurance to trustee indemnity insurance (discussed below).

Liability for breach of trust

If a charity trustee breaches any of the duties and responsibilities described earlier and the charity suffers loss because of such breach, he or she may be personally responsible for the loss.

However, the Charity Commission has power to relieve charity trustees from such liability if it considers that they have acted honestly and reasonably and ought fairly to be excused.

In addition, charity trustees are generally allowed to purchase indemnity insurance to protect themselves if a breach of trust claim is made against them. The Charities Act 2006 has recently given charity trustees a statutory power to pay for such insurance out of charity funds, whether or not express permission is given in the governing documents of the charity, subject to certain conditions.[9]

It is worth noting that trustee exemption clauses contained in trust deeds can validly exempt the trustees of charitable trusts from liability for breaches of trust unless the trustee acts dishonestly. However, the directors of a charitable company cannot be exempted in this way, and this should be taken into consideration when choosing the legal form for a charity.

So you still want to be a charity trustee?

To be a charity trustee requires time, understanding and effort. It was said in a 1747 case that a trust is an office "attended with no small degree of trouble and anxiety. It is an act of great kindness in anyone to accept it". The judge in that case wasn't referring to a charitable trust, but the statement was and remains true of trusteeship of any charity.

[9] The charity trustees cannot purchase insurance out of charity funds if this is expressly prohibited by the charity's governing documents (although these can be amended with the consent of the Charity Commission) or if it is not in the best interests of the charity to do so. In addition, charity trustees cannot purchase indemnity insurance using the funds of the charity if the terms of the policy are such that the trustees would be protected from the consequences of their own fraud or recklessness.

Anyone considering becoming a charity trustee should consider carefully whether they will have the time and energy required to fulfil all the duties and responsibilities demanded by the role. A passive trustee, or one with too little time to devote to his position, could in a worst case scenario find himself personally liable for loss caused to the charity through his own negligence or that of his fellow trustees.

However, a committed, conscientious and energetic charity trustee should not be too concerned about personal liability. His participation in the affairs of charity will, no doubt, constitute “an act of great kindness” but it should also be personally rewarding.

Contact details

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