

Good Governance. A Guide

Section One. Introduction and background

1.1 What is Governance?

Definitions of the term 'governance'

- The art or skill of managing an organisation - from Tessi Akpeki, (NCVO).
- To govern ...to rule with authority ... to regulate proceedings of (corporation, etc) - from Oxford Handy Dictionary.
- The act or manner of governing - from The Concise Oxford Dictionary, 9th Edition. The dictionary explains that the word 'governance' developed from a Greek word 'kuberna' which means to steer.
- Governance - a useful term for distinguishing between the day to day management from governing a voluntary organisation, ie ensuring the organisation has clear objectives, priorities, an agreed programme of work, leadership, safeguards for its money and other assets, supervision for paid workers, and the capacity to manage its work within the law ... - from *Faith and hope don't run charities (trustees do)*, published by the Wales Council for Voluntary Action, 1999.
- Internal control is a process, effected by an entity's board of directors, management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:
 - Effectiveness and efficiency of operations
 - Reliability of financial reporting
 - Compliance with applicable laws and regulations...

From the Committee of Sponsoring Organisations of the Treadway Commission, a voluntary private sector organisation dedicated to improving the quality of financial reporting through business ethics, effective internal controls and corporate governance.

1.2 How did governance issues arise?

Professor John Taylor (an expert on management) says concerns about governance originated in the worlds of politics and business¹. During the 1970s and 1980s, he says, there were many debates about standards of conduct among Members of Parliament,

¹Professor John Taylor, Glasgow Caledonian University speaking at SCVO's 1999 conference on governance *'The fish rots from the head'*

local authorities, and 'captains of industry'. There was growing public opinion that corrupt individuals were causing all the problems and therefore laws and regulations should be tightened to deal with such individuals.

In the 1990s people were genuinely shocked by revelations about sleaze in politics, and scandals involving powerful business-people such as Robert Maxwell. At the same time concepts such as ethical capitalism were beginning to develop, as exemplified by businesses such as the Body Shop.

The debate continued to develop over time and the language used also changed. Now there is talk of governance not just in political life but in public bodies, and in the voluntary and community sector. As time went on, people realised that solutions based on new or tougher laws to deal with corrupt individuals were difficult to operate, often failed to stamp out problems, and even created new ones.

It is now believed that tougher laws or new regulations are not always the answer to problems of corruption and mismanagement (though they are sometimes the answer). Now the challenge is to try to set up organisational structures with in-built checks and balances that prevent individuals from contemplating wrong-doing.

That is basically what good governance and good internal control are about - putting in place systems and practices that encourage and help people to 'do the right thing'.

The governance debate resulted in a lot of research and study by experts. Special committees were set up by government and others to investigate the problems and to suggest solutions.

Key governance issues in England and Wales

- The *Report of the Nolan Committee* into standards in public life
- The *Deakin Commission* on the future of the voluntary sector
- The *Cadbury Report*
- Reports on governance in the UK voluntary housing sector
- The World Bank's *Handbook on Good Practices for Laws Relating to NGOs* drafted by The International Centre for Not-for-Profit Law

Charity law in England and Wales was updated and tightened in 1992, partly in response to some of the problems highlighted by the governance debate

Key governance issues in Scotland

- *Faith and Hope in Charity?* – a report by the Scottish Council for Voluntary Organisations (SCVO) called for charity regulation to be strengthened.

Charity law in Scotland was strengthened in 1995 and at time of printing is under review by the Scottish Assembly.

1.3 Governance issues in Northern Ireland - NICVA's Millennium Debate

NICVA, through the Millennium Debate, wanted to ensure that the issue of governance would be carefully examined in Northern Ireland. A series of round-table discussions was held as part of the Debate and Tesse Akpeki of the Trustee Unit at NCVO and Derek Alcorn of the Northern Ireland Association of Citizens Advice Bureaux contributed papers to a one day conference on governance in 1997. This guide would not have been possible without the input of Tesse, Derek and all the individual board members, volunteers and employees who contributed their ideas and experiences to the governance strand of the Millennium Debate.

At the governance conference and seminars, both Tesse and Derek explained how a look back at the voluntary and community sector (both here and in England) during the 1990s shows why governance became a key issue. The 1990s were a rapidly changing environment in many sectors. There was considerable pressure on voluntary organisations to become more business-like. This often conflicted with some of the core values of the voluntary and community sector - humanitarianism, caring, idealism. At the same time, there were increasing pressures on voluntary organisations to meet ever-increasing social needs. This put a great strain on the resources of the sector, both material and human.

At the conference, Tesse Akpeki argued convincingly that voluntary sector boards are under-developed resources. They have the potential to be powerful forces for leadership and change in society, but do not always fulfil their full potential. This is not the case in all voluntary and community organisations, but it is a serious concern. If boards are under-developed, unbalanced and ineffective, then how will new volunteers be attracted to join voluntary and community sector organisations and serve as board members in the future? This is a concern to the sector as a whole. Tesse suggested some possible reasons why board development may be hindered:

- Low expectations (internally and externally)
- The difficulties of recruiting a competent and balanced (ie representative) board
- Lack of clear awareness of board members' responsibilities
- Poor board/staff relations

Tesse Akpeki predicted that as the voluntary sector continues to expand, it will significantly increase its contribution to society. However, if the sector is to continue having the support and participation of the public, its organisations must develop methods of strengthening internal controls and good practice. NICVA's Millennium Debate provided a significant platform on which to begin to explore how voluntary sector boards can be developed in a proactive programme to shape the future of the voluntary sector.

1.4 The debate on governance and charity regulation in Ireland

In the Republic of Ireland

- The Costello Report into Fundraising Law and Practice and Charity (1990) - this report of a Committee set up by the Irish Government examined the framework of charity regulation and its inadequacies, especially in terms of regulating charity fundraising activities and safeguarding public confidence in charities.
- Insights into the Boards of Irish Voluntary Agencies - Report on a questionnaire survey by Gwen Jaffro, School of Business Studies, Trinity College, Dublin².

In Northern Ireland

The Department of Health and Social Services (now known as the Department for Social Development) produced a White Paper on Charity Law in Northern Ireland which was published for consultation in late 1995 and early 1996. The main proposals of the 1995 White Paper were:

- To set up a simple register of charities for Northern Ireland
- A sliding scale of accounting regulations for charities
- Some additional regulations for professional fundraisers
- An updating of the law on charitable collections

The outcome of the consultation was that the proposed law reforms were postponed due to a change of government and a failure of the outgoing government to prioritise charity law reform in Northern Ireland.

1.5 Key governance issues in Northern Ireland

In his paper, *Governance and Democracy in Charities* (1997), Derek Alcorn³ cites the powerful impact of the so-called 'contract culture' that has left its mark on the voluntary sector in Northern Ireland.

Derek Alcorn identified some of the problems the contract culture has led to as:

- Distortion or drift of an organisation's mission
- A muzzling of the advocacy role of some organisations
- A shift of responsibility from voluntary board members to professional staff

² published in *Administration*, the journal of the Institute of Public Administration, Dublin, November/December 1998

³ Director of NIACAB, contributor to NICVA's Millennium Debate on governance.

Derek Alcorn pointed out that, at the same time, the *Report of the Nolan Committee into Standards in Public Life*, the *Deakin Commission on the Future of the Voluntary Sector*, the *Cadbury Report*, and reports on governance in the voluntary housing sector, led to greater awareness of the issue of conflict of interest, among others.

Other phenomena that have influenced the development of the Northern Ireland voluntary and community sector include:

- 30 years of violence and sectarianism
- Censorship (within communities) and 'political vetting' of community groups by government
- The peace process
- The European Peace funding that followed

As well as universal governance issues, there are possibly governance issues arising in Northern Ireland-based organisations which are directly linked to the conflict and its effects on organisations and individuals. In many ways the voluntary and community sector has been at the leading edge of promoting progressive change in Northern Ireland. Organisations, particularly the small community-based organisations, have operated in circumstances that have been and continue to be very challenging, to alleviate needs and to change society for the better.

The environment that voluntary and community sector organisations work in will continue to change, and the sector as a whole will have to develop new methods to encourage and promote good practice and good governance. This guide is only one small stage in the process of promoting good governance within the Northern Ireland voluntary and community sector, and perhaps there needs to be some in-depth research into issues of governance in our voluntary and community sector.

1.6 Is governance just red tape and bureaucracy?

Good governance is not about throwing rule books at people, or creating a lot of written documents that people will never read. Good practice models, rules, regulations, policies and procedures are useful tools for governance and good practice. But they are only effective if they are straightforward, sensible, clear and agreed by all.

Good governance is not about using jargon or waffle to intimidate people. It is about being truthful, sharing skills and knowledge and, ultimately, empowering people. Mostly, good governance is just a matter of commonsense and doing the right thing.

¹Professor John Taylor, Glasgow Caledonian University speaking at SCVO's 1999 conference on governance 'The fish rots from the head'

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³Director of NIACAB, contributor to NICVA's Millennium debate on governance

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Section Two. Choosing an appropriate legal structure

2.1 Why should you think about legal structures?

When a group of people get together to carry out a particular activity, they may not give much thought to the legal nature of the group they are forming. They tend to act together to carry out a task without realising that they may have created obligations and responsibilities in law to each other.

The legal nature of a group usually becomes an issue when the group decides to write down some form of rules for the group (usually in response to a request from a grant-making body) or in the course of seeking charitable status.

There are several legal structures to choose from. Groups should choose the structure which most suits their present needs and the needs they can envisage for the future, as the group develops. Four of the most commonly used structures are discussed in this section.

Each of the four structures discussed below could be used by a group carrying out charitable activities and this guide is designed for such charitable voluntary groups.

The charitable nature of a group is determined by the objects for which it is established and the activities it carries out (see section 3 of this resource pack for further information).

Once a group has considered the four options below, it may adapt a structure to both suit the group and to satisfy the Inland Revenue's requirements as a charitable group.

There are advantages and disadvantages to each structure and these should be considered carefully. In some cases one aspect of the structure is an advantage to one group. Yet the same aspect may be seen as a disadvantage by another group. The four alternatives described below should be studied with the present and future needs of your group in mind.

2.2 Unincorporated bodies (trusts and associations)

Trust

This is the traditional structure for a charity and many older charities are trusts. A trust is governed by a trust deed which sets out the objects of the trust, names the trustees and provides for the administration of the trust. A trust is usually established by an individual or a group wishing to settle their own property or specific property on charitable trusts.

Advantages of a trust:

- (i) Continuity - when a trust is established, the trustees are usually chosen by the founder or founder group setting up the trust. Trusts do not have a membership. Trustees are not elected, and usually remain in office until they retire or die, although some trusts are less rigid in their structure, eg by providing for the trustees to stand down after a fixed period. When new trustees are needed, they are appointed by the existing trustees.

This can be a disadvantage where a trustee is for some reason unsuitable or has behaved improperly and is not willing to retire voluntarily. If there is no power to remove a trustee in the trust deed, an application may have to be made to court to remove him or her. It is unlikely, however, that the court will take any action unless the trustee's actions have caused the administration of the trust to deteriorate to such an extent as to damage the interests of the charity.

On the other hand, as trustees are independent (not answerable to any body of members), they may act as they consider right, provided they follow the provisions of their trust deed (the governing document of a trust).

The self-perpetuating nature of a trust ensures a certain type of continuity. It also attempts to ensure that people acceptable to the original founder/s will be appointed as trustees in the future. This continuity may help to reduce disputes about how the trust should be run in the future

- (ii) Confidentiality - the deliberations of trustees are usually private. Trustees are answerable for their conduct only to the courts. They need not give reasons for the way they have exercised their discretion. They need not disclose any documents or details of their deliberations. If they act outside the terms of the trust deed, they can be taken to court in an action for breach of their trust, otherwise their decisions cannot be questioned.

Again, this point may be considered a disadvantage by groups which desire to be open and accountable. Some trusts wish to be open and accountable and will call an annual meeting which is open to the public, and will publish an annual report in the interests of good practice.

- (iii) Cost - there is no charge to set up and run a trust. The Charity Advice Service can assist with drafting a trust deed, but groups are advised to have the draft trust deed approved by a solicitor before using it. A trust need not be expensive to run. There are no annual fees to be paid (as there are in companies) and there is no requirement that accounts be audited, though it could be argued that all but the smallest trusts should have their accounts audited annually in the interests of good practice

- (iv) Certainty - the nature and scope of a trustee's duties are well established in law, so if problems are encountered, there are well established guidelines for the trustees to consult and follow

Disadvantages of a trust

- (i) Inflexibility - a trust deed can only be altered by a court order and only then in certain circumstances. If trustees consider that the objects for which the trust was set up are now outdated, they must apply to court for consent to alter the deed. However, if the trust deed is carefully drafted in the beginning, this objection can be avoided. It is possible to make sure that the deed contains the power to vary the administrative powers of the trust and that the objects clause is drafted as widely as possible. If this is the case, there should be no need to go to court to have the deed altered
- (ii) Personal Liability - a trust is an unincorporated type of structure, so trustees do not have the advantage of limited liability. Trustees, like the members of any unincorporated group, are responsible for contracts entered into on behalf of the trust or actions against the trust. If these contracts are not honoured, or if the trust is sued, it will be the individual trustees who must pay the debt or who may be sued. The trustees are entitled to be indemnified by the trust, ie they can reclaim any monies rightfully due from the trust's bank account. A problem arises when there is not adequate money in the trust's account. In such a situation, the trustees would be personally liable to meet the obligations of the trust

Insurance will cover many potential liabilities and the funds of the trust may be sufficient to cover any debts or obligations which arise, but where these are insufficient, the trustees are at risk. Trustees must, therefore, ensure that the activities of the trust are carefully supervised and that there is adequate control of all financial matters

- (iii) Transfer of assets to new appointees - when new trustees are appointed or when old trustees retire, the property of the trust will have to be transferred into new names. This may involve trouble and expense, particularly where the old trustees have lost touch with the activities of the group and can no longer be reached
- (i) Restriction on the trustees' powers of delegation - it is a general principle of trust law that a trustee cannot delegate the performance of his/her duties to others. A majority of trustees in a charitable trust can make decisions and would usually delegate the day to day administration of the charity to paid staff, especially where there is a large number of trustees or where meetings are held infrequently.

Please note that at the time of this guide going to print, a piece of legislation called the Trustee Bill is under consideration at the Northern Ireland Assembly. If it becomes law, the Trustee Bill will (among other things) define the types of functions that charity trustees can delegate. It will also allow all trustees to take

advantage of a full range of investment opportunities and will make access to professional advice and expertise easier. The legislation also aims to set out a clear 'statutory duty of care' for trustees in carrying out a range of functions

- (v) Lack of control by members - a trust is composed of the trustees. It does not have members. Trustees are not accountable to anyone for their decisions and are only answerable to the courts for their actions. If the charity envisages a membership organisation which has effective democratic involvement and control over the actions of an accountable management group, the trust structure is not suitable and the structure of a company or an unincorporated association may be more appropriate

Membership association

This is the most common form of structure for voluntary organisations. The association exists where a group of people join together to carry out an agreed object (otherwise than for profit) and where it is intended that there should be some provision for continuing membership and the future existence of the group.

The association is governed by a set of rules (called a constitution) which sets out the objects of the association, its membership and structure, and the powers it gives itself to carry out its objects. The association is composed of members who delegate their power to a management board to carry out the association's activities. The management board is accountable to and elected by the members.

Advantages of an association

- (i) Flexibility - the constitution of the association can be tailored to fit the varying types of association. The association is free from the statutory controls which govern the limited company
- (ii) Cost - an unincorporated association is cheap to set up and run. The Charity Advice Service can help any group with its constitution

Disadvantages of an association

- (i) No separate legal identity - an association has no separate legal existence apart from the members of which it is comprised. The constitution is the legal document which governs the association. It forms a contract between the members and establishes the rights and duties they have to each other. Within the association the members and the management group act as a group of individuals and the group has no separate legal status. This means that the association cannot own property or enter into contracts in its own name. These responsibilities must be carried out by individuals within the association, or outsiders who agree to hold property on behalf of the association (holding trustees)

- (ii) Holding Trustees - as the association cannot own property, provision must be made for individuals to be appointed as trustees to hold the assets of the association in accordance with a written deed of trust. Frequently, the association does not formally appoint trustees, and property (eg land leases or equipment) is bought in the name of officers or board members. These individuals may be acting as holding trustees without any clear definition of the trusts on which they hold the property. Problems can arise where trust property continues to be vested in individuals, whether formally appointed as trustees or not, who are no longer connected with the running of the charity or where the association has become defunct
- (iii) Personal Liability - the management board of an association may incur personal liability. If, for example, a contract authorised by the management board is entered into and the charity's funds are inadequate to pay for the services rendered by a third party under the contract, the individual members of the board would be personally liable to make good the debt. If an officer of the association incurs liability in the course of his/her work for the charity but has acted properly (not negligently) and within the terms of the constitution and the authority conferred upon him/her, he/she will be entitled to be reimbursed (indemnified) from the association's funds. The indemnity clause in a group's constitution states this 'right of indemnity' clearly

It is important that the management board of an association should ensure that they comply with the constitution, take reasonable care in dealing with the charity's affairs, only enter into commitments if sufficient funds are available, and ensure that competent agents and employees are employed. Procedures should be put in place to minimise risks occurring and insurance should be taken out to cover any foreseeable risks.

2.3 Incorporated bodies (companies and industrial and provident societies)

Company limited by guarantee

A company is constituted by its memorandum and articles of association which are normally drawn up by a solicitor. A company limited by guarantee is the usual form of limited company found in the voluntary sector. A minimum of two members is required to set up a company.

Advantages of a company limited by guarantee

- (i) Flexibility - there is power in the Companies (NI) Order 1986 to alter both the objects of a company and the regulations which govern administrative matters. However, a charitable company must ensure that no alteration is made to its memorandum or articles of association which would cause it to cease to be a charity at law

- (ii) Corporate identity - a company is, in the eyes of the law, like a person. It is therefore capable of owning property in its own name and of taking or defending actions in court. As it can own property, etc, in its own name, there is no need to appoint holding trustees to hold the property of the charity
- (iii) Limited liability - the company is a legal person and its debts and contracts belong to the company itself and not to its members. A member of a company is not personally liable if the company is sued or owes money. (It is important that the directors or management board of the company are members.) The liability of members in the event of the company being unable to meet its obligations or debts and going bankrupt, is limited to the amount that he/she guarantees when becoming a member. This amount is usually £1.00

Members of the company are protected by this limited liability of the company in respect of contracts they enter into on behalf of the company, but it is important that they make it clear to third parties that they are entering into a contract on behalf of a company, and not in their own name.

This limited liability is important where the charity is considering borrowing large sums of money, buying land or buildings, or employing staff who might create liabilities for the charity by acting outside the practical control of the person responsible for overseeing staff.

Please note that the protection from liability is not absolute. If an officer or director acts negligently, or not in the best interests of the company, or while disqualified, etc, they may not be able to avoid personal liability.

It is also worth noting that limited liability does not always provide protection, as banks and lending institutions or landlords may require a personal guarantee from directors before they are willing to lend money or lease property to a charitable company. Businesses or suppliers entering into contracts with the company may also insist on the individual directors entering into any transaction as individuals and not as company directors

- (iv) Involvement of members - the company is inherently a democratic structure where the members have ultimate control over those managing the company. Directors are answerable to the members for the conduct of the company's affairs and may be removed from office by a resolution of the company's members. New members can join the company and can also be expelled from the company without undue formality
- (v) Continuity - until it is wound up, a company has perpetual succession, ie it continues to exist, even though its members may change, die or cease to be involved in the activities of the company. While winding up the company is a complex business, it may be necessary if the purpose for which the company was originally formed is no longer applicable, or if the company becomes insolvent

Disadvantages of a company limited by guarantee

- (i) Cost - it costs money to set up and run a company. The articles and memorandum of association (the governing document of a company) is usually drafted by a solicitor and there is a registration fee of £35.00 to be paid when a company is registered at the Registrar of Companies. Annual accounts and an annual return must be submitted to the Registrar of Companies. There is an annual fee of £20 for filing returns
- (ii) Lack of privacy - there is a statutory requirement to inform the Registrar of Companies of any changes in directors. Company documents are available for public inspection. This is an advantage for organisations which desire to be open and accountable in their activities
- (iii) Bureaucracy - companies must comply with the statutory requirements of the Companies Orders. These set out detailed rules governing change of objects, rights of members, meetings, etc. A company may consider it to be worthwhile employing someone who is familiar with these requirements as the Company Secretary to ensure that these formalities are complied with. For example, the law requires that the name of a company must appear on all its literature

The limited liability offered by the company structure may not be required by charities which after all seldom get involved in quasi-commercial activity where limited liability is important. However, where groups are considering taking on employees or borrowing large sums of money, then the advantages of the company structure may outweigh the disadvantages. In most other cases those responsible for the activities of the charity may protect themselves against most hazards by insurance.

Companies must have the following information on all business letters and order forms:

- The company's place of registration and its company registration number
- The address of its registered office
- Where a company has permission to omit the word 'limited' from its title, the fact that it is a limited company must be stated on letter headings and order forms

Companies which are also charities and which do not have the word 'charity' or 'charitable' in their title, must state the fact that they are charitable on all business letters, notices, official publications, bills of exchange, promissory notes, endorsements, cheques, orders, conveyances, invoices, receipts and letters of credit.

Charities or voluntary groups which are companies must comply with company law. For further information, see Part Two, Section 7 of this guide, *Notes on Companies*.

Industrial and provident society (IPS)

An IPS is a society carrying on an industry, business or trade for the benefit of the community. It must also be either a co-operative society or a business conducted or intended to be conducted for the benefit of the community. An IPS usually tends to be a bona fide co-operative society which is democratically run and which ploughs profits back into the society. A minimum of seven members is required to set up an IPS. An IPS is set up by the adoption of model rules or rules drawn up by the group itself. Registering an IPS is quite expensive, especially if model IPS rules are not used.

It is possible for an IPS (with charitable objects) to be formally recognised as a charity.

Advantages of an industrial and provident society

- (i) Incorporation - an IPS is an incorporated group with the same advantages of the company structure mentioned above, ie corporate identity, limited liability, continuity and involvement of members. The rules of the IPS are not as flexible as the rules of the limited company
- (ii) Arbitration - the Registrar of Friendly Societies may arbitrate when disputes arise

Disadvantages of an industrial and provident society

- (i) Cost - the rules of the IPS are submitted to the Registrar of Friendly Societies who will register the IPS on payment of a fee. The fee is £115.00 where model rules are used, or £380.00 where the group draws up its own rules. It takes longer to register the IPS with the Registry than it takes to register a limited company
- (ii) Lack of privacy - in common with the company structure, the IPS is subject to public scrutiny as annual returns are made to the Registrar
- (iii) Charitable status - as an IPS is defined as a 'society carrying on an industry, business or trade', it is unlikely to be compatible with the requirements of charity law, which prohibit a charity from trading. In addition, a bona fide co-operative is run for the benefit of its members which is in direct opposition to the charitable principle that charities benefit the public. However, some Industrial and Provident Societies, notably housing associations, are deemed to be charitable

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Section Three. Notes on seeking charitable status

The word charity comes from the Latin word *Caritas* meaning 'care' and charitable status is a privilege which the government confers on certain voluntary groups which can demonstrate that they are driven by a certain type of altruism or caring.

In return charitable groups have to conform to certain strict conditions (which are established in charity law and the law on trust). In the case of Northern Ireland-based groups, the body that can formally confirm whether a group is a charity or not, is the Inland Revenue. The Revenue has a special office in Bootle, Merseyside, which makes such decisions.

3.1 Advantages and disadvantages of charitable status

Advantages

The advantages of charitable status are mainly financial and include:

- Relief from Capital Transfer Tax
- Relief from Capital Gains Tax
- Relief from Stamp Duty
- Probable 100% rates relief on premises
- Recovery of Income Tax on donations from taxpayers through tax-efficient schemes (eg NICVA's Taxplus Schemes)
- Only charitable organisations are, strictly speaking, eligible to receive grants from charitable grant-making trusts
- Easier access to charitable appeals on radio and television
- The general public usually has more confidence in a body which is formally recognised as charitable

Disadvantages

Though desired by most groups, charitable status is not suitable for every voluntary group. Some groups prefer to be non-charitable - perhaps because the group wishes to avoid the restrictions or disadvantages of charitable status. In such cases, advice should be sought from the Charity Advice Service if a group wishes to establish a not-for-profit non-charitable association. That is a sort of voluntary group which is set up for the benefit of the community, without actually being a charity. Some of the disadvantages of charitable status include the following:

- A charity must confine its objects and activities to those which are charitable in law

- A charity cannot carry on permanent trading activities unless the trade is exercised in the course of carrying out a primary purpose of the charity, or the work in connection with the trade is mainly carried out by the beneficiaries of the charity
- A charity cannot have 'political objects', although a charity can quite properly seek to influence opinion on particular issues which are directly relevant to its objects and experience
- Charity trustees (those on the board of a charity) can never be paid for acting as a trustee, nor can they be remunerated for work that they do in a professional capacity for the charity (eg providing training and receiving a fee for it). Only solicitors or accountants who are charity trustees may be paid for legal or accountancy work which they are asked to do on behalf of their charity. There are a few exceptions to this rule, and advice should be sought by any charity contemplating allowing its trustees to be remunerated. Unless there are very good reasons for this, and strict checks and balances built in, the Inland Revenue will not agree to this

3.2 How are decisions on charitable status made?

In Northern Ireland, the Inland Revenue is the body which can decide if an organisation is capable of being considered a charity for tax purposes. (In the South of Ireland it is the Revenue Commissioners who make such decisions.) The Inland Revenue bases its decisions on charity law.

3.3 The four heads of charity

The law says that only the following purposes are charitable, provided they are carried out for the public benefit:

- (i) The advancement of education
- (ii) The promotion of religion
- (iii) The relief of poverty
- (iv) Other purposes beneficial to the community

This last phrase does not, however, mean all other purposes beneficial to the community, as some activities, which undoubtedly benefit the community, are not charitable.

3.4 Examples of objects and activities which are charitable in law under heading 3.3 (iv) above

- (i) The protection and preservation of health (including the relief of aged and disabled persons); the protection of the natural environment
- (ii) The provision of facilities for recreation or other leisure time occupation, if the facilities are provided in the interests of social welfare, ie the facilities are provided with the object of improving the conditions of life for the persons for whom they are intended, and either:

- Those people have need of such facilities by reason of their youth, age, infirmity or disablement, poverty or social or economic circumstances
 - The facilities are to be available to the public or female members of the public at large
- (iii) *"The relief of unemployment for the public benefit in such ways as may be thought fit, including assistance to find employment"* is now considered a legally charitable object for the first time since the Charity Commission Review of the Register project in 1999 examined the case for such an object to be considered charitable
- (iv) *"The promotion of community capacity building"* is now considered a legally charitable object as an outcome of the Charity Commission's Review of the Register project. In order to be charitable, this type of object must be directed at geographical areas of need where deprivation is evident, or at non-geographical communities in which people share a common experience of deprivation
- (v) Also as an outcome of the Review of the Register project, the *"promotion of urban and/or rural regeneration in areas of social and economic deprivation (and in particular [specify an area]) by the following means:*
- *The relief of poverty*
 - *The relief of unemployment*
 - *The advancement of education, training or retraining particularly among unemployed people, and providing unemployed people with work experience*
 - *The provision of financial assistance, business advice or consultancy in order to provide training and employment opportunities for unemployed people in cases of financial or other charitable need through help in setting up their own businesses, or to existing businesses*
 - *The creation of training and employment opportunities by the provision of workspace, buildings, and/or land for use on favourable terms*
 - *The provision of housing for those who are in conditions of need and the improvement of housing in the public sector or in charitable ownership provided that such power shall not extend to relieving any local authorities or other bodies of a statutory duty to provide housing*
 - *The maintenance, improvement or provision of public amenities*
 - *The preservation of buildings or sites of historic or architectural importance.*
 - *The provision of recreational facilities for the public at large or those who by reason of their youth, age, infirmity or disablement, poverty or social and economic circumstances, have need of such facilities*
 - *The protection or conservation of the environment*
 - *The provision of public health facilities and childcare*
 - *The promotion of public safety and the prevention of crime*
 - *Such other means as may from time to time be determined by the Charity Commissioners of England and Wales."*

3.5 Examples of objects which are not charitable in law

- (i) Promotion of peace or reconciliation between different communities or nations
- (ii) Campaigning or pressurising government whether local or national
- (iii) Political objects such as pressurising government or civil servants to change laws, policy or administrative decisions

So, if your group wishes to pursue the activities in (e), (f), or (g), it will not get charitable status. If its activities are a mixture of charitable and non-charitable activities, it will not get charitable status, since the law says that a charity must have exclusively charitable purposes.

Note on the Charity Commission's Review of the Register project - at the time of going to print, it was not possible for this guide to describe all of the changes in policy resulting from the Review of the Register, because the Review is not yet complete. NICVA's Charity Advice Officer will be happy to provide information and advice on the Review and its implications.

When decisions are made (by the Inland Revenue) about individual Northern Ireland groups having such objects, the Revenue will require detailed information about the proposed activities of the applicant group. In particular, the group will have to show that the area they are operating in is deprived, that the public will benefit from the group's work, and any benefit to individuals is incidental to the public benefit of the project which must be the top priority.

3.6 Activities must be consistent with objects

The governing document, or constitution, of a charity should set out good charitable objects, ie those which comply with the headings (i)-(iv) set out in sub-section 3.3.

In addition, a charity must limit its activities to those which further its charitable objects and must not undertake any activities which are not allowed, such as unlawful campaigning or carrying on a permanent trade.

When a group is considering whether it is eligible to become a charity, it must consider both the objects it has written down in its constitution and the activities which it undertakes to carry out those objects.

3.7 Umbrella bodies and networks seeking charitable status

Networks or umbrella bodies often have had difficulty securing charitable status because often their work is indirect (eg influencing policy decisions). Networks wishing to be charities have to show the Inland Revenue that either:

- The network is directly pursuing charitable objects or
- The network has a primary charitable object such as advancing education

If you are not sure whether your group is likely to be considered to be charitable by the Inland Revenue, contact NICVA for advice. If your group is interested in being recognised as a charity, the following step by step guide will explain exactly what you will have to do.

Becoming a charity in Northern Ireland

As stated already, the Inland Revenue is the body which can confirm if a group in Northern Ireland is accepted as a charity for tax purposes or not.

Step One

The officers of the new group which wishes to be a charity should send a copy of its constitution (or its draft constitution), plus a summary describing the practical activities the group intends to pursue, to:

HM Inspector of Taxes
Inland Revenue
FICO (Trusts and Charities)
St John's House, Room 380C
Merton Road
Bootle
Merseyside L69 9BB

The letter to the Inland Revenue, accompanying your group's constitution should include the following:

"I would be grateful if you could confirm whether the above association/group may be recognised as a charity under the provisions of the Income and Corporation Taxes Act 1988.

I enclose a copy of the group's constitution and a summary describing the practical work of the group and its future plans."

Step Two

If the Inland Revenue has looked at a group's constitution or its draft constitution and requires some further information, or has questions about the group's activities, the group should reply to the Revenue answering any such queries, or perhaps providing documentary evidence such as press clippings or leaflets which illustrate the practical activities or work of the group.

Step Three

If the Inland Revenue formally recognises (in a letter) that a group is capable of being a charity, if it adopts the constitution draft shown to the Revenue, the group should take care to adopt the Inland Revenue approved constitution at an Annual General Meeting of the members or at a Special General Meeting of the members. The adoption should be recorded in the minutes of the meeting. The Charity Advice Service recommends that you also keep a record of the date of adoption of the constitution in a space provided in the actual constitution itself. A copy of the adopted constitution, showing the date of adoption, should be sent to the Inland Revenue as soon as it is available. The Revenue will then confirm that the group is considered a charity for tax purposes.

Step Four

Once a letter has been received from the Inland Revenue formally confirming that a group is considered a charity for tax purposes, the charity may quote the reference number shown on the Revenue's letter to indicate that the group is indeed recognised as a charity for tax purposes (note, however, that this number is not a 'registered charity number', it is an 'Inland Revenue reference number').

Charities may quote their Inland Revenue reference number on letter headings, flyers, etc. Company law requires that charitable companies must state that they are a charity and quote their Inland Revenue reference number on all correspondence, letter headings, compliment slips, bills, invoices, flyers and posters.

Step Five

A charity which has received an Inland Revenue letter confirming that it is a charity for tax purposes must not assume that it need never bother about charitable status from then on. In order to retain its charitable status, a group must always be aware of the restrictions of charitable status (eg restrictions on certain types of trading, and on 'political' activities) and must observe them at all times.

Furthermore, a group must be prepared to submit its annual accounts to the Inland Revenue (FICO) if required. This is because the Inland Revenue must be satisfied that the group's income is applied only to charitable purposes. Northern Ireland's charity legislation¹ clearly states that a charity must keep accounts and must preserve them for at least seven years.

Further Reading on the Topic of Charitable Status

So You Want To Be a Charity? by Bill McStay, NICVA, 1987 (to be re-issued in 2001).

¹ The *Charities Act (N.I.) 1964*

Northern Ireland Charities - A Guide for Trustees, available free of charge from the Voluntary Activity Unit (Charities Branch), Department for Social Development, 5th Floor, Churchill House, Victoria Square, Belfast BT1 4SD, tel: 028 9052 0500.

Charities, Trading and The Law, by Stephen Lloyd, published by the Charities Advisory Trust in association with the Directory of Social Change, 24 Stephenson Way, London, NW1 2DP, tel: 0207 209 5151.

The Charity Shops Handbook by Hilary Blume, published by the Charities Advisory Trust, Radius Works, Back Lane, London NW3 1HL.

Charitable Status: A Practical Handbook by Andrew Phillips, published by InterChange Books, 15 Wilkin Street, London NW5 3NG, 1988, price £7.95.

The Charity Commission publishes a range of guidance notes on charitable status on its website www.charity-commission.gov.uk

For advice and information on charitable status, contact:

Charity Advice Service
NICVA
61 Duncairn Gardens
Belfast BT15 2GB

Tel: 028 9087 7777
Email: brid.mckernon@nicva.org

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Section Four. Notes on board duties, roles and procedures

4.1 Why have a board?

The rules of an organisation are usually set out in a written governing document (usually a constitution). The constitution is the source document from which the board and its powers are derived.

The constitution of an organisation usually states

- The objects or purposes of the organisation. That is what it is established for
- Who is eligible to apply to become a member of the organisation
- The rights of the members of the organisation (eg the right to vote)
- How the organisation's board of management is to be selected
- How and when General Meetings of the whole membership may be called, and what business is to be conducted at Annual General Meetings
- How the organisation's finances are to be controlled
- How the constitution can be altered
- How the organisation might be dissolved

A constitution normally recognises:

- That it's not practical for all the members of a group to run that group (except perhaps in a very small group)
- That the members' powers are, therefore, delegated to a board made up of some members, and that the board acts in the name of and on behalf of all the members
- That some powers are not delegated to a board, but are retained by the whole membership, eg election of a board, altering the constitution, deciding to dissolve the organisation
- That the board is answerable to the members meeting together at an Annual or Special General Meeting

A board may be called simply 'the board' or it may have another title as laid down in the constitution, such as:

- Board of Trustees
- Executive Council
- Executive Board
- Management Board

- Central Board
- Management Board
- Board of Directors (the 'board' of a charitable company may be called 'the directors')

4.2 Responsibilities (and rights) of board members

You are a member of a board. Here is a list of the things that are expected of you (and what you are entitled to expect):

- Attend regularly - send an apology if you can't
- Find out if the board has rules/regulations - are these written down in your group?
- Participate in decisions - don't be shy
- Carry out any tasks you agree to take on - say beforehand if you are unable or unwilling
- Offer to lead if you have special skills
- Understand your legal responsibilities, especially in regard to:
 - Employment of paid staff, legal and good practice requirements regarding child protection and protecting any vulnerable people
 - Health and Safety regulations
 - Protecting against liability, and having adequate insurance
 - Monitoring finances (if insolvency results, you may be personally liable)
- Be loyal to the board - respect confidentiality
- Remember you are accountable to the membership as a whole

You have rights to match your responsibilities:

- The right to correct information
- The right to be heard
- The right to be consulted
- The right to respect and loyalty from colleagues

4.3 Roles of office bearers

(i) Honorary officers

Honorary officers (or office-bearers) are unpaid people acting in a voluntary capacity, as distinct from the employees of the organisation, who are sometimes called 'the officers'. The key members of a board are:

- The Chairperson (also called Chairman, Chairperson or Moderator)
- The Honorary Secretary (or just Secretary)
- The Honorary Treasurer (or just Treasurer)

In larger groups it may be helpful if these office-bearers have deputies, eg Assistant Treasurer. A board may have other titles for the office-bearers, such as Minutes Secretary, Press Officer, etc

(ii) Election of officers

The constitution will say whether office-bearers:

- Are elected at and by an Annual General Meeting.
- Are elected by and from among the members of the elected board.

4.4 Roles of the office-bearers of a board

The Role of the Chairperson is:

- To ensure the agenda and minutes are prepared
- To ensure that the agenda is followed
- To ensure everyone has a chance to speak
- To keep speakers to the point
- To promote fairness and to resist the opportunity to put own opinion first
- To sum up discussion preparatory to decision
- To strive for consensus - use voting as a last resort
- To ensure tasks allocated are carried out
- To speak for group publicly, unless otherwise agreed

The Role of the Secretary is:

- To prepare venue and arrive early
- To prepare agenda and minutes
- To record decisions of meeting clearly and briefly
- To ensure the Chair is fully briefed
- To handle and file all correspondence
- To order stationery supplies, etc
- To prepare an annual report for board approval, and then submission to the Annual General Meeting

The role of the Treasurer is:

- To open a bank account for the group
- To keep records of all income and expenses
- To give or obtain receipts for all income and expenses
- To lodge all monies (except for a small cash float) in the bank
- To report state of finances at all meetings, and to invite questions
- To ensure the organisation's annual accounts are audited, or at least are examined by an independent person (ie someone not connected with the group)
- To prepare the annual statement of accounts for approval by the board first, and then for submission to the Annual General Meeting
- To preserve the accounts for at least seven years

4.5 The relationship of paid employees and the board

In all charities, employees are prohibited from being members of the board (and board members from being employees) unless the constitution provides otherwise (and the Inland Revenue approves of this provision). Where the prohibition applies, a member of the board who becomes employed by a charity, even for a short time, must resign.

Some organisations state in the constitution that employee representatives can attend and have a full voice in board meetings. If so, there should be a clear policy for situations where a conflict of interest arises, eg conditions of employment affecting the member of staff present at the meeting. Employee representatives in this kind of situation should declare an interest and withdraw from that part of the meeting.

Any board member who is likely to become employed by the charity or who is applying for a job, or might apply for a job with the organisation should not take part in discussions or decisions about the job description, person specification or terms of employment, etc.

4.6 Remuneration of board members of a charity

Board members of a charity (charity trustees) can never be paid a wage or rewarded for acting as trustees. Charity law requires trustees not to profit from his/her trust, so charity trustees cannot receive remuneration even though the time they devote to serving as a trustee may be significant. Trustees are entitled to claim out of pocket expenses incurred in the course of their work on the charity's behalf.

4.7 Remuneration for specific services provided to a charity by a board member

Remuneration for services involves being paid for work done for the organisation, whether as an employee or on a self-employed basis. Many payments of this kind which are seen as 'payment for expenses' are in fact remuneration and must be treated as such.

Ordinary members of an organisation - those who are not members of the board - may be paid by the organisation unless this is prohibited by the governing document of the organisation.

Charity law requires trustees to act altruistically - not to profit from his/her trust, so charity trustees cannot receive remuneration unless the constitution of the charity allows it. It is very rare that the Inland Revenue will accept a group as a charity for tax purposes if the group's constitution allows payments to be made to the board.

In some cases, if there are very strong reasons for permitting some of the trustees to be paid for services, the Inland Revenue may accept the necessity for including a rule in the constitution to allow this, or for amending the constitution to include such a rule. However, even then, the Revenue would expect to see firm checks and balances in place to prevent the trustees from exploiting this situation to the detriment of the charity or its beneficiaries.

At the time of going to print, the Trustee Bill - a proposed piece of legislation which aims to clarify the circumstances in which Northern Ireland charity trustees could be remunerated - is being considered by the NI Assembly.

Section five: planning and running meetings

5.1 Procedures at meetings

The experience of people who have been on voluntary boards suggests that an agreed and understood procedure for meetings will contribute to the board's efficiency and effectiveness.

Who to invite to the meeting

Membership associations can get confused about the difference between a 'board meeting' and a 'General Meeting'. It is important to know the difference because all of the members of an association must be invited to a General Meeting.

The members do not have to be individually notified of a meeting, but steps must be taken to ensure that they have a fair chance to get to hear about the meeting, eg posters in a prominent place can be adequate, or flyers advertising the meeting.

Many voluntary groups find that a special set of rules for board meetings are helpful. Such rules are often called 'Standing Orders'. A set of model Standing Orders is set out in Appendix 1 of this guide, but remember they are for guidance only. Your board can draw up its own Standing Orders or ground rules for meetings. When they are drawn up, they should not be changed from meeting to meeting.

In general, meetings will be more efficient and effective when members:

- Study the minutes of the last meeting and the agenda for the forthcoming meeting before and not at the actual meeting
- Arrive in good time for the meeting
- Don't discuss business at the meeting except through the Chair
- Follow the guidance and abide by the rulings of the Chair

5.2 Model agenda for a board meeting

The agenda of a meeting is the list of items which should be discussed at the meeting. A typical agenda includes the following items:

- Apologies
- Chair's business (any special announcements about matters not otherwise on the agenda)
- Minutes of last meeting (a written record of decisions taken which requires members to agree its accuracy)
- Matters arising from the minutes (if not otherwise on the agenda)

- Reports from the Secretary, Treasurer, Staff, Sub-Committees, etc
- Items of main business (eg new premises, fundraising events)
- Any other business
- Date, time and venue of next meeting

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Section Six. Charity trustees' responsibilities in Northern Ireland

At the time of going to print, the powers and duties of trustees in Northern Ireland are governed by the Trustee Act (Northern Ireland) 1958, the Trustee Investments Act 1961, the Trustee (Amendment) Act (Northern Ireland) 1962 and the common law. The governing documents of charitable trusts is the primary source of powers and modern, well drafted trust documents often confer wider powers than statute or common law, but if a governing document lacks the wider powers, then statute and common law come into play.

The Office of Law Reform (NI) produced a consultation paper in August 2000 which aimed to update Northern Ireland's trust laws to allow all trustees to take advantage of a wider spectrum of powers. If the proposed changes go ahead, all trustees will be able to enjoy the wider powers of investment currently practised by those with modern, well drafted governing documents. Additionally, there will be new powers to appoint agents, nominees and custodians, to insure trust property, to pay professional trustees, and to appoint and replace trustees.

There will be also be a new statutory duty of care which will clarify the current standard duty which has developed out of case law. That is the principle that a trustee must take care of his/her charity affairs as 'an ordinary prudent business person' would take care of his/her own business affairs and a higher duty of care for paid or professional trustees.

6.1 What is a charity trustee?

There is no definition in the Charities Act (NI) 1964 but usually the people who have the 'general control and management of the administration of a charity' are the trustees, whether they are aware of it or not, and regardless of what name they are called.

The term charity trustee includes not only a trustee of a charitable trust, but also the directors of charitable companies and the members of management boards of charitable unincorporated associations.

6.2 Who can become a charity trustee?

Anyone may become a trustee provided they are over eighteen and are not disqualified under the Companies (NI) Orders if the charity is incorporated. Certain charities may require additional qualifications, for example, a charity working across the religious divide may require a balance of different religious believers among its trustees.

Usually the power to appoint someone as a charity trustee lies within the governing document of the charity. In an association or a company, the management board or

directors will usually be elected. A trust will be established by its trustees who will have the power to appoint a new trustee.

A trustee should be chosen for the qualities they can bring to the position, eg interest in the work of the charity, willingness to give the required time and effort to the charity's work and organisational ability.

A trustee takes on legal responsibilities and could incur personal liabilities. Organisations should consider training or job descriptions for trustees as no trustee should be appointed who does not appreciate the nature of the position they are taking on.

Trustees should read a copy of the governing instrument, should ensure they have details of the charity's property and how it is held, as well as copies of recent minutes and accounts so that they are aware of the charity's current financial and general activities.

6.3 Powers of trustees

As stated in the introduction, trustees' powers are derived from trust law, common law and from the governing document of their charity (for example, its trust deed, its constitution or its articles and memorandum if the charity is a company).

Trustees' powers include the following:

Land

Trustees of a charity have the power to sell, exchange or mortgage and otherwise deal with land. Where a mortgage is concerned, the trustees should obtain written advice from a person with ability and practical experience in such matters. That person can be an employee or officer of the charity although they must not have any personal interest in the mortgaging arrangements. The advice must cover such points as whether the loan is necessary to enable the charity to carry out a particular project, whether the terms are reasonable and whether it would be possible for the charity to repay the loan on the proposed terms.

Investments

Charity trustees have a duty to promote the interests of the charity and should seek to maximise investment. They must maintain a balance between the interests of present and potential beneficiaries and avoid high risk investment.

The standard of care required is that of an ordinary prudent business person investing for people for whom they feel morally obliged to provide. In practical terms, the trustees should obtain written advice from experts, whether agents or surveyors in relation to land, or stockbrokers in relation to stocks and shares.

6.4 Duties of charity trustees

In general terms, the duty of a charity trustee is to promote the interests of the charity and to ensure that its assets are applied for the charitable purposes authorised by its governing instrument and for no other purpose.

The trustees must ensure that the charity's income is spent solely for the charitable purposes set out in the charity's governing instrument. They must make appropriate distributions with absolute fairness between those persons qualified to benefit under the terms of the charity. Income should not normally be accumulated without good reason.

Trustees should never allow their activities to overstep the terms of their charitable objects. Trustees should be aware, for example, of the distinction between education and propaganda and should confine any 'political' activities to those which are 'reasonable' and which educate the public and the decision-makers about their own beneficiaries.

Trustees should also be aware that the responsibility for the management and organisation of the charity and for its decisions lies with them. Charities may employ officers and give them a high degree of responsibility, but the ultimate responsibility lies with the trustees and they have a duty not to delegate this. Trustees must establish proper administrative controls and make themselves aware of how the charity is run on a day to day basis.

In certain circumstances, a trustee can be held personally liable, where the fault lies not with the trustee but in the activities of a co-trustee, for example, if a trustee has unquestioningly allowed his/her co-trustee to deal with charity property in a way which has resulted in a loss to the trust fund.

Obviously, larger charities must have employees, and trustees themselves cannot personally handle every document or every day to day administrative arrangement. What the trustees must ensure is that proper systems are in place so that the conduct of the charity's business is subject to sufficient checks to avoid the problems outlined above. Many of the precautions are straightforward such as the requirement that charity bank accounts are drawn by two signatories or that the charity's finances should never be allowed to be solely in the hands of a single person.

Trustees have a responsibility to ensure that their charity maintains adequate insurance cover. Cover is required for a wide range of items including: the property of the charity (such as land, building, plant, furniture, computers and should cover structure, contents and consequential loss); cash on the premises or in transit; its liabilities to employees, volunteers and the public; motor insurance; and insurance for fundraising or special events.

6.5 Remuneration and charity trustees

Generally a charity trustee should act without payment although in exceptional circumstances a constitution may authorise payment to a trustee or, alternatively, allow an employee to be a trustee.

Trustees are entitled to be reimbursed for their out of pocket expenses such as postage, stationery, telephone calls, and travelling expenses. Unless the governing instrument contains an authority for such charges, a charity trustee engaged to supply goods and services to the charity by their co-trustees should not make a profit at the expense of the charity. The goods and services should be provided free of charge or below cost.

6.6 Potential liabilities and penalties

Trustees can incur personal liability in the course of their work for a charity. The exact circumstances when personal liability will be incurred depend to some extent upon the legal structure of the charity itself, ie whether it is a trust, company or an unincorporated association. In general terms, a charitable company offers more protection to trustees (its directors) in dealing with third parties, eg in relation to contracts for goods and services provided to the charity, than a trust or an unincorporated association. Note that the protection offered by incorporation is more limited than is often supposed (see Charity Advice Service pamphlet - *Notes on Charitable Companies*).

Examples of situations where trustees could find themselves personally liable for breach of their charitable trust and could be called upon to make up a loss to the charity and account for any profits include the following:

- Where the trustees act outside the authority given by the charity's governing instrument, for instance, by making speculative investments or distributing charity assets to those not within the definition of the charity's beneficiaries
- Where the trustees do not exercise proper care in carrying out their duties
- Where the trustees benefit personally from the charity, ie by furthering their own interests rather than those of the charity by arranging an indirect benefit to themselves
- The use of a charity's assets by the trustees for their own purposes

In addition, the trustees often enter into personally binding legal obligations. Examples include:

- When a trustee enters into a lease or a contract without specifically limiting the liability of that trustee to the assets of the charity
- When a trustee acting as employer fails in his/her statutory obligations
- When a trustee personally guarantees a loan on behalf of a charity

6.7 How can charity trustees protect themselves from personal liability?

Where trustees are uncertain about any decision affecting the charity, they can apply to the Charities Branch of the Voluntary Activity Unit, Department for Social Development, 5th Floor, Churchill House, Belfast BT1 4SD, for written advice. Action taken in accordance with this advice is protected against any accusation of breach of trust.

Where a trustee is in doubt about the activities of their co-trustees, they should discuss this or seek advice from the Charities Branch. They can be held responsible as noted above. They should not retire in the knowledge that a breach of trust may be about to take place as they may be held equally responsible with the trustees who actually commit the breach. However, if the trustee has acted honestly, reasonably and in good faith, he/she will have any liabilities incurred met out of the charity's assets.

If the trustee does not act honestly, reasonably and in good faith, they may be in breach of trust and personally liable to make good any loss to the charity. What is reasonable in the circumstances will be different in each case.

6.8 Trustee indemnity insurance

There is an increasing trend to seek insurance to indemnify individuals against liabilities they incur in acting as trustee of their charities. This is insurance which is in addition to property, employers, public liability insurance, etc.

A typical trustee indemnity policy covers losses incurred by the trustees in relation to breach of duty, breach of trust, breach of warranty of authority, negligence, error or omission and making misleading statements. An illegal act cannot be insured against and it could be argued that the only way in which the trustees do not act honestly, reasonably and in good faith, is when they are deliberately negligent or fraudulent.

If a charity wishes to use charity funds to take out insurance to protect the trustees from personal liability, it will need the power to do so in its governing instrument. The areas of risk should be identified, the amount of cover assessed and this should be balanced with the number of trustees and the size of premium quoted.

If the risk of incurring liabilities justifies taking out insurance, ensure that the cover includes:

- insurance against breaches of trust made as a result of honest mistakes
- protection in respect of claims for wrongful advice or information (professional indemnity insurance)
- insurance to protect the charity against fraud or dishonesty by employees or trustees

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Section Seven. Charitable companies

7.1 A limited company

(i) Legal identity

A company has a 'legal personality' separate from the individual people who are involved in the company. This means a company can own property in its own name, can enter into contracts, can sue and can be sued, in its own name. This is convenient because normally there is no need for individual people (acting as 'holding trustees') to hold any property in their own names, or to enter contracts, etc, on behalf of their organisation. Unincorporated organisations (ie any organisation that is not a company) must make arrangements for property to be held by individual people, who hold such property in their names on behalf of the unincorporated organisation.

A company is like a person in the eyes of the law. That means that the directors of a company are not normally held personally liable if the company becomes insolvent. The company - legally 'a person' in its own right - is responsible for its own debts and liabilities. However, company directors must bear in mind that if they give personal guarantees to a lender or in respect of any contract, they would be held personally liable. Usually the directors of a charitable company are simply called 'the board'.

A company may be perceived as more professional than a simple unincorporated association. The corporate structure is well known in the business sector. Some funders may be more willing to give a grant to a company than to an unincorporated body.

The law governing companies is clearer and more detailed than that applying to unincorporated associations.

(ii) Limited liability

The members of the company are not normally legally responsible for its debts beyond the amount they have guaranteed, usually a nominal amount eg £1.

(i) Democratic structure

Members have rights and responsibilities and can elect directors. Directors have powers and responsibilities under the Companies (NI) Orders 1986-1990.

7.2 Disadvantages of setting up a limited company

(i) Cost

The cost of setting up a company is higher than the cost of setting up an unincorporated body. A solicitor would charge a fee for drafting the Memorandum and Articles of Association - the 'governing document' of a company - and for advice about establishing the company. There is a registration fee of £30 when registering the company at Companies House.

There are ongoing costs of money and time in administration of the company once the company is up and running. For example, there is an annual fee of £20 for making annual returns to the Registry of Companies (ie details of the company's directors, Secretary and official address). Dissolving a company also involves time and expense.

(ii) Bureaucracy

The Companies (NI) Orders 1986-1990 are the legislation which regulates companies in Northern Ireland. The need to comply with company law could be a burdensome responsibility on members of a voluntary management board. Most voluntary organisations incorporate when they secure funding and are able to pay workers with the time and know how to ensure that company administration is dealt with efficiently.

(iii) Public accountability

Companies' details are stored on the Company Register which is open to the public. For a small fee anyone can look up details about an individual company. This is really an advantage in most cases - it assists those voluntary organisations which believe in openness and accountability to the general public.

(ii) An annual audit is normally required by the registry of companies

Accounts must be kept in accordance with the Companies (NI) Orders 1986 and 1990 and will include a balance sheet and profit and loss account for each financial year of the company, giving a true and fair view of the company's affairs, profits and losses.

Until 1995 all companies' accounts had to be audited by a company 'auditor', ie a member of a recognised supervisory body. A relaxation of company law regulations in May 1995 means that small companies may now choose not to have their accounts audited. A small charitable company can claim exemption from audit if its gross income does not exceed £90,000 per annum. A small charitable company with income greater than £90,000 but less than £250,000 per annum

may deliver unaudited accounts with an accountant's report. For companies having income greater than £250,000 per annum, accounts must be audited.

Accounts (whether audited or not audited) must be returned to Companies House each year on time. Fines may be levied against a company and its directors, if a company is late filing its annual accounts with the Registry of Companies.

7.3 Rights and responsibilities of company directors

A director's rights include:

- The right to be notified and attend meetings
- The right to vote at meetings
- The right to inspect the company's books, etc
- The right to be paid reasonable expenses (a director of a charitable company cannot receive payment or loans)

A director's duties include:

- Duty to use 'reasonable skill and care' in the management of the company's business
- Duty not to act beyond the scope of the objects of the company, or outside the powers in the articles and memorandum. The management board must ensure that all decisions are within the scope of the objects and powers of the articles and memorandum of the company, and that proper resolutions are passed
- Duty to draw up proper accounts annually (and generally have the accounts audited before returning them to the registrar)
- Duty to present a written annual report giving a fair review of the development of the company. This will include the names of the directors that year, describe the company's principle activities, any changes in those activities or in its assets, and planned future developments
- Duty to act honestly
- Duty to act in good faith, ie the law sets out a number of duties to act in good faith (called 'fiduciary' duties) which directors owe to their company
- Directors must act in the interest of the members of the company generally and to have regard to the interests of its employees
- Directors must not use their power for own personal benefit or personal gain
- A director must tell the management board of any direct or indirect personal interest in any contract or transaction (this includes when a person connected with the director stands to benefit)

Directors of charitable companies have additional duties (arising from trust law and charity law) which include:

- Duty to exercise powers in a 'prudent and business-like way'
- Duty to act honestly and in good faith in all dealings

- Not to benefit personally
- To act personally, although some delegation allowed
- To ensure numbers are sufficient
- To take joint decisions with other directors
- To take proper financial advice when investing charity's funds

7.4 Company directors' potential liabilities

Company directors are not normally held personally liable if their company becomes insolvent, but they may be held personally liable if:

(i) Negligent

If a director fails in his/her 'duty of care', this may be considered to be negligence. The standard of skill expected of a director is the standard of skill which could reasonably be expected from a person with that director's knowledge and experience, ie it is relevant to that person's knowledge and skill. Failure to take reasonable care is negligence.

Examples of negligence:

- Signing a cheque or authorising a payment without asking why a payment is being made
- Discovering that another director has been dishonest or negligent but not reporting this to the members of the company
- Allowing one director to take complete control without the proper authorisation

(ii) Guilty of fraudulent trading

A director could be personally responsible for the debts of his/her company if he/she 'traded fraudulently'.

Examples of fraudulent trading:

- Carrying on business with the intention of defrauding the company's creditors
- Carrying on operating with the intention of defrauding another person's creditors
- Any other fraudulent purpose

A director found guilty of fraudulent trading could be personally liable to make such contributions as the court thinks proper in the circumstances.

(iii) Found guilty of wrongful trading

Under the Insolvency (NI) Order 1989 a director may be personally liable if the company has gone into insolvent liquidation and he/she had carried on business after he/she knew or ought to have known that the company was heading for insolvency.

Note - in company law, the term 'director' includes a 'shadow director', that is 'a person in accordance with whose directions or instructions' the directors of a company are accustomed to act.

The court can order a director found guilty of wrongful trading to repay money and property or contribute such sum as the court thinks is just.

(iv) Acting in breach of statutory or fiduciary duty

Failures to comply with company law often result in criminal offences, even for innocent technical mistakes. These are usually punishable by fines which can range from hundreds of pounds for minor offences to fines of thousands of pounds for serious offences, or even imprisonment. Companies House will normally warn directors if they are consistently failing to comply with the Companies Order.

The law sets out a number of duties to act in good faith (called 'fiduciary' duties) which directors owe to their company.

(iii) Acting 'ultra vires' (ie acting beyond the scope of the objects of the company)

Where this happens and a company suffers loss as a result, the directors may be held personally liable, unless their actions were ratified afterwards by Special Resolutions of the company's members or if the actions were found to be acts to fulfil a previous legal obligation of the company.

(vi) Acting in breach of the charitable objects:

This is failing to ensure that the money or property of a charitable company was disposed of only in furtherance of the charitable objects of the charity.

(vii) Acting when an individual was disqualified from acting as a company director

The courts can disqualify individuals from acting as a company director. This is done by a 'Disqualification Order'.

The Companies Order does not place an age restriction on who can become a director of a private company, but it is almost certain that a minor (person aged under eighteen) cannot be a company director.

7.5 Different types of companies

There are four types of company - the first three described below are 'private companies'.

(i) Private company limited by shares

This is the most common type of company in the commercial sector. The members own shares in the company and the members' liability towards the company is 'limited' to the amount unpaid on shares held by them. This enables the commercial company to invite persons to subscribe to the company by purchasing shares which are only partially paid, enabling the company at a later stage to call for further funds from its members to the maximum of the unpaid amount. (One or more persons may form such a company by subscribing to the memorandum of association.)

(ii) Private unlimited (share) company

There is no limit on the members' liability. (Two or more persons may form such a company by subscribing to the memorandum of association¹.)

(iii) Private company limited by guarantee

This is the most common type of company in the voluntary sector. The members' liability is limited to the amount they have promised to contribute to the company's assets if it is wound up - usually a nominal sum such as £1. (One or more persons may form such a company by subscribing to the memorandum of association.)

(iv) Public company

The members' liability is limited to the amount unpaid on shares held by them, and which must have an authorised share capital of at least £50,000 at the time of incorporation. (Two or more persons may form such a company by subscribing to the memorandum of association).

7.6 Off the shelf companies

These can be bought from a 'company registration agent', a 'company formation agent', a solicitor or an accountant. Off the shelf companies are nearly always limited by shares rather than by guarantee so care should be taken to get the right sort of structure if an off the shelf company is purchased.

Registration agents keep their fees low by providing a basic service. They give little or no advice - the purchaser is expected to understand exactly what they want and specify it. Also the purchaser is expected to find out themselves the duties of company directors.

¹ Article 12 of the Companies (Northern Ireland) Order 1986

An off the shelf company may be useful if there is a need for great speed in setting up a company, eg in order to sign a lease. The company name can later be changed and the memorandum and articles of association can be amended. But in the meantime, the organisation may be operating a totally inappropriate type of company (eg non-charitable) so such a step should only be taken as a very last resort.

NICVA's Charity Advice Service offers advice and information on setting up a charitable company limited by guarantee.

7.7 Sources of further information on companies

Northern Ireland's Companies Registry produces a range of guidance notes to assist new and established companies. Guidance notes which may be of interest to voluntary sector companies include:

Incorporation/Registration

- CRN1 New companies
- CRN2 Choosing a company name
- CRN4 Change of company name
- CRN8 Exemption from using the word 'limited' in a company name
- CRN9 The new company - looking forward

Officers' responsibilities

- CRN15 Directors and companies registry
- CRN16 The duties and responsibilities of a company secretary

Document registration

- CRN20 Accounting reference dates
- CRN21 Dormant companies
- CRN22 Late filing penalties

Company closure

- CRN27 Striking off, Dissolution and Restoration
- CRN28 Liquidation and Insolvency

These 'Notes for Guidance' booklets can be obtained from:

Companies Registry
IDB House
64 Chichester Street
Belfast BT1 4JX

Tel: 028 9023 4488

