

Defining Charity: UK Perspective

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1. UK Jurisdictions

- 1.1 The United Kingdom comprises 3 charity jurisdictions – Scotland and Northern Ireland, alongside England and Wales, each with a distinctive legal inheritance, and in the case of Northern Ireland, an inheritance shared with the Irish Republic. As with other ‘federal’ systems the fiscal dimension is a central tax led influence over charity and its determination – Inland Revenue (a UK wide department) comparable to IRS. But the distinctive feature in the UK is the Charity Commission. This is a legal and regulatory authority which has developed out of the Chancery Court and Attorney General functions (comparable to US State functions) in England and Wales (only).

- 1.2 Reflecting the predominance of charitable activity in England (sheer size rather than ethos!) the role of the Charity Commission has come to dominate charity law throughout the UK. This is reflected in the fact that the courts have laid down that Inland Revenue should apply the charity law of England throughout the UK. This is for tax purposes, but the tax dimension has become so important in charity that, as a generalisation, one can say that at present it is the charity law of England, as determined by the Charity Commission of England and Wales subject to appeal to the courts, which applies throughout the UK. This paper accordingly concentrates on the English perspective, and reform issues there; but the situation is naturally not acceptable in Scotland and Northern Ireland, so reference is also made to the wider reform issues in those parts of the UK.

- 1.3 A government report setting out wide ranging proposals for the reform of charity law and regulation was published for consultation in September. The body of this paper sets out the present position, but section 9 briefly describes the reform proposals.

2. The Charity Commission

2.1 As a standing body the Charity Commission was established in 1853, initially to fulfil the oversight and reform responsibilities of the Chancery Court, bogged down in Dickensian constrictions. Legislation in 1960 and 1993 have made the Commission as much an administrative ‘regulatory’ body as a ‘quasi-judicial’ one. Technically it is a non-ministerial government department, under 5 Commissioners appointed by the Home Secretary (after an open recruitment process) but responsible for exercising functions set out in the Charities Act 1993 independent of Government control. The functions are to determine charitable status; maintain a register of charities; set a framework of accountability for registered charities; give advice and guidance on charity law and good practice; and investigate and remedy mismanagement and abuse.

2.2 The Commission has a staff of about 600, mostly administrative but supported by a couple of dozen lawyers and a dozen accountants, with an annual budget of over £25 million. Much of its work can be characterised as supervisory and advisory, relying on cooperation though backed up by powers of intervention when abuse or mismanagement is established. The annual reporting requirement of activities and accounts is now the basis for supervision. The Commission monitors the returns, has a programme of ‘inspection visits’ and follow up to the returns and risk factors built up on the basis of experience. Registration as a charity is now the entry (‘gateway’ as the Commission puts it) into the continuing process of supervision and accountability. Many issues of policy arise – as discussed briefly below; one in particular is controversial, namely the fact that determination of charitable status by the Commission, which the Charities Act makes binding and authoritative, is not only legal but also a ‘regulatory’ act.

3. The Determination of Charity

a. The scope of charity and the basis for its determination is under question. It is the dominant distinction in the voluntary sector (as not for profits tend to be called in the UK). In principle it marks the distinction between independent non profit

distributing bodies devoted to a public purpose and those directed at private or sectional interests. But the basis for that distinction, and the place of bodies fulfilling a public purpose through the interests of members (mutuals and cooperatives), raise reform issues. In particular there is a question about whether the concept of public benefit, on which charity is based, ought to be so central; and if so how it might be determined.

- b. The value of charitable status is threefold: automatic fiscal privileges; access to grant funding; and public fundraising. These factors push many voluntary bodies to seek charitable status. For example the effect of the creation of the National Lottery has led many small community bodies to set up as charities in order to access lottery funding. Self help groups, for which some form of mutuality status might be more suitable, have similarly been affected.
- c. The concept of charity in English law continues to derive from the Preamble to the Charitable Uses Act of 1601 (The Statute of Elizabeth). The ups and downs of court judgements over 400 years, through the distorting lens of mortmain, constitute a 'living' body of tradition on which day to day decisions are made by the Charity Commission, since 1960 (when it was made responsible for establishing a register of charities) the main source of legal determination of charitable status. The precise authority of the Preamble as a text (rather than a definition of charity) is disputed. The notion of applying its 'spirit and intendment' has largely been replaced by the concept of 'analogy'. The Commission basis for determining novel applications for registration has, since the 1980s, been to look for analogies with purposes accepted by the corpus of court judgements developed under the Preamble.
- d. It is well established that a key requirement of charitable purpose is that it provides a public benefit. A complex body of interpretation has been developed around the interpretation of public benefit, in particular from the Pemsel judgement of 1891

which codified charitable purposes under the four ‘heads’ of relief of poverty, advancement of education, advancement of religion and other purposes beneficial to the community. Under Pemsel there is a rebuttable assumption that purposes under the first three heads are public benefit, whereas the public benefit from other purposes has to be individually demonstrated.

- e. It is fundamental to the common law concept of charity that it changes as public need changes, with issues previously being regarded as charitable ceasing to be accepted when they are obsolete or superseded, and new ones accepted as new needs arise. The Charity Commission draws on this principle to introduce new charitable purposes, such as the promotion of harmonious community relations in the 1980s, and removing charitable status from gun clubs in the 1990s. The principle has been systematised in the long running review of the register which the Commission initiated at the end of the 1990s. This has led to the introduction of a number of new charitable purposes, such as the promotion of human rights this year.

4. Issues in Charitable Status

- a. There are concerns about whether the scope of charity, as it has developed in England, is too wide and in particular too far from the conception of relief of need as the general public understand it. It has certainly grown to extend far beyond ‘remedial philanthropy’ to provide a legal and institutional framework for organisations serving the public interest in the well-being of the community. Culture, learning and heritage are obvious, well-established branches of charity. That the Royal Opera House at Covent Garden provides ‘elite’ entertainment (at high price) is held to be variance with the notion of charity by many critics. On the other hand more ‘popular’ arts centres serving a wider public are less criticised (and charitable status encourages institutions like Covent Garden to develop programmes to attract a wider public).

- b. The traditional targets for criticising charitable status as in need of modernisation in Britain are the ‘public’ schools (notably Eton) which are held to be elitist, and private hospitals serving rich patients. Whatever view is taken of this issue it is a narrow point (on which the court judgement that charging for services ceases to be charitable if it prices out all but the well to do) rather than fundamental to the interpretation of public benefit.
- c. Issues also arise over bodies in the public sector with charitable status, like the British Council and the Arts Council. They retain charitable status so long as, in addition to their undoubted public benefit purpose, their trustees operate genuinely independently, despite reliance on public funds (and government appointment).
- d. Alongside public benefit there are three other principles which are fundamental distinguishing features of charities in Britain: non-profit distributing; independent trustee governance; and non-political.
- e. The not for profit principle is a fundamental reflection of the trust principle that trustees may not benefit personally from their trust. Though charities take many institutional forms in Britain (at least 9!) trust law influences all types, especially in governance. In recent years the Charity Commission has relaxed the non-benefit principle, allowing user trustees in accordance with current standards of good practice, and even (for example with the Wellcome Foundation) remunerated trustees. And charities have wide discretion to engage in commercial or trading activities, either directly in pursuance of their charitable purpose or indirectly through a non-charitable subsidiary.
- f. Likewise the fundamental principle of trust law that a trustee’s ultimate duty is the best interests of the trust underpins charity law, and the independence of charities. Trustees have absolute responsibility for deciding how to seek to realise the purpose of their charity. The independence of charities is a controversial issue in

the context of growing public/voluntary sector partnership, formalised by a government/sector negotiated framework of principles known as the ‘Compact’. The Commission has issued guidance on the responsibility of trustees to maintain their independence but there are concerns that it is undermined by the influence of funders, especially public sector funders.

- g. The principle that charities should be non-political is highly restrictive in British law, again influenced by trust law. Purposes directed at changing the law or government policy are regarded as political and incompatible with charitable status. This reflects the principle that the ultimate role of the courts is to enforce charitable (trust) purposes, and their role (as the English courts see it) is to uphold the existing law and leave government policy to the political process. The fact that the Charity Commission has recently accepted the promotion of human rights as charitable confirms, rather than being an exception to, this principle, since it is based on the fact that the European Convention on Human Rights has been made a part of UK law by the Human Rights Act. The Charity Commission has however been able to mitigate the effect of this by giving guidance enabling charities to engage relatively freely in campaigning and advocacy provided that it is in pursuance of their charitable purposes. Thus aid NGOs can campaign freely on issues, such as debt relief and the arms trade, relevant to poverty.

5. Tax Relief

- a. Charitable status attracts a range of fiscal benefits. A significant difference to most systems is the fact that basic tax relief on donations is paid to the recipient charity and not to the donor. Thus Inland Revenue makes a payment to the charity equivalent to the tax which the donor would have paid. There is much debate in Britain about how to create a better culture of giving, one issue being whether the form in which tax relief is given is an inhibiting factor.

b. The fact that tax privileges flow automatically from charitable status, combined with the fact that status is determined by the independent Charity Commission, not answerable to the tax authorities (though giving them an opportunity to comment in novel cases), raises questions as to whether tax relief ought to be automatically linked to charitable status, or whether there ought also to be some test of relevance to government policy. This is an important principle, whether government ought to support public benefit purposes, as developed by the Charity Commission out of the charity law tradition, regardless of whether a charity's trustees seek to achieve it in ways of which the government of the day approves.

6. 'Pay out'

a. English charity law operates on broad principles, in particular that the best interest of the charity should be met. The basic principle is that the resources of a charity must be used to achieve its purpose, and if indirectly, for example on fundraising or administration, economically and commensurate with achieving the charity's purpose effectively. Charity law administration, reflected in the practice of the Charity Commission (and accepted by Inland Revenue), is based on the application of these principles and does not set percentages, for example on expenditure in relation to capital or on political activities.

b. The accumulation of reserves by charities has been controversial and the Commission has issued guidance on the approach trustees should adopt. These are expressed in terms of questions trustees should ask themselves – on the premise that charitable resources should be used for the benefit of beneficiaries unless there are justifiable reasons for retaining them, e.g. to safeguard commitments in the event of a down turn in income or to meet exceptional developments. The principle of endowed capital remains, under which capital is solely for income, but the Commission (with opposition from charity lawyers) has sought to relax the constraint on the expenditure of endowed capital.

7. Accountability

- a. The accountability of charities is based on standardised requirements for reporting activities and accounts annually, graduated by turnover. These are set in regulations under the Charities Act 1993 and elaborated in the Charity Commission's Statement of Recommended Accounting Practice (SORP). This fulfils three functions: it is designed to encourage good management; to provide transparency in charities' activities and finances; and to provide the basis for Charity Commission supervision.

- b. Information about registered charities is available on the Commission's website and their reports and accounts must be publicly available. The Commission's aim is to maintain public confidence in the integrity of charities. Its focus is on good governance, management and financial practice. Its formal powers of intervention, which, after investigation, extend to removing trustees and winding up charities, may be invoked only if a high threshold of mismanagement or abuse is exceeded. Much of its work is advisory and preventative.

- c. Standards of efficiency and effectiveness in charities, particularly large ones delivering public services, are of increasing concern. The issue of how far Commission 'regulation' should encroach on the independence of charities and how far 'self-regulation', for example promoted by umbrella bodies like the National Council for Voluntary Organisations (NCVO) and the Institute for Fundraising are under discussion. A key question is where the balance lies between the traditional independent discretion of trustees and public confidence and effectiveness.

8. Governance

- a. Linked to accountability and standards is the question of governance and the role of trustees. Charity law places absolute responsibility on essentially unremunerated trustees. In practice in charities employing staff, especially larger ones, the role of

trustees is oversight, holding staff to account, and strategic, setting the direction and ethos of the charity. Issues over the balance between trustees and staff arise, but the value of altruistic voluntary trusteeship, even for large public charities, continues to command public and sector support.

- b. Although many charities operate commercially to quite a large extent, there are calls to extend the scope of not for profit enterprise, for example in the form of a new 'public interest company' form. Whether this is necessary and/or desirable is debatable – examples of modern forms of entrepreneurial activity within the form of charity include the Jorvic Centre in York (providing a Viking visitor centre both earning money for the York Archaeological Trust and furthering its educational purposes) and the London wetlands centre, developed in partnership with private property developers out of redundant reservoirs in West London by the Wildlife Wetlands Trust to provide a recreational and ecological resource for wildlife near the heart of London. On the other hand it is argued that charity law is a constraint both on the public interest purposes and ethos which a more flexible commercial model would meet, for example opening access to funding from the capital markets more easily.

9. Reform

- 9.1 The long awaited report by a team led by the Cabinet Office of the UK on the law and regulation of charities and the voluntary sector was published at the end of September. Billed as the most far reaching reform of charity for 400 years it proposed a range of fundamental changes to the legal and regulatory basis for voluntary bodies. (From the perception of this ex 'regulator', however, the changes the report proposes are more radical in form than content, building on the changes made following the Charities Act 1993.) The report makes 61 recommendations. At this stage it is a consultation document, with comments invited by the end of 2002. The report is on the website on <http://www.strategy-unit.gov.uk/2001/charity/main.shtml> .

9.2 The reports' main proposals are

- that charity should be redefined in law, with greater emphasis on the public benefit test;
- relaxation of trading restrictions to encourage enterprise;
- encouragement of campaigning;
- the creation of a Community Interest Company;
- modernisation of the law on mutual bodies;
- a new legal form, the Charitable Incorporated Organisation;
- improved accounting requirements;
- strengthened regulatory role for the Charity Commission, reconstituted as a statutory corporation, the Charity Regulation Authority (CRA).

9.3 The report envisages that legislation will replace the Preamble and Pemsel by 'a new definition (sic) comprising 10 purposes'. The aim is to provide a clearer, modern framework within which the Charity Commission (CRA) will determine charitable status on the basis of public benefit. The report envisages that this framework will continue the retention of existing case law with flexible evolution responding to changing society. This approach is reminiscent in particular of that adopted by the Australian inquiry into the determination of charity.

9.4 The report places increased emphasis on the public benefit test, both at the point of determination and as part of ongoing accountability. (The report specifically endorses the Charity Commission's 'gateway' approach see above para 2.2.) The report refers explicitly to the concerns over the charitable status of independent schools and hospitals, in effect building on the existing common law test. (Initially such media attention as the report has received has focussed on this issue.) The CRA would carry out an annual 'public benefit' audit.

- 9.5 The report has nothing to say about the constraint which prevents bodies like amnesty from having charitable status on the grounds that their objects are, under the very wide common law definition, ‘political’ - it accepts that charities ‘cannot be established with the aim of furthering the interests of a political party or securing or opposing any change in the law or policy and decisions of a government whether in this country or abroad’! Its emphasis is on clarifying and relaxing the restrictions on the activities of bodies which meet the test of not having political objects. It endorses the Charity Commission’s statement of the legal position that charities may engage in activities which are ‘political’ in charity law if they are reasonably undertaken to fulfil their charitable purposes. It calls for greater endorsement of the right of charities to engage in campaigning activity.
- 9.6 The recommendations on regulation by the Charity Commission, transformed into the Charity Regulation Authority with a Chief Executive accountable to a Chairman and widened Board, are designed to provide a new accountability framework based on increasing public trust and confidence; ensuring compliance with charity law; enabling and encouraging charities to maximise their social and economic potential; and enhancing charities accountability to donors and beneficiaries. The functions of the CLA are those of the Charity Commission, with emphasis on performance reviews of the sector.
- 9.7 If implemented the report’s recommendations will complete the transformation of the Charity Commission from a quasi-judicial legal body to a quasi-regulatory administrative body. Tensions in the relationship between the legal and administrative functions which already exist will become more pronounced. More fundamentally the wholesale incursion of the legislature into common law will take the legal basis of charity into new territory. It is significant that the report does not address the question of trust law and its permeating influence over charity governance.

10. The rest of the United Kingdom

10.1 Scotland The fact that there is no equivalent to the Charity Commission in Scotland, and in particular that there is no publicly accessible register of Scottish charities, has been a matter of concern north of the border. The creation of a Scottish Charity Office in the 1990s limited to an investigation and remedial role, with no powers or resources to fulfil an advice giving function, together with the fact that the Inland Revenue applies English charity law, led to the establishment of the McFadden Commission by the newly devolved Scottish Executive to review the arrangements for charity law and regulation in Scotland. The McFadden report recommended the establishment of Charity Scotland, with a role comparable to the Charity Commission, to develop charity in Scotland distinct from, but on principles comparable to, the law in England and Wales. The delay in the publication of the Government has stalled reform in Scotland. It makes no recommendations for Scotland, given its 'devolved' jurisdiction. Now that the report has appear the way is clear for the implementation of the McFadden recommendations, no doubt taking the Cabinet Office report into account.

10.2 The position is similar in Northern Ireland. Discussion of the need for reform, in common with the Republic has begun; but, as in Scotland has stalled while the Cabinet Office report has been awaited. There are however, currently no official proposals for reform on the table. Calls for reform have been made in a report by the Centre for Voluntary Action Research at Ulster University.