Charities (Protection and Social Investment) Act 2016

Elen Griffiths | 04 May 2016

The Charities (Protection and Social Investment) Act 2016 (the Act) has been hailed as "part of a big reform programme for charities and social enterprises" by Rob Wilson, the Minister for Civil Society. We explained the background to the Act and its development in our briefing in August 2015. The Act received Royal Assent on 16 March 2016; in this article we set out its key provisions and highlight points for charities to note.

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The Act has widened the Charity Commission's regulatory powers in a number of ways, notably extending its powers to suspend, remove or disqualify charity trustees. The Act also responds to current trends and concerns in the sector, by including new provisions around charity fundraising and granting a new power to charities to make social investments.

Main features of the Act

Regulatory Powers

Official warnings by the Commission

Section 2 of the Act brings in a new power for the Charity Commission to issue official warnings to trustees or charities it considers have breached their duties or otherwise engaged in misconduct or mismanagement. This power is intended to furnish the Commission's armoury with a weapon of medium strength: an official warning should have more impact than the publication of general guidance or informal discussions between the Commission and a charity, but land less of a blow than the opening of an inquiry.

Prior to issuing such a warning, the Commission will have to give notice to the charity in question. There is no prescribed notice period, but when the Act was being debated in the House of Commons, Minister for Civil Society Rob Wilson indicated that in most cases it is likely to be around 14 days. The notice must contain a number of prescribed elements:

- grounds for making it;
- action the Commission considers should be taken, or which the Commission is

considering taking, to rectify the mismanagement or misconduct;
- whether the Commission intends to publish the warning; and
- a period in which representations can be made to the Commission about the contents of the proposed warning.

During the passage of the Act through Parliament, calls were made for charities to be given a right to appeal to the Tribunal against any official warning from the Commission. However, this was considered to be disproportionate, and it is to be noted that the Act does not grant charities the right to appeal against official warnings. The only recourse for trustees and charities who feel the warning was unjustified will be to apply to the Courts to have it judicially reviewed.

When the Act was being debated in the Commons, the Opposition expressed concern that the requirement for the notice to state the action that should be taken to rectify misconduct or mismanagement amounted to a covert power for the Commission to tell trustees what to do. Rob Wilson said that it did not: the decision on how to rectify misconduct or mismanagement would ultimately lie with the trustees, though they would need to demonstrate that their action had been effective. He also mentioned that the Commission has indicated that it would not publish warnings ***"if it considered that it would not be in the public interest to do so"***. He added that the Commission is statutorily obliged to act proportionately and would have to remove published details of warnings after a period, noting that it currently archives material after two years.

Taking into account wider conduct by a charity trustee

Where the Charity Commission has opened a formal inquiry into a charity and found misconduct or mismanagement, it has power to take several steps to protect the charity, including suspending trustees or appointing interim managers. The Act adds to these provisions: if the Commission is satisfied that a particular individual is implicated in the wrongdoing, it may – when deciding how to exercise those powers – take into account any conduct by that person in relation to another charity or which appears to the Commission to be damaging to public trust and confidence in charities.

Automatic disqualification from being a trustee

The Act extends the list of offences which automatically disqualify a person from being a charity trustee (set out in section 178 and new section 178A of the Charities Act 2011). These now include money-laundering, bribery, a range of terrorism offences, contempt of court and perverting the course of justice, among others. Persons who are disqualified under this list will also be prevented from holding an office or employment with 'senior management functions' in the charity. Potential trustees or office-holders who fall under this category will need to apply for a waiver from disqualification, which the Commission have the discretion to grant as set out in Section 181 of the Charities

Act 2011. Charities may need to review the list to check whether their trustees are affected, particularly as trustees who have been disqualified and continue to act could face prosecution in the future under Section 183 of the Charities Act 2011. Recognising that this section will apply to serving trustees and senior office holders, Rob Wilson has said that charities will be given notice of ***"at least six to 12 months"*** before it is brought into force. It is estimated that the number of trustees and senior officers who will be affected is in the low hundreds.

Power to disqualify someone from being a trustee

In our earlier briefing, we noted that Section 10 is one of the most important provisions in the Act. It introduces a new Section 181A into the Charities Act 2011, giving the Commission a discretionary power to make "disqualification orders". These allow the Commission to disqualify a person from being a trustee or any office-holder with senior management functions in relation to a particular charity, a class of charity or all charities.

To make such an order, the Commission will need to satisfy itself that at least one of a list of conditions is met; that the person is "unfit" to be a charity trustee; and that making the order is desirable in the public interest. Some of the wording in this power has been criticised for being too broad and the Opposition sought to tighten it up when the Act was passing through Parliament. Their amendments were rejected; the Minister referred to the Charity Commission's policy paper on how it plans using the power, pointing out that the Commission is committed to working this paper up into draft guidance and consulting prior to issuing a final version, before the provision is brought into force.

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Power to direct charities not to take certain actions

The Charity Commission already has the power to direct a charity to take certain actions; and this new power is the flip side of the same coin. Section 6(2) of the Act now grants the Commission the power to direct charities **not** to take action that it considers would constitute misconduct or mismanagement. This provision follows the Act's general trend of widening the Commission's regulatory powers and introduces another weapon to its armoury. It should be noted, however, that both these powers are only exercisable after the Commission has opened a formal inquiry into the charity in question.

Social investment

The Act isn't purely a way of fattening the Commission's rule-book; it gives charities some additional powers too. Section 15 of the Act grants a power to charities to allow them to make social investments, that is, investments that are not solely aimed at

achieving a financial return for the charity, but also at furthering the charity's purposes. This provision explicitly grants charities the power to make such investments, erasing any question marks that charities might previously have had over whether they were allowed to go down this route.

Charities that do wish to take advantage of this provision must ensure that any such investment directly furthers the charity's purposes. If a charity is investing special trust property[1], then the social investment must further the purposes of that special trust. The new power only permits charity trustees to make social investments involving permanent endowment where the charity trustees expect that making the social investment won't contravene any existing restriction on expenditure, which (according to the Explanatory Notes to the Bill[2]) is likely to mean that the trustees expect the value of any such investment to be maintained.

New charities that do not wish to take advantage of the new power to make social investments will be able to restrict or exclude the power in their governing document. It is further worth noting that the new power is not available to charities established by Royal Charter or by legislation.

Fundraising measures

Sections 13 and 14 of the Act contain a range of provisions aimed at raising standards in charities' fundraising activities. These respond to a perceived need among the public for charities' fundraising activities to be better regulated, following the media interest in the death of poppy-seller Olive Cooke. The provisions lay the ground for a new regulatory regime to oversee charity fundraising, extend the list of matters that must be included in agreements with professional fundraisers and commercial partners, and introduce a requirement for certain charities to set out fundraising matters in their annual reports.

Additional statutory inclusions

Section 13 of the Act adds to the list of matters that must be included in professional fundraising agreements and commercial participation agreements[3], which charities are required to put in place. Such agreements will now need to specify how the professional fundraiser or commercial participator will protect people from unscrupulous fundraising practices and what voluntary scheme (if any) the

[1] That is, property that is held for charitable purposes that are narrower than the charity's overall purposes.
[2] Apparently there are to be Explanatory Notes to the Act but, at the time of writing, only the Notes to the Bill are available. You can find them here. They do not cover the sections on fundraising, which are discussed later in this article.
[3] A "commercial participator" is any person or organisation carrying on a business (other than as a professional fundraiser) that, as part of a business venture, states that it will be making charitable contributions, for instance by saying that a percentage of the purchase price will be given to charity.

professional fundraiser or commercial participator has agreed to put in place. A clause will also need to be inserted setting out what arrangements are in place so that the charity can monitor compliance.

Reporting requirement

Once the relevant section has been brought into force, charities that are statutorily required to have their accounts audited[4] will have to include information about their fundraising activities in their annual reports. The reporting requirement introduced in Section 13 of the Act sets out a number of items charities will need to report on, including the charity's approach to fundraising activities, whether the charity has used a professional fundraiser or commercial partner, the details of any voluntary scheme the charity has adopted to regulate fundraising activities and any breaches of that scheme. The focus is on better regulating and supervising fundraising activities, with charities to which the provisions apply being required to state what steps they take to monitor fundraising activities and to combat intrusive or pressurising fundraising tactics. Charities will also need to report how many complaints were received relating to fundraising activities.

A possible new regulator

Section 14 of the Act strengthens the existing reserve power for fundraising to be statutorily regulated, either by the Charity Commission or by a new fundraising regulator, at a later date. If the power is exercised, charities will be obliged to comply with any regulator's requirements, have regard to its guidance, register with the regulator and pay fees to it. In Parliament, Rob Wilson indicated that this is a fall-back provision that will only be used if the self-regulatory regime currently being developed fails – at least in the eyes of the Minister – to address ongoing concerns about fundraising.

Interaction with CC3

In our previous briefing, we considered how the Act might interact with the Charity Commission's CC3 Guidance, specifically whether the Commission may deem charity trustees' failure to follow specified good practice to be evidence of misconduct or mismanagement, potentially leading to the Commission issuing a formal warning under Section 1 of the Act (or taking other regulatory action). Rob Wilson referred to this when the Act was being discussed in Parliament, pointing out that paragraph 26 of the Explanatory Notes states: ***"Failure to follow good practice could not automatically be considered to constitute misconduct or mismanagement"***.

If you require further information on anything covered in this briefing please contact Elen Griffiths (elen.griffiths@farrer.co.uk; 020 3375 7211) or your usual contact at the firm on 020 3375 7000. Further information can also be found on the Charities page on our website.

[4] Currently, this applies to (1) charities whose gross annual income exceeds £1m, and (2) charities with assets worth over £3.26m and a gross annual income of over £250k.

Nevertheless, trustees who decide not to follow the Commission's best practice recommendations will need to be able to explain and justify their decision to adopt an alternative approach. Any decision by the trustees to depart from best practice will need to be conscious and the reasons for doing so carefully minuted.