

Financial Responsibilities of the Board

- ◆ Financial Governance
- ◆ Delegation
- ◆ Charities & Trading - overview

FINANCIAL GOVERNANCE

The FINANCIAL aspects of Governance are an especially important area of Board Members' general duties and responsibilities as Directors and Charity Trustees.

General Duties

There are two headline roles for trustees:

- Stewardship of the past (heritage, original vision and values) and of the future (next generations of beneficiaries; assets)
- Governance of present activities and resources

"Governance is the process and activity by which a governing body ensures that an organisation is effectively and properly run. Governance is not necessarily about doing, it is about ensuring things are done". Sandy Adirondack, Trainer in Legal Aspects of Governance

The board must

Ensure (are the right reporting requirements, accountability structures, procedures, policies, skills and resources in place?)

Oversee (are you getting all - but only - the reports and information you need?)

Authorise (have all decisions been properly delegated or brought to the Board as recommendations?)

General Legal Duties of Trustees

Act in Good Faith

Act with Prudence (the opposite is recklessness)

Act with Care (the opposite is negligence)

Getting expert advice when needed, including from your staff

Obtain and understand reports and information

Acting in Good Faith in Financial matters

Accepting overall responsibility of ensuring, overseeing and authorising

Acting within your powers as set out in Articles

Honesty and transparency - declaring conflicts of interest, bringing important or exceptional decisions to the whole Board

Complying with regulatory requirements especially regarding audit and filing of accounts

Acting with Prudence in financial matters

Ensuring funds and assets are only used to further the charity's stated objects

Budgeting and financial planning

Keeping both the immediate and long-term interests of beneficiaries in mind e.g. having a Reserves policy

Safeguarding the Assets - avoiding unnecessary or undue risks, identifying and managing other risks

Ensuring solvency but safeguarding creditors' interests if an insolvency risk exists

Acting with care in Financial Matters (1)

Ensuring appropriate financial policies, procedures and controls e.g. cheque signatories; preventing fraud

Robust financial reporting by staff at a level which Trustees can (i) interpret and (ii) use to inform their decisions

Oversight of Restricted Funds especially to comply with funders' requirements

Board approval of accounts as well as AGM endorsement

Appointment of suitable auditors

Acting with Care in Financial Matters (2)

Ensuring sufficient resources to undertake specific activities especially staffing and skills

Authorising fundraising

Ensuring adequate insurance cover

Relationship with Trading Company

Obtain advice when needed especially when required – investments

DELEGATION

The Board of a Company is DELEGATED by the Members to act on behalf of the Company as a Corporate body.

As such the Board can only delegate matters further insofar as there is an EXPLICIT power to do so in the Company's Articles

Trustees are unable to "shift their duties on to others"

Any delegation by a trustee body is to enable the trustee body as a whole to better fulfil their duties

The delegation does not enable or cause the trustee body as a whole to ADBICATE from their collective responsibilities – the Board holds responsibility for its choices in any acts of delegation

DELEGATION in WHCF

Article 43 enables the Board to delegate any of their powers and functions to a committee (or committees)

It also sets out the terms on which they may do so

A committee must be made up of two or more Directors i.e. any other person who is brought in to aid a committee in its work is there in an advisory capacity only

The Terms of Reference of any committee MUST be recorded in Board minutes

The proceedings of the committee must be "fully and promptly" reported back to the Board

"SUBSTANTIVE" Terms of Reference

The purpose(s) of the Committee MUST INCLUDE: Scope of the work (e.g. topics or issues) it is authorised - and thought competent - to cover

Specific Tasks of the committee NOTE: these can be time limited, as with a "working party"

Whether it has decision-making powers

KEY ISSUE: Whether it can authorise expenditure, and if so within what limits

NOTE: Especially relevant for appointment panels

Whether it can only propose or recommend actions to the Board, for the whole Board to decide upon

Usually described as an 'Advisory committee'

Requirements for reporting back to the Board

e.g. “at the next following meeting”; or “quarterly”

“ADMINISTRATIVE” Terms of reference

The make-up of the committee e.g. names and/or or any ‘ex-officio’ members (e.g. Treasurer)

Whether other Board members have a right to attend (e.g. Chairperson)

Whether they can appoint advisors

General administrative matters e.g. keeping minutes, frequency of meetings (as relevant)

Budget issues

Sometimes a committee will need its own budget

The period of office of members e.g. until the first Board meeting following an AGM

EXAMPLE DELEGATION TASK

Review and Re-draft terms of Reference for the WHCF Finance Committee

for discussion with/advice from the CEO and Finance Officer and Proposal of final draft for Board approval

This task could be undertaken by the present Finance Group, WHCF staff or by a working party of a couple of Board members

CHARITIES AND TRADING - OVERVIEW

Trading by Charities is subject to:

Constraints in law

Tax issues

Charity Commission guidance

Trustee duties of Trust, duty of Prudence and duty of Care

Good Practice

The Articles of the Charitable Company, and in particular the Powers

The Articles of the Trading Company itself

Considerations of maximizing income

Internal administrative capacity and efficiency

HEADLINE ISSUES

A Charity MUST use its resources WHOLLY and EXCLUSIVELY in the furtherance of its Charitable Objects

It follows that a Charity can ONLY be engaged in trading activities where the Purpose of any specific Trading Activity is as a means of putting into practice its specific Charitable Objects

Where the trading activity is a DIRECT means of fulfilling the Charity's Objects , this is called PRIMARY PURPOSE TRADING

Sometimes a Charity can only fulfil its Objects effectively if its Trading activities include an element of indirect or unrelated trading

For example, a Playhouse might go bankrupt through lack of playgoers if there was no on-site bar open around the times of performances

Where trustees can reasonably justify that such indirectly or unrelated trading is essential or significantly contributive to the fulfilment of its direct mission through a primary purpose trade, this is called ANCILLARY TRADING

For example the Playhouse above might have to be charging for admission (i.e. trading as a theatre); if performances were free, there would be no primary purpose trading activity

Primary Purpose trading by a charity, and trading that is ancillary to a Primary Purpose Trade, is exempt from Corporation Tax.

If a Charity engages in trading that is not exempt from corporation tax, and tax is levied, the trustees risk being made personally liable to make good the loss to the Charity

Apart from anything else, payments to HMRC are non-charitable expenditure!

There may also be issues of negligence or reckless disregard

Regardless of the tax position, a Charity MUST use all its resources wholly and exclusively on activities covered by its particular and specific charitable purposes

For example, it would be a breach of Trust for a charity set up to benefit young people to provide services for the elderly (unless as an activity provided by the young people for the young people's own benefit) regardless of how worthy or charitable meeting the needs of elderly people might be.

Similarly it would be a breach of Trust for a charity to focus on an geographical area of benefit unrelated to an area stated in its Objects even if a Trading Activity meets the Primary Purpose test

Trading activities are inherently risky

- special trading risks , such as Sale of Goods Act obligations

- risk of Tort e.g. from selling food

The Charity Commission therefore advise that a Trading Company is normally used if there is such a risk

Trustees are obliged to avoid needless risks

Trustees are obliged to identify and manage any unavoidable and/or "sensible" risks

a trading company is a way of managing the risk

A Trading Company is mainly set up to:

Bring in additional income to the charity

Manage any risk of "business failure" or "trading deficit"

Avoid negligence in incurring tax payments for which the charity ought not to be liable

A Trading Company must not set up solely for tax avoidance or implement activities outside the charitable purposes of the charity including other activities that may be charitable

Introduce an additional "soft" resource or asset

An exception to the general case for using a Trading Company when a charity is engaged in substantial and/or permanent and/or taxable trading can usually ONLY occur where:

There is Primary Purpose Trading

AND

The administrative cost to the Charity of operating a Trading Company is disproportionately burdensome in comparison to the income received by the Charity

AND

The risks of the trading activity are LOW

There is a general tax exemption for small scale trading by charities

It can only be used where the total turnover from taxable trading is less than £50,000 and sometimes a lot less (£5000) for smaller charities

If there is "mixed trading" the administrative and tax complexities are more burdensome because tax exempt trading and potentially taxable trading must then be kept separate WITHIN the internal charity accounts

Mixed trading occurs if e.g. some goods are sold, or services provided, which are not directly related to the Charity's Objects

Renting out property can be a taxable trade if services are also provided to the use

The governing body of a Charitable Company will be in breach of their duties as Company Directors AND their duties as Charity Trustees if they do not act within their POWERS

The Articles of many modern Charitable Companies EXPLICITLY prohibit the Charity from taxable trading and/or "permanent trading activity"

So, to do so would be "ultra vires" activity - i.e. outside of, and in breach of, the trustees' powers

A Trading Company is incorporated as an independent "legal person". This means:

It must be governed in accordance with Company Law

The Directors are bound by the duties of company directors

These include Statutory Duties to :

- Promote the success of the Trading Company

- Act within their powers and in line with the Articles of the Trading Co.

- Exercise independent judgment

- Declare personal or "connected" interest

- Avoid conflicts of interest and loyalty including those with the charity itself

The role of Trading Companies is likely to become more significant e.g. lack of grants, sustainability, independence

Trading Company Directors often need a different skills set e.g. business connections; risk-taking; using loan finance

The two "Sets" of directors can overlap but should not overlay

Conflicts of loyalty must be manageable

Conflicts of interest can arise

Trading Company directors have full legal delegation and independence

Trading Company is a resource

To be used as effectively and productively as possible for the charity

