



The Law Reform Commission  
AN COIMISIÚN UM ATHCHÓIRIÚ AN DLÍ

# **CONSULTATION PAPER**

**LEGAL STRUCTURES FOR CHARITIES**

**(LRC CP 38-2005)**

**IRELAND**

**The Law Reform Commission  
35-39 Shelbourne Road, Ballsbridge, Dublin 4**

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## THE LAW REFORM COMMISSION

### Background

The Law Reform Commission is an independent statutory body whose main aim is to keep the law under review and to make practical proposals for its reform. It was established on 20 October 1975, pursuant to section 3 of the *Law Reform Commission Act 1975*.

The Commission's Second Programme for Law Reform, prepared in consultation with the Attorney General, was approved by the Government and copies were laid before both Houses of the Oireachtas in December 2000. The Commission also works on matters which are referred to it on occasion by the Attorney General under the terms of the Act.

To date the Commission has published 77 Reports containing proposals for reform of the law; 11 Working Papers; 37 Consultation Papers; a number of specialised Papers for limited circulation; An Examination of the Law of Bail; and 26 Annual Reports in accordance with section 6 of the 1975 Act.

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## NOTE

The Law Reform Commission's Second Programme for examination of certain branches of the law with a view to their reform: 2000-2007 identified the law of trusts including the law of charities for examination.

Given the considerable interaction between general trust law and the law relating to charitable trusts, the Commission published two consultation papers in February 2005 - *Trust Law: – General Proposals* (LRC CP 35-2005) and *Charitable Trust Law: General Proposals* (LRC CP 36-2005). The Consultation Papers examined some specific areas of the law of trusts and the law of charities particularly in relation to the role, powers and duties of trustees.

This Consultation Paper continues the Commission's review of charity law by examining the existing legal structures within which charities operate and considers whether there is a need for an alternative new legal structure tailored specifically to meet the needs of charities.

The Commission intends to publish in one Report its final recommendations on this topic and on the earlier Consultation Paper *Charitable Trust Law: General Proposals*.



## INTRODUCTION

1 The purpose of this Consultation Paper is to examine the existing legal structures within which charities operate in Ireland and to consider whether there is a need for an alternative new legal structure tailored specifically to meet the needs of charities.

2 Apart from charities, many associations such as community groups and social enterprise groups are also formed for public benefit and not-for-profit purposes. It should be noted that this Consultation Paper deals only with organisations set up for charitable purposes. The need for a separate legal structure for other not-for-profit organisations may also require consideration in the future and, in this regard, the Commission notes that the Company Law Review Group has recommended that there should be a new legal vehicle for bodies wishing to maintain clearly defined objects known as designated activity companies (DACs).<sup>1</sup>

3 The Paper begins in Chapter 1 by looking at the existing legal structures used by charities. These structures include the charitable trust, the unincorporated association and the company – usually a company limited by guarantee. The advantages and disadvantages of each of these structures are summarised.

4 Chapter 2 reviews the current institutional arrangements for the regulation of charities in Ireland and also looks at the proposals for the introduction of a statutory body for the regulation of charities.

5 Chapter 3 examines developments in other jurisdictions in relation to the design of an alternative new legal vehicle tailored exclusively for charities.

6 Chapter 4 considers whether there is a need for a new legal structure for charities in Ireland.

7 Chapter 5 summarises the provisional recommendations of the Commission.

8 The Commission usually publishes in two stages: first, a Consultation Paper and then a Report. This Consultation Paper is intended to form the basis for discussion and accordingly the recommendations,

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<sup>1</sup> *Company Law Review Group Second Report 2002-2003.*

conclusions and suggestions contained herein are provisional. The Commission will make its final recommendations on this topic following further consideration of the issues and consultation. Submissions on the provisional recommendations included in this Paper are also welcome. In order that the Commission's Report may be made available as soon as possible, those who wish to make their submissions are requested to do so in writing or by e-mail to the Commission by **31 March 2006**.

## CHAPTER 1    EXISTING LEGAL STRUCTURES FOR CHARITIES

### A            Introduction

1.01        The voluntary sector in Ireland is rich and diverse and has played a significant role in the economic and social development of communities and society as a whole. Charities comprise one part of the voluntary sector and the value of the charity sector has been estimated to be worth €20 billion.<sup>1</sup>

1.02        Charities<sup>2</sup> may be constituted in many different ways and all charitable activity requires some form of legal structure within which to operate and, if relevant, within which to hold charitable property. Charitable status is dependent on an organisation having charitable purposes, rather than on the specific legal form that is taken.<sup>3</sup> The distinction between charitable status which relates to the existence of charitable purposes and a charity's legal structure should be noted. The choice of structure lies with those who create the charity, or with those who control it.

1.03        The importance of legal frameworks for voluntary organisations<sup>4</sup> in the European Community has been recognised.

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<sup>1</sup>        See *Submission from the Charities Regulation Study Group to the Department of Community, Rural and Gaeltacht Affairs on the Consultation Paper on Establishing a Modern Statutory Framework for Charities*, May 2004. For a number of reasons, including the lack of an agreed definition of charity and the lack of a charities registration system, this figure can only be taken as a guide.

<sup>2</sup>        There is no definition of a 'charity' as such. Charities are identified and defined by reference to their 'charitable purposes'. In *Commissioners for Special Purposes of Income Tax v Pemsel* [1891] AC 531, four categories of charitable purposes (the 'Pemsel' categories) were identified: the relief of poverty; the advancement of education; the advancement of religion and other purposes beneficial to the community.

<sup>3</sup>        Certain charities are recognised by the Revenue Commissioners as qualifying for charitable exemption from tax liability. However, it should be noted that not all charities apply for tax exemptions and this does not affect their status as a "charity". The fact that a body may not have an exemption from tax may not necessarily mean that that body is not a charity.

<sup>4</sup>        Including both charitable and other not-for-profit organisations.

In its 1997 Communication,<sup>5</sup> the European Commission emphasised that:

“The importance of having clear, positive legal and fiscal frameworks for voluntary organisations and foundations to work in cannot be underestimated. Organisations find it difficult to develop their work when such frameworks do not exist, whether they be at national or European levels.”

1.04 The European Commission has proposed certain measures such as the creation of a European Association aimed at giving organisations a legal personality in other countries within the European Union. This would be an incorporated body established under Community law, which would ensure equal recognition for associations in all Member States and allow them to operate freely throughout the European Union.

1.05 Charities in Ireland currently operate under various different legal structures and each of these structures has a separate body of law governing its operation. The traditional legal structures used by charities are the charitable trust, the unincorporated association or the company – usually a company limited by guarantee.<sup>6</sup> Charitable trusts are subject to general trust law, unincorporated associations are subject to general contract law and charitable companies are subject to company law. Each structure is also subject to the law in respect of charities. This creates obvious difficulties in any attempt to regulate and codify any set of rules to apply across all of the different legal structures.<sup>7</sup> Difficulties relating to the interaction of charity and trust and company law have also been encountered in other jurisdictions.<sup>8</sup>

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<sup>5</sup> *Promoting the Role of Voluntary Organisations and Foundations in Europe* – COM (1997) 241 Final, 6 June 1997.

<sup>6</sup> There are also other charitable bodies such as societies incorporated by charter (for example, the Royal College of Surgeons in Ireland), or created by statute or under other legislation (such as the industrial and provident societies legislation).

<sup>7</sup> In its Consultation Paper, *Establishing a Modern Statutory Framework for Charities* December 2003, the Department of Community, Rural and Gaeltacht Affairs proposed (at page 16) that the law should be codified so that the role, duty of care, responsibilities and duties of charity trustees/officers/directors would be confirmed as being the same no matter what form of legal structure or governing instrument was used.

<sup>8</sup> In England, the *Trustee Act 2000* does not apply to charitable companies. The Law Commission of England and Wales (whose recommendations formed the basis for the Act of 2000) had concluded that “it had become apparent in finalising the recommendations that there would be considerable technical difficulties in doing so... [c]haritable corporations are not necessarily subject to all the rules applicable to trustees, and it is by no means clear that it would be appropriate for some of the proposed provisions (such as those relating to powers of delegation) to be applied to them” see Law Commission Report *Trustees’ Powers and Duties* (no 260 1999) at paragraph 1.20.

1.06 The nature of the existing legal structures for charities has been covered in depth in existing literature<sup>9</sup> and what follows therefore is just a brief analysis of the main legal structures within which charities currently most commonly operate and how each is governed. Each structure has its own advantages and disadvantages and it is widely acknowledged that none of the existing vehicles is ideally suited to facilitate the activities of modern charities.<sup>10</sup>

## **B Charitable Trusts**

### **(1) General**

1.07 A trust is an arrangement whereby one or more persons hold property for the benefit of another person or persons. A charitable trust is an obligation imposed on one or more persons in equity to hold property for charitable purposes. Charitable trusts are based on equitable principles and the general law of trusts and have been used by charities for many years.

1.08 A charitable trust is normally established by way of a governing instrument known as a trust deed or by way of a declaration of trust. The trust deed sets out the objects of the trust and provides for the administration of the trust. The trust deed will also normally provide for the appointment or replacement of trustees whose purpose is to administer the trust.<sup>11</sup>

1.09 The individuals involved in controlling and managing the administration of a charity through the structure of a trust are known as trustees. Trustees may be individuals or corporate bodies<sup>12</sup> or a combination of both. This is a single-tier structure, with no members other than the trustees who perform the dual roles of governing body and membership. The legal title to any trust property is held in the names of individual trustees or in the company's name in the case of a corporate trustee.

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<sup>9</sup> See for example O'Halloran *Charity Law* (Round Hall Sweet & Maxwell 2000); Luxton *The Law of Charities* (Oxford University Press 2001); Picarda *The Law and Practice Relating to Charities* (3<sup>rd</sup> ed Butterworths 1999); Law Society of Ireland *Charity Law: The case for reform* (2002).

<sup>10</sup> See Law Society of Ireland *Charity Law: The case for reform* (2002) at 204; Luxton *The Law of Charities* (Oxford University Press 2001) at 17; O'Halloran *Charity Law Review in Ireland* and O'Halloran 'Challenges for the State/Third Sector Partnership' *International Journal of Not-for-Profit Law* (2002) 5.

<sup>11</sup> Where the trust deed is silent on the appointment of trustees the *Trustee Act 1893* is relevant. See Law Reform Commission *Consultation Paper on Charitable Trust Law: General Proposals* (LRC CP 36-2005), chapter 1.

<sup>12</sup> This arises where the charity is set up by deed of trust but the trustee is a corporate entity. In such circumstances, the governing instrument is the trust deed and not the memorandum and articles of the company.

1.10 In some cases, trustees are effectively self-perpetuating, with future trustees appointed by the present ones. In other cases, the trust deed will specify organisations or agencies which are entitled to nominate one or more trustees, or detail some other procedure by which trustees are identified and appointed. In default of such provision for the appointment of trustees they may be appointed by the court or under existing legislation by the Commissioners of Charitable Donations and Bequests.<sup>13</sup> The trust deed will usually make provision for trustees' meetings and the number of trustees required for a quorum.<sup>14</sup>

1.11 Any contracts entered into by the trustees of a charitable trust are entered into by them personally. Trustees have no limited liability and can therefore be sued in their personal capacity for breach of trust even though acting reasonably and honestly.<sup>15</sup>

1.12 There are no specific provisions in the *Trustee Act 1893* or the *Charities Acts 1961 and 1973* as to the minimum or maximum number of trustees required. Section 56 of the *Charities Act 1961* makes provision for a body corporate to act as sole trustee in certain circumstances. However, for the purposes of granting charitable tax exemption, the Revenue Commissioners specify that there should be a minimum of three trustees, who are not related and the majority of whom must be resident within the State.<sup>16</sup>

1.13 The trust deed will also normally contain provisions governing the distribution of the assets of a charitable trust on termination of the trust. If the trust deed does not contain such provisions a *cy-près*<sup>17</sup> application may have to be made to the Commissioners of Charitable Donations and Bequests under current legislation.

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<sup>13</sup> Section 43 of the *Charities Act 1961* as substituted by section 14 of the *Charities Act 1973*.

<sup>14</sup> If the trust deed is silent on this, then the trustees must act unanimously.

<sup>15</sup> For a full discussion of the liability of trustees see Law Reform Commission, *Consultation Paper on Trust Law – General Proposals* (LRC CP 35-2005), chapter 7.

<sup>16</sup> See Law Reform Commission, *Consultation Paper on Charitable Trust Law – General Proposals* (LRC CP 36-2005), paragraph 1.24.

<sup>17</sup> *Cy-près* means “as near as possible” to the spirit of the original gift. The doctrine allows the High Court, or the Commissioners of Charitable Donations and Bequests to give effect to a donor’s charitable intention where it is impossible or impracticable to give effect to the donor’s wishes in the precise terms intended, for example, where the gift can be better used in conjunction with other property and can suitably, regard being had to the spirit of the original gift, be made applicable to common purposes.

**(2) Advantages**

1.14 The advantages of charitable trusts may be summarised as follows:

- a charitable trust truly reflects that trustees hold property in trust for its charitable purposes;
- a charitable trust is relatively easy to set up and can be an inexpensive option;
- it is suitable for smaller charities;
- the regulatory requirements are minimal.

**(3) Disadvantages**

1.15 The disadvantages of charitable trusts may be summarised as follows:

- trust law is not easily understood and therefore professionals must usually be engaged to assist;
- the trustees of a charitable trust are, to a large extent, confined by the terms of the trust deed and difficulties may arise in relation to the alteration of the trust deed;<sup>18</sup>
- the absence of power to alter the terms of the trust deed may mean that the trustees have to apply to the High Court or the Commissioners of Charitable Donations and Bequests for assistance;
- problems may arise in relation to replacement or removal of trustees;
- any contracts entered into by the trustees are entered into by them personally;
- trustees have no limited liability and may therefore find themselves personally liable on such contracts or for breach of trust;
- breach of trust may arise if trustees fail to discharge the duties of their office or if they act in excess of the authority conferred by the trust deed;
- a trust may be unsuitable for larger organisations holding significant assets and engaging employees;

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<sup>18</sup> Trust deeds are usually stated to be irrevocable and it is difficult at the outset to envisage all of the functions which may be required.

- accountability may be minimal as there is no requirement to make any returns or to have accounts audited;<sup>19</sup>
- on the death of the last trustee it may be necessary to extract a grant of probate to administer the assets of the trust.

## **C Unincorporated Associations**

### **(1) General**

1.16 Apart from charities, many unincorporated associations such as community and social enterprise groups are formed for not-for-profit purposes. It should be noted that this Consultation Paper deals only with unincorporated associations set up for charitable purposes.

1.17 The use of an unincorporated association as a legal structure for charities gained popularity in the 18<sup>th</sup> century with the rise of voluntary societies and reflected the change from individual to associated philanthropy.<sup>20</sup>

1.18 An unincorporated association involves a group of individuals working together towards a common aim. The structure was defined by Slade L.J. in *Re Koepler's Will Trusts*<sup>21</sup> as: “an association of persons bound together by identifiable rules and having an identifiable membership”.

1.19 An unincorporated association is usually subject to a governing instrument in the form of a constitution or a set of rules. The governing instrument is essentially a contractual agreement between the members of the association. The constitution sets out the objects of the association, its membership and structure, and the powers it gives itself to carry out its objects. An unincorporated association does not have a separate legal identity distinct from its members. The members usually nominate or elect a committee to manage the organisation.

1.20 The individuals involved in controlling and managing the administration of a charity through the structure of an unincorporated association are normally referred to as the “governing body”, “management committee”, “committee” or “committee members”.

1.21 The structure is generally two-tier, with the committee accountable to a wider membership. The constitution will generally make provision for the election of a committee, meetings of the committee,

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<sup>19</sup> However, it should be noted that the Revenue Commissioners require audited accounts for those charities which seek tax exemptions.

<sup>20</sup> See Owen, *English Philanthropy 1660-1960* (Harvard University Press, 1965) at 71.

<sup>21</sup> [1985] 2 All ER 869, 874.

quorum and chair. Members will typically hold voting rights at general meetings and will elect all or some of the committee.

1.22 An unincorporated association has no legal personality of its own. The legal title to any property is usually vested in the members or, if there are a large number of members, in the names of some of them. In this instance the term “trustees” or “holding trustees” may be used to describe the members in whose names the property is held. The property is effectively held on a quasi-trust.

1.23 Sometimes the association’s constitution will provide expressly that its assets are to be held on trust for its charitable objects, so that the association combines both the concepts of trusts and contract. However as Luxton points out:

“[e]ven in the absence of an express declaration of trust, it is possible to infer a trust for the association’s purposes in its rules; indeed, in modern times it appears that the assets of every charitable unincorporated association are to be treated as being held on trust, whether express or implied”.<sup>22</sup>

1.24 An unincorporated association does not afford the protection of limited liability to its members. Members are therefore personally liable for their actions including any debts of the association.

1.25 There are no specific provisions as to the minimum or maximum number of members but, for the purposes of granting charitable tax exemption, the Revenue Commissioners specify that there should be a minimum of three officers, who are not related and the majority of whom must be resident within the State.

## **(2) Advantages**

1.26 The advantages of unincorporated associations may be summarised as follows:

- an unincorporated association is relatively easy and inexpensive to set up;
- it is suitable for smaller charities;
- it is suitable for charities where activities are to be carried on in the short term;
- the regulatory requirements are minimal.

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<sup>22</sup> Luxton *The Law of Charities* (Oxford University Press 2001) at 261.

**(3) Disadvantages**

1.27 The disadvantages of unincorporated associations may be summarised as follows:

- the members of an unincorporated association do not have limited liability and may therefore find themselves personally liable for their actions and any debts of the association;
- where the committee members enter into contracts they may be treated as contracting on behalf of all the members or personally as trustees depending on the circumstances;
- liability under contracts will fall on members of the committee, individual members of the association or individual members personally according to the general law of agency;
- an unincorporated association may be unsuitable for larger organisations holding significant assets and engaging employees;
- on the death of a member in whose name the charity property was held, it may be necessary to extract a grant of probate to administer the assets of the charity.
- there is no requirement to make any returns or to have accounts audited.<sup>23</sup>

**D Companies**

**(1) General**

1.28 Companies are established under the *Companies Acts 1963 to 2005*. A company is a separate legal entity with an existence independent from that of its members. There are a number of different types of companies but the structure most commonly used by charities is a company limited by guarantee and not having a share capital.<sup>24</sup> A charity may operate through a company limited by shares but this may not prove satisfactory due to the possibility of change of ownership by way of the transfer of shares.

1.29 In a company limited by guarantee each member guarantees to contribute a specific sum of money, usually a nominal amount, to the company in the event of it being wound-up. The sum is fixed at a nominal amount so there is no possibility of profit by the members by means of

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<sup>23</sup> It should be noted that the Revenue Commissioners require audited accounts from those charities which seek tax exemptions.

<sup>24</sup> 44% of the 6,700 charities granted tax-exempt status by the Revenue Commissioners are constituted as companies limited by guarantee without a share capital.

selling their stake. The maximum liability of the members is the amount of the guarantee.

1.30 In the case of a charity operating through the medium of a company, the governing instruments are the memorandum and articles of association. The memorandum of association sets out the objects of the company which, in the case of a charity, must be exclusively charitable. The articles of association set out the internal rules and regulations of the company.

1.31 The individuals charged with the governance of a charity operating through the structure of a company limited by guarantee are normally referred to as members. This responsibility is then normally vested in the directors or the board of directors of the company who are involved in controlling and managing the administration of the company subject to the overall direction of the members.

1.32 This is essentially a two-tier structure, with the board of directors accountable to a wider membership. Members will typically hold voting rights at general meetings and will elect the directors.

1.33 While technically charitable companies may have a separate membership structure, in many cases the same people are both directors and members. A single-tier structure may be used by simply stating that only directors may be members and vice-versa. Thus, although these two roles will still exist within the company, the same people will perform both. In this situation there is no equivalent of the members (shareholders) to monitor the performance of the directors.

1.34 In the case of charities operating through a company, the provisions of the *Companies Acts 1963 to 2005* apply. Every company must have at least two directors.<sup>25</sup> A body corporate cannot act as a director.<sup>26</sup> Except in certain specified circumstances at least one of the directors must be resident in Ireland.<sup>27</sup> A company limited by guarantee can have unlimited membership but must have a minimum of not less than seven<sup>28</sup> and it must have at least two directors. All companies are required to have a secretary. This person may also be a member or director, but need not be.

1.35 For the purposes of granting charitable tax exemption, the Revenue Commissioners specify that there should be a minimum of three

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<sup>25</sup> Section 174 *Companies Act 1963*.

<sup>26</sup> Section 176 of the 1963 Act.

<sup>27</sup> Section 43 *Companies Amendment (No.2) Act 1999*.

<sup>28</sup> Section 5 *Companies Act 1963*.

directors, who are not related and the majority of whom must be resident within the State.

**(2) Advantages**

1.36 The advantages of using a company structure for charitable activities may be summarised as follows:

- a company structure is suited to larger charities with substantial assets that employ staff;
- incorporation affords the protection of limited liability to its members;
- incorporation facilitates contractual relations with third parties;
- assets can be held in the name of the company as opposed to the names of individuals;
- a company is a separate legal entity from its members and continues in existence despite changes in its membership;
- a company's memorandum and articles of association may be altered;
- a company can bring and defend court proceedings in its own name;
- incorporation of a charity demonstrates that the charity is regulated and accountable to a governing body and is required under statute to keep accounts;
- incorporation may be required as a prerequisite to qualification for certain grants and funding.

**(3) Disadvantages**

1.37 The disadvantages of using a company structure for charitable activities may be summarised as follows:

- in the case of a company, its assets are generally held for the benefit of its shareholders or members. This concept does not sit easily with the ethos of charities which exist to carry out a particular purpose and not for the purposes of making a profit for its members;
- the costs of forming and maintaining a company are generally higher than those associated with other legal forms;
- compliance with the legal requirements of the *Companies Acts 1963 to 2005* can prove onerous in terms of administrative and reporting requirements which are not ideally suited to charities. Companies

are obliged to file an annual return including a profit and loss account and balance sheet,<sup>29</sup>

- companies are subject to regulation by the Office of the Director of Corporate Enforcement;
- incorporation for the purposes of availing of grants and funding may be onerous and costly for smaller charities with very few or no assets;
- because of the regulatory requirements of company law, individuals may be fearful of becoming involved in charitable companies.

1.38 A more practical view of the disadvantages of using the company vehicle can be gleaned from The Wheel's<sup>30</sup> submission to the Company Law Review Group (based on a survey of its members) which noted that:

- groups feel that the duties in complying with company law can bite into time that should be used for their 'core activities';
- groups feel daunted by the paperwork involved. Additional costs associated with preparation and filing of yearly accounts also adds to running costs. The requirement for all submitted accounts to be audited causes groups to have to pay an accountant to prepare the accounts as well as an auditor;
- prospective directors are often frightened by and/or misunderstand their responsibilities. This can make it very difficult to recruit new Board members;
- groups face significant hidden costs in relation to the increasing responsibilities of directors as they need to invest in appropriate training for board members purely so that they know enough to fulfil their legal obligations;
- while groups wishing to avail of the tax-exemption register and can get some help from the Revenue Commissioners in drawing up articles and memoranda, the language is often complex and confusing and professional services and therefore fees are usually required.<sup>31</sup>

1.39 The Commission acknowledges the views advanced by organisations such as the Wheel and notes that the increased responsibility

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<sup>29</sup> But see section 128(4) *Companies Act 1963* and section 2(1) *Companies (Amendment) Act 1986* which provides an exemption for religious charities.

<sup>30</sup> The Wheel is a network of organisations and individuals working in the Community and Voluntary sector.

<sup>31</sup> See [www.wheel.ie](http://www.wheel.ie).

may lead to formulaic compliance with company legislation which may mean that charities miss out on proper regulatory reporting appropriate to a charity.

## **E Other Structures**

1.40 Organisations such as friendly societies and industrial and provident societies may also be used as structures for charities but are more usually used as mutual benefit bodies rather than for the benefit of the public at large.

1.41 Charities may also be formed by Royal Charter or directly by statute.

1.42 A charity can also apply to the Commissioners of Charitable Donations and Bequests to be incorporated,<sup>32</sup> that is, granted separate legal status.

## **F Conclusion**

1.43 There are currently a number of different legal structures available to charities. Such structures are necessary to give effect to the charity's purpose. In the Commission's view a major difficulty is that none of these structures were specifically designed with charities in mind.

1.44 Each of the current legal structures available to charities comes with its own advantages and disadvantages. The main distinction lies between the incorporated (companies) and the unincorporated (trusts and associations) forms of charities. Charitable companies sit somewhat uncomfortably between charity law, based on trust law, and company law which was designed primarily for commercial organisations. On the other hand, incorporation offers the comfort of limited liability which is not available in the case of trusts and unincorporated associations.

1.45 Regardless of which legal structure is chosen it is imperative, in the Commission's view that trustees or officers or directors need to be aware of their legal responsibilities. In many instances, charities hold funds which have been donated by the general public, who have no further scope for monitoring the use of the funds they have given. Many charities also receive substantial tax benefits. For these reasons, it is important that all charities are held accountable and that regulation is applied uniformly regardless of the legal structure used. With the advent of regulation in the form of a Charities Regulator,<sup>33</sup> the issue of legal responsibility will be emphasised. The

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<sup>32</sup> Section 2 *Charities Act 1973*.

<sup>33</sup> See paragraph 2.17 below.

Commission is of the view that, regardless of what format it takes, a Charities Regulator<sup>34</sup> will have an important role to play in educating and informing trustees or officers or directors on their legal responsibilities.

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<sup>34</sup> See paragraph 2.20.



## CHAPTER 2      REGULATION OF EXISTING LEGAL STRUCTURES AND PROPOSALS FOR REFORM

### A            **Current Regulation of Charities**

#### **(1)            *Introduction***

2.01        There is currently no single body in Ireland charged with supervising charities or ensuring their registration. This may be contrasted with the situation in England and Wales where the Charity Commissioners, who were initially established in 1853,<sup>1</sup> oversee the regulation and registration of charities. There are a number of organisations in Ireland which interact with charities and these bodies and their role in relation to charities are discussed in the following paragraphs.

#### **(2)            *Commissioners of Charitable Donations and Bequests***

2.02        The Commissioners of Charitable Donations and Bequests for Ireland, a collegiate body established in the mid-19<sup>th</sup> Century,<sup>2</sup> have a wide role as an enabling body, rather than as a regulatory body with investigative or punitive powers.

2.03        Under the diverse statutory powers currently conferred on the Commissioners by the Oireachtas in the *Charities Acts 1961* and *1973*, they may assist charitable trustees where the trust deed does not provide sufficient powers, for example, by the approval of voluntary dispositions for less than market value, and by the approval of proposed compromises of litigation, and also by giving approvals in respect of the exercise of powers of sale<sup>3</sup> and the application of the proceeds therefrom; and also giving approvals in respect of the exchange of land when for the benefit of the charity. They also have a wide power to frame a *cy-près* scheme (now without a financial

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<sup>1</sup> Commissioners were appointed on an *ad hoc* basis to inquire into impropriety in the administration of charities under the *Statute of Charitable Uses 1601*. That practice died out in 1803. The Charity Commissioners were established on a permanent basis by the *Charitable Trusts Act 1853*. The Commissioners functions and powers are now contained in the *Charities Act 1993*.

<sup>2</sup> The Commissioners of Charitable Donations and Bequests were originally established under the *Charitable Donations and Bequests (Ireland) Act 1844*.

<sup>3</sup> A total of 141 sales were sanctioned in 2004: see *Annual Report of the Commissioners of Charitable Donations and Bequests for Ireland 2004*.

ceiling),<sup>4</sup> thus giving a means at minimal cost of applying a gift to an alternative charitable purpose. This function was exercised more usually by the courts until 1961.

2.04 They are also empowered to approve a scheme for the establishment of a common investment fund for charities<sup>5</sup>, which has been done and is of benefit to many small charities with limited funds. They may also give trustees advice on difficult charity problems and, where trustees act on this advice and in good faith, the trustees are personally indemnified.<sup>6</sup> The Commissioners may certify certain charity cases to the Attorney General for his attention as the protector of charities.<sup>7</sup> The Commissioners also have a role in relation to the appointment of trustees,<sup>8</sup> suing for the recovery of charitable gifts,<sup>9</sup> directing the institution of legal proceedings<sup>10</sup> and applying for conduct of administration suits and suits for carrying out trusts of wills in case of delay.<sup>11</sup>

### **(3) Revenue Commissioners**

2.05 The Revenue Commissioners have a role in establishing a charity's entitlement to certain tax exemptions under the Taxes Acts.<sup>12</sup> The Revenue Commissioners determine applications for tax exemptions and maintain a list of organisations which have been granted exemption from tax.<sup>13</sup> Each charity which is granted approval is allocated a specific charity reference number (a CHY number).

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<sup>4</sup> See section 16 and Part 2 of the Schedule to the *Social Welfare (Miscellaneous Provisions) Act 2002*, which repealed the previous financial ceiling on the Commissioners' powers in *cy-près* schemes. This ceiling had been progressively increased over the previous 50 years by the Oireachtas. A total of 40 *cy-près* schemes were dealt with during 2004, of which 10 were sealed.

<sup>5</sup> Section 46 *Charities Act 1961*. The Common Investment Fund was established in April 1985 under a scheme pursuant to section 46.

<sup>6</sup> Section 21 *Charities Act 1961*. 7 such cases were dealt with and sealed in 2004.

<sup>7</sup> Section 26 *Charities Act 1961*.

<sup>8</sup> Section 43 *Charities Act 1961* as amended by section 14 *Charities Act 1973*. 68 such orders were made during 2004.

<sup>9</sup> Sections 23 and 24 *Charities Act 1961*.

<sup>10</sup> Section 25 *Charities Act 1961*.

<sup>11</sup> Section 27 *Charities Act 1961*.

<sup>12</sup> *Taxes Consolidation Act 1997*, *Stamp Duty Consolidation Act 1999* and *Capital Acquisitions Tax Consolidation Act 2003*.

<sup>13</sup> At present a total of 6,689 bodies have been granted charitable tax exemption by the Revenue Commissioners.

2.06 The Revenue Commissioners do not regulate the activities of charities. However, tax exemption<sup>14</sup> may be withdrawn (retrospectively if necessary) where the charity does not comply with its charitable objects or the conditions associated with the tax exemption.

2.07 A charity wishing to apply for tax exemption must submit a copy of its governing instrument to the Revenue Commissioners and identify the charitable activity in which it is involved. The charity must furnish a statement of its activities to date and its proposed activities referring to the objects or purposes set out in its governing instrument. Financial statements including a statement of income and expenditure and a statement of assets and liabilities must be furnished. Where the annual income exceeds €50,000, the accounts must be audited. The Revenue Commissioners also stipulate that there should be a minimum of three officers or trustees or directors and that the officers or trustees or directors shall not receive any remuneration. On the winding up of the trust, association or company any remaining property must be transferred to some other charitable institution having similar main objects.

**(4) Registrar of Companies**

2.08 All companies, including charitable companies, are obliged to register with the Companies Office. A company is subject to rules such as the keeping of a register of members and directors, annual general meetings, minutes of meetings, annual returns and notification of any alteration to its memorandum or articles of association, directors or secretary or in the name of the company.

2.09 Companies limited by guarantee without a share capital must file an annual return with the Register of Companies each year. These companies do not qualify for audit exemption nor do they qualify to file abridged accounts. They must file full accounts, director's report and an auditor's report. They are also required to hold an annual general meeting each year.

2.10 The normal requirement to file annual accounts with the Companies Office does not apply to "a company, not having a share capital, which is formed for an object that is charitable and is under the control of a religion recognised by the State under Article 44 of the Constitution, and which exercises its functions in accordance with the laws, canons and ordinances of the religion concerned".<sup>15</sup>

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<sup>14</sup> Including exemption from income tax, corporation tax, capital acquisitions tax, capital gains tax or stamp duty.

<sup>15</sup> Section 128(4) *Companies Act 1963* and section 2(1) *Companies (Amendment) Act 1986*.

**(5) Director of Corporate Enforcement**

2.11 The Director of Corporate Enforcement also has a role where a charity operates as a company. The investigative and enforcement role of the Director is quite extensive. The Director's main legal powers arise in the following areas:

- the initiation of fact-finding company investigations;
- the prosecution of persons for suspected breaches of the *Companies Acts 1963 to 2005*;
- the supervision of companies in official and voluntary liquidation and of unliquidated insolvent companies;
- the restriction and disqualification of directors and other company officers;
- the supervision of liquidators and receivers and
- the regulation of undischarged bankrupts acting as company officers.

2.12 The Director also has a role in encouraging compliance with company law.

**(6) Attorney General**

2.13 The Attorney General has a role as the protector of charities. The Attorney General may bring proceedings in defence of charities and also has a role when proceedings are brought against charities. He is required to be notified of any proceedings and may be joined to represent the interests of beneficiaries or the public interest.

**(7) Valuation Office**

2.14 The Valuation Office has a role in establishing a charity's eligibility for rates exemption on charitable grounds.

**(8) Garda Síochána**

2.15 The Gardaí investigate any breaches of criminal law by charities and also have a role in authorising collection permits under the *Street and House to House Collections Act 1962*. Authorisation is obtained from the Garda Chief Superintendent for the locality in which the collection is to take place. A Chief Superintendent may refuse to grant a collection permit<sup>16</sup> or

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<sup>16</sup> For example if he or she is of the opinion that the proceeds of the collection would benefit an unlawful object, an object contrary to public morality or benefit an illegal operation.

may attach conditions<sup>17</sup> to the permit. In practice however very few applications are refused.

**(9) Common Law / Statutory Provisions**

2.16 Charitable trusts are governed and regulated by general trust law, unincorporated associations are generally subject to contract law and charities operating through a company are subject to the *Companies Acts 1963 to 2005*. The principal legislation governing charities is contained in:

- the *Trustee Acts 1893 and 1931*;
- the *Trustee (Authorised Investments) Act 1958*;
- the *Charities Acts 1961 to 1973*.<sup>18</sup>

**B Proposals for a New Regulatory Body**

2.17 In December 2003, the Department of Community, Rural and Gaeltacht Affairs published a consultation paper entitled *Establishing a Modern Statutory Framework for Charities*. This was followed by the publication of a *Report on the Public Consultation* in September 2004.<sup>19</sup> The Department's consultation paper proposes a new independent statutory body for the regulation of charities.<sup>20</sup> It is envisaged that the statutory functions of the regulatory body might include:

- determining charitable status (with a right of appeal to the High Court);
- maintaining a register of charities;
- ensuring the public accountability of charities;
- regulating and monitoring of charities, including their fund-raising activities, on an ongoing basis including where necessary enforcing compliance with charities legislation and in relation to charitable fund-raising activities;
- providing authoritative guidance to trustees and directors of charities, particularly in relation to compliance with registration, other legal requirements and good practice generally;

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<sup>17</sup> For example limiting the areas where the collection may be held or limiting the number of collectors.

<sup>18</sup> As amended by the *Courts and Court Officers Act 1995* and the *Social Welfare (Miscellaneous Provisions) Act 2002*.

<sup>19</sup> Both papers are available from the Department's website [www.pobail.ie/en/CharitiesRegulation/](http://www.pobail.ie/en/CharitiesRegulation/).

<sup>20</sup> *Establishing a Modern Statutory Framework for Charities* at 9.

- protecting the public interest by monitoring and investigating possible abuses (including in relation to charitable fund-raising activities);
- advising the Minister on charity legislation, its own functions, and on matters relating to charity generally; and informing the public as appropriate or necessary;
- determining *cy-près* applications (that is, by ensuring that all charitable donations, whether willed or otherwise, are applied to charitable ends, even where the original charity no longer exists or the aims of the charity have been changed);
- issuing Codes of Conduct, Best Practice Guidelines and model Constitution documents;
- receiving notifications of charitable bequests and follow-up monitoring as appropriate;
- issuing performance reports on areas of the charities sector.<sup>21</sup>

2.18 If these proposals are implemented in legislation, Ireland would have a regulatory body charged with supervising charities and ensuring their registration. In the case of companies registered under the Companies Acts, it is as yet unclear how the role of a Charities Regulator would be reconciled with that of the Registrar of Companies and the Director of Corporate Enforcement who currently regulate the activities of charitable companies.

2.19 A formal decision on the format of the new regulatory body has not yet been taken but, in a response to a number of parliamentary questions, the Minister for State at the Department of Community, Rural and Gaeltacht Affairs, Mr. Noel Ahern T.D. stated that:

“The new legislation will introduce an integrated system of mandatory registration, proportionate regulation and supervision. The independent regulatory body, to be positioned as the centrepiece of the regulatory regime, will be charged with setting up and maintaining a register of charities.”<sup>22</sup>

2.20 The Minister also indicated that a Bill to give effect to this proposal is likely to be published in 2006. The Commission would welcome the establishment of such a regulatory framework whatever its precise form. In the absence of a decision on the format of the proposed regulatory body, for the purposes of this Consultation Paper, the proposed new regulatory body is referred to as “the Charities Regulator”.

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<sup>21</sup> *Establishing a Modern Statutory Framework for Charities* at 10.

<sup>22</sup> Volume 16 *Dáil Debates* col. 1166 (26 October 2005).

## **C Conclusion**

2.21 As can be seen from the above discussion, while there is currently no regulatory body governing charities in Ireland, there exists a myriad of organisations with which charities regularly interact. The advent of a new regulatory body provides an ideal opportunity to integrate some of the functions currently carried out by the existing bodies and to streamline procedural requirements for charities. The development of a new legal structure for charities must be seen as an integral part of the reform process. A separate new structure would provide an opportunity to streamline the registration and regulation of charities so that all charities regardless of their legal status would be subject to the same form of regulation. This issue will be discussed further in Chapter 4.



## CHAPTER 3 OTHER JURISDICTIONS

### A Introduction

3.01 The existing forms of legal structures used by charities in Ireland, as outlined in Chapter 1, are almost identical to those currently used in other common law jurisdictions, most notably in England and Wales and in Scotland. Following some major studies, reports and extensive consultation processes, each of those jurisdictions has decided to introduce a new legal structure for charities. More recently, in Northern Ireland, a consultation paper issued by the Charities Branch Voluntary and Community Unit of the Department for Social Development also proposes a new type of organisation for charities.<sup>1</sup>

3.02 In considering the need or appropriateness of a new legal structure for Irish charities it is helpful to review the developments which led these other jurisdictions to introduce a new legal structure for charities and to consider the format proposed for these new structures.

### B England and Wales

#### (1) Overview

3.03 It should be noted that, unlike the situation pertaining in Ireland, charities in England and Wales have been subject to regulation by the Charity Commissioners for many years. The Charity Commissioners were initially established in 1853 and their functions and powers are now contained in the *Charities Act 1993*. The Charity Commission carries out supervisory, policing and advisory functions. It maintains a register of charities which is open to public inspection. All charities, including charitable companies, are subject to regulation by the Charity Commission.

3.04 The recommendation for a new legal form specifically for charities arose from the Department for Trade and Industry's Company Law Review.<sup>2</sup> In its earlier consultation, the Department had stated:

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<sup>1</sup> *Consultation on the Review of Charities Administration and Legislation in Northern Ireland in 2005* see [www.dsdni.gov.uk/charities\\_consultation.doc](http://www.dsdni.gov.uk/charities_consultation.doc).

<sup>2</sup> *Modern Company Law for a Competitive Economy: Final Report* 26 July 2001, paragraphs 4.63 ff.

“We believe that there is advantage in having a separate vehicle for charitable companies which would be more specifically attuned to their needs and to the public policy interest in the regulation of charities as well as removing the burden of dual registration and reporting.”<sup>3</sup>

3.05 In its response to the proposal for a new legal structure, the Charity Law Association summed up the position by stating that:

“What is missing at present, as the research has shown, is a form of incorporated charity with limited liability for its trustees which is simple and inexpensive to administer and subject to the supervisory jurisdiction only of the Charity Commission and the court.”<sup>4</sup>

3.06 The proposal for a Charitable Incorporated Organisation (CIO) was subsequently developed by an advisory group set up by the Charity Commission. The report from the advisory group<sup>5</sup> recommended the following basic requirements for CIOs:

- the legislation should provide for a new form of legal entity to be known as a charitable incorporated organisation (CIO);
- it should provide for the CIO to be a body corporate (with legal personality separate from that of its members) which is formed by being incorporated under the legislation and which may sue or be sued in its own registered name;
- the members liability should be limited to the making of a contribution to the settlement of the liabilities of the CIO in the event of its being wound up, in the amount of the guarantee (if any) contained in the constitution of the CIO;
- the new structure should not be mandatory.

3.07 A comprehensive review of the legal and regulatory framework governing charities and other not-for-profit organisations was subsequently published in September 2002. The report *Private Action, Public Benefit*, prepared by the Prime Minister’s Strategy Unit, made a series of recommendations intended to modernise charity law, including

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<sup>3</sup> *Modern Company Law for a Competitive Economy: Developing the Framework* March 2000 at 9.19.

<sup>4</sup> Charity Law Association Response to the DTI proposals for a new Charitable Vehicle, July 2000.

<sup>5</sup> *Charitable Incorporated Organisation – Report from the Advisory Group to the Charity Commission*, Spring 2001.

recommendations aimed at improving the range of available legal forms enabling organisations to be more effective.

3.08 Following an extensive consultation process, in July 2003, the Government published its response to the Strategy Unit's proposals – *Charities and Not-for-Profits: A Modern Legal Framework*.<sup>6</sup> In its response, the Government accepted most of the main recommendations in the report. Amongst the recommendations accepted was one in relation to the creation of a separate legal form for charities.

3.09 The *Charities Bill 2004* was introduced into the House of Lords on 20 December 2004<sup>7</sup> to give effect to many of the proposals including those made by the Company Law Review Group. For the purposes of this paper only the proposals relating to the introduction of a new legal form for charitable organisations, the Charitable Incorporated Organisation (CIO), will be considered. These provisions are discussed in detail at 3.17 below.

## **(2) *Private Action, Public Benefit***

3.10 The report *Private Action, Public Benefit* noted that there were no corporate forms designed to meet the specific needs of charities. It then listed the difficulties which this may cause:

- Charitable companies face a burden of dual registration, regulation and reporting between the Charity Commission and Companies House;
- The company corporate governance regime is not tailored to fit the trustee governance structure;
- The role for members of a company limited by guarantee is based on the underlying assumption of a financial interest in the company, which is not the case for charities;
- Anyone who is a board member of a charitable company is both a company director and a charity trustee. It is unclear exactly how the duties imposed on directors by company law overlap with the duties imposed on trustees by charity law and, where there is a conflict, which takes precedence;
- The company limited by guarantee is unwieldy for charities in which the directors are the same people as the members since they

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<sup>6</sup> See <http://www.homeoffice.gov.uk/>.

<sup>7</sup> The *Charities Bill 2004* has passed through the House of Lords and and at the time of writing is under consideration in the House of Commons.

have to make some decisions in one capacity and other decisions in the other capacity.<sup>8</sup>

3.11 The report then went on to recommend:

“That a new legal form designed specifically for charities, the Charitable Incorporated Organisation (CIO), be introduced, which will only be available to charitable organisations.”<sup>9</sup>

3.12 The report outlined the main characteristics of the CIO as follows:

- Incorporated legal form;
- Members’ liability limited;
- Foundation and membership formats, so that it is appropriate for charities with and without a membership structure;
- Flexible administrative powers, to reflect the diversity of the sector in terms of size and purpose;
- Model constitutions prepared by co-ordinating bodies, tailor-made for particular parts of the sector;
- Requirement for constitutions to be complete and written in plain English;
- Explicit statement of trustees’ duty of care, consistent with the *Trustee Act 2000*;
- Default provisions for new and existing charities to convert to a CIO by special resolution or by unanimous written resolution;
- Transfer mechanisms to ease conversion from other incorporated forms.

3.13 The report recommended that, to begin with the CIO should be an additional legal form for charities but that the Government should consider, three years after the introduction of the CIO, whether or not other corporate forms should continue to be available for charities.

3.14 Following the publication of the report *Private Action, Public Benefit*, the UK Government sought the views of organisations and people interested in the law and regulation of not-for-profit organisations through an open public consultation. There were 1,087 responses from people and organisations including 124 from umbrella bodies including, for example,

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<sup>8</sup> *Private Action, Public Benefit* at 57. The proposal for a CIO was originally made by the Department of Trade and Industry’s *Modern Company Law for a Competitive Economy: Final Report 2001*, para. 4.63 ff.

<sup>9</sup> *Ibid* at 58.

the National Council for Voluntary Organisations (NCVO).<sup>10</sup> Organisations such as the Charity Law Association<sup>11</sup> also gave detailed responses.

**(3) Charities and Not-for-Profits: A Modern Legal Framework**

3.15 The UK Government's response *Charities and Not-for-Profits: A Modern Legal Framework* noted that there was a high degree of support for the proposal on a new legal form for charities. However, many respondents believed that the three year review period was too short to allow a proper assessment of the CIO's prospects. There was also significant support for the view that the CIO form should be an addition to the existing range of forms, not a replacement for any of them. In other words, that it should not become the compulsory form for charities wanting to establish themselves in a corporate form.

3.16 The Government accepted the recommendation that a new legal form be introduced for charities and indicated that it would include provisions for the introduction of the CIO in its Charities Bill. It proposed to review the need for other legal forms five years after the introduction of the CIO.

**(4) Charities Bill 2004**

3.17 Clause 34 and Schedule 7 of the *Charities Bill 2004* make provision for a CIO. The CIO is the first legal form to be created specifically to meet the needs of charities. Its purpose is to avoid the need for charities that wish to benefit from incorporation to register as companies and be liable to dual regulation by Companies House as well as the Charity Commission.

3.18 The Bill contains provisions dealing with:

- the nature and constitution of the CIO;
- its registration as a charity;
- the conversion of a charitable company or registered industrial and provident society into a CIO;
- the amalgamation of CIOs, the transfer of a CIO's property, rights and liabilities to another CIO;
- the Secretary of State's power to make regulations about the winding up, insolvency and dissolution of CIOs, and about their administration.

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<sup>10</sup> The NCVO is the umbrella body for the voluntary sector in England.

<sup>11</sup> This Association currently has over 760 members including many of the UK's largest charities and most leading charity lawyers.

3.19 The main features are as follows:

- a CIO must be a body corporate with a constitution (in a specified form) and one or more members with no or limited liability;
- any one or more persons may apply to the Charity Commission for a CIO to be constituted and registered as a charity;
- a charitable company or a registered industrial and provident society (except for a company or society which has a share capital not fully paid up, or which is an exempt charity) may apply to the Charity Commission for conversion to a CIO;
- two or more CIOs may apply to the Charity Commission to be amalgamated;
- one CIO may, subject to approval by the Charity Commission, transfer all its properties, rights and liabilities to another;
- the Secretary of State may make regulations about the winding up, insolvency, dissolution, and revival and restoration to the register following dissolution, of CIOs.

3.20 There are further provisions:

- that a CIO may do anything which is calculated to further its purposes and gives the CIO's charity trustees the responsibility of managing its affairs;
- concerning the validity of acts done by the CIO and provide that, in general but with some limitations, the validity of those acts may not be called into question on the ground that the CIO lacked constitutional capacity;
- that require members of a CIO and CIO charity trustees, subject to regulations made by the Secretary of State, to act in the way most likely to further the purposes of the CIO and, in the case of trustees, to exercise reasonable care and skill;
- that prevent CIO charity trustees from benefiting personally in certain circumstances from arrangements or transactions entered into by the CIO;
- that allow a CIO to amend its constitution and specifies the circumstances in which it may do so. The CIO must send the Charity Commission a copy of the amendment and the Commission may refuse to register it in certain circumstances.

3.21 At the time of writing the *Charities Bill 2004* has been passed by the House of Lords and is currently under consideration in the House of Commons.

## **C Scotland**

3.22 In Scotland, charity law was, until recently, governed by the *Law Reform (Miscellaneous Provisions) (Scotland) Act 1990*.

3.23 Since the enactment of the 1990 Act there were a number of reviews of charity law in Scotland culminating in the Scottish Charity Law Review Commission's Report (the Mc Fadden Report) in 2001.<sup>12</sup> As in the UK, this report recommended, *inter alia*, the introduction of a new form of incorporation for charities called Charitable Incorporated Organisations (CIO's). The report recommended that the CIO should be optional for charities and that existing charities incorporated under other regimes should have the option to convert to the new structure.

3.24 A lengthy public consultation process took place on the proposals regarding charities. There were 201 responses to the consultation. Respondents represented a broad range of organisations. The responses came mainly from local and national charitable organisations, churches, professional associations and interested individuals, with smaller numbers from public bodies and various umbrella organisations<sup>13</sup>, including professionals, lawyers and chartered accountants.

3.25 Following the consultation process, the *Charities and Trustee Investment (Scotland) Act 2005* was enacted on 14 July 2005.<sup>14</sup> The 2005 Act contains provisions for Scottish Charitable Incorporated Organisations (SCIOs). These provisions are similar to the proposals for a Charitable Incorporated Organisation (CIO) to be introduced in England and Wales. The SCIOs are an optional new structure and will be regulated by the Office of the Scottish Charity Regulator (OSCR).

3.26 The main provisions regarding SCIOs are as follows:

- a SCIO must be a corporate body with a constitution with more than one member;

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<sup>12</sup> *Charity Scotland – The Report of Scottish Charity Law Review Commission*, May 2001.

<sup>13</sup> Including the Scottish Council of Voluntary Organisations.

<sup>14</sup> Before the main provisions of the Act can come into force there are several preparatory steps to be taken, including a section 104 order under the *Scotland Act 1998*. It is intended that the order will be approved by the UK Parliament and come into force in February 2006.

- the members of a SCIO will have no liability to contribute to the assets if it is wound up;
- the SCIO must apply for registration to the Charity Register;
- a charity that is a company or an industrial and provident (or friendly) society may apply for conversion to a SCIO;
- the OSCR will consider the application for conversion and may only allow conversion if the charity when converted can continue to meet the charity test;
- a number of SCIOs can amalgamate with the consent of the OSCR;
- a third party dealing with a SCIO is entitled to assume that the SCIO has sufficient powers under its constitution to act in the way it is attempting or proposing to act.
- the Scottish Ministers may make regulations setting out further provisions on SCIOs.

## **D Northern Ireland**

3.27 In Northern Ireland, the Charities Branch Voluntary & Community Unit of the Department for Social Development has recently published a *Consultation on the Review of Charities Administration and Legislation in Northern Ireland in 2005*.<sup>15</sup>

3.28 The Department proposes to set up a new type of organisation, equivalent to the Charitable Incorporated Organisation (CIO) to be introduced in England and Wales. This would be similar in some ways to a limited company but would not need to be formally constituted as such, and would have the following characteristics:

- it would have legal personality;
- it would protect trustees from personal liability for the charity's debts;
- it would avoid the disadvantage of dual regulation under both company and charity law;
- it would have to be established for charitable purposes;

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<sup>15</sup> See [http://www.dsdni.gov.uk/charities\\_consultation.doc](http://www.dsdni.gov.uk/charities_consultation.doc).

- it would be able to change its purposes as long as the new purposes remained charitable and the Northern Ireland Charity Commission<sup>16</sup> consented to the change;
- it would have to apply its income only for charitable purposes;
- on winding up, all its assets would have to be applied for appropriate alternative charitable purposes;
- it would have to be registered by the Northern Ireland Charity Commission in the register of charities before it could become a CIO;
- it would be regulated by the Northern Ireland Charity Commission;
- an existing charitable company could convert easily to CIO form, without having to make any change to its purposes.

## **E The European Dimension**

3.29 The importance to the European economy and society of co-operatives, mutual societies, associations, foundations and social enterprises (which together are sometimes referred to as the social economy) is now receiving greater recognition in Member States and at European level. A draft proposal for a Regulation on the Statute for a European Association (EA)<sup>17</sup> has been advanced to enable associations to take advantage of the single market in the same way as companies can. Once constituted, it is proposed that an EA may carry out any activity necessary for the achievement of its aims in a Member State, whilst remaining subject to local legal and administrative rules governing the conditions under which the activity in question may be exercised. It is hoped that the EA would simplify the rules for organisations that operate across borders and eliminate administrative difficulties in relation to cross border transactions.

3.30 The European Commission has also emphasised the need for higher standards of transparency and accountability on the part of non-profit organisations. It is particularly concerned about the vulnerability of the non-profit sector to terrorist financing and other criminal abuse. The

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<sup>16</sup> The Department proposes that a Northern Ireland Charity Commission should be established to operate the Northern Ireland Register of Charities and act as a charities regulator for all charities operating in Northern Ireland.

<sup>17</sup> In 1992 the Commission presented 3 proposals for Statutes for the creation of a European Co-operative, European Mutual Society and European Association (Official Journal no. C 99 of 21/04/92). They were amended in 1993 in the light of opinions of the Parliament and Economic and Social Committee (OJ no. C 236 of 31/08/93, pp. 1-56). The Statute for a European Association is currently under discussion in the European Council working groups.

Commission has issued a *Draft Recommendation to Member States regarding a Code of Conduct for Non-Profit Organisations* to promote transparency and accountability best practices.<sup>18</sup> The recommendation is designed to implement the Financial Action Task Force Recommendation VIII in relation to non-profit organisations. This recommendation states that countries should review the adequacy of laws and regulations that relate to entities that can be abused for the financing of terrorism. Non-profit organisations are particularly vulnerable, and countries should ensure that they cannot be misused:

- by terrorist organisations posing as legitimate entities;
- to exploit legitimate entities as conduits for terrorist financing, including for the purpose of escaping asset freezing measures; and
- to conceal or obscure the clandestine diversion of funds intended for legitimate purposes to terrorist organisations.

3.31 Apart from these developments, it should be noted that there are continuing doubts about whether EU Company Law Directives apply to charitable companies or might do so in the future.<sup>19</sup> Article 48 of the EC Treaty provides that Company Law Directives should not apply to not-for-profit bodies, but there is unresolved ambiguity about whether not-for-profit bodies, incorporated under a regime which also allows for the incorporation of commercial bodies, and has no lock on their re-constituting as commercial bodies, are exempt from the provisions of Company Law Directives. These type of ambiguities lend further support to the need for a separate legal structure for charities.

## **F Conclusion**

3.32 While developments in Northern Ireland are at an early stage, it is clear that in England and Wales and in Scotland the need for a separate legal structure for charities has been on the agenda for a number of years and has been the subject of extensive consultation and legislative action which will lead to a new legal structure specifically for charities. The involvement of charities themselves in this process should be noted. For example, the members of the advisory group to the Charity Commission in relation to the proposals for a CIO were drawn from charities, umbrella bodies and professional bodies advising charities and with a wide experience of the charity sector.

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<sup>18</sup> European Commission 22 July 2005.

<sup>19</sup> See *Private Action, Public Benefit: Charitable Incorporated Organisation* Prime Minister's Strategy Unit September 2002.

3.33 As noted above, an overwhelming number of the respondents to the public consultations welcomed the proposals in relation to the CIO. This is obviously evidenced by the fact that both jurisdictions have seen fit to make provision for CIOs in their recent enacted legislation.

3.34 Given that the existing legal structures being used by charities in Ireland are similar to those in England and Scotland, the experience and developments in those jurisdictions has to carry weight and be of some assistance in informing the current Irish position. The need for a similar type structure in Ireland will be considered in detail in Chapter 4.



## CHAPTER 4 THE NEED FOR A NEW LEGAL STRUCTURE FOR CHARITIES IN IRELAND

### A Introduction

4.01 As noted earlier, there is no legal structure specifically designed to cater for charities. Having looked at the existing legal structures for charities, the advantages and disadvantages associated with each and the current and proposed regulatory frameworks, the question arises as to whether there is there any real need for a new legal structure for charities operating in Ireland.

### B Previous Studies of Charity Law in Ireland

4.02 A number of studies and reports have already been undertaken in relation to charity law in Ireland. While none of these studies focused exclusively on the issue of legal structures for charities, many contain useful insights and suggestions into the topic which are summarised hereunder.

#### (1) *The White Paper*

4.03 The *White Paper on a Framework for Supporting Voluntary Activity and for Developing the Relationship between the State and the Community and Voluntary Sector*<sup>1</sup> published by the Government in 2000 contained a wide range of practical measures to ensure better support for community and voluntary groups. This paper stated that:

“It is strongly recommended that Community and Voluntary organisations should adopt an appropriate legal framework; in most cases this will – under the legal arrangements at present available – involve registering as companies limited by guarantee. For this purpose it is proposed that the Companies Office would provide guidelines for registration.

In this regard the Government accepts the need for a more modern legal framework of law governing the sector. It welcomes the review of charity legislation being carried out at present by the

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<sup>1</sup> Published in September 2000. This paper was preceded by: *Supporting Voluntary Activity: A Green Paper on the Community and Voluntary Sector and its Relationship with the State* published in 1997.

Law Society and looks forward to publication of that report in due course ...”

*Tipping the Balance*<sup>2</sup> was a response by the voluntary sector to the White Paper. It noted that:

“It is acknowledged that many volunteers now work in a management role with responsibilities as employers and financial managers. There can be a fear of the legal responsibilities involved, especially for directors.”

**(2) *Charity Law: The case for reform***

4.04 The Law Society’s Report *Charity Law: The case for reform*<sup>3</sup> published in 2002 (and mentioned in the Government’s White Paper) represented a comprehensive review of charity law in Ireland. In its review of the legal structures for charitable organisations,<sup>4</sup> it summarised the discussions in the UK over the previous decade on the question of a new incorporated structure for charities including the consultation paper in 2000 from the Department of Trade and Industry (DTI) Company Law Review Steering Group, that there should be a new corporate structure for charities.<sup>5</sup>

4.05 The report indicated that there was an advantage in having a separate vehicle for charities, which would be more specifically attuned to their needs and to the public policy interest of charities, as well as removing the burden of dual registration and regulation.

4.06 The report recommended that the proposals of the DTI be considered, notably:

- that a new form of incorporation called Charitable Incorporated Organisation (CIO) should be made available to Irish charities;
- that the CIO should be restricted to charities, and
- that the CIO should be optional not mandatory for charities.

4.07 It also recommended that the proposals of the UK Charity Commission in relation to CIOs be considered, specifically as those proposals had been made as a result of their experience and consultation with the charity sector and added that any development of a new legal structure for charities along these lines should take into account developments in the UK and the wider European Community.

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<sup>2</sup> *Report of the National Committee on Volunteering* – October 2002.

<sup>3</sup> *Charity Law - The case for reform*, Law Society of Ireland, July 2002.

<sup>4</sup> *Ibid*, Chapter 4.

<sup>5</sup> See paragraph 3.04, above.

4.08 In formulating its proposals it is clear that the Law Society consulted widely with charities and also drew on the experiences of the legal profession in dealing with charities over the years.

**(3) Company Law Review Group**

4.09 In its review of company law<sup>6</sup>, the Company Law Review Group (CLRG) recommended, *inter alia*, that there would be “a new legal vehicle for bodies wishing to maintain clearly identified objects – they would become known as designated activity companies (DACs)”

4.10 The Wheel<sup>7</sup> has made a submission to the CLRG suggesting that:

“There is a need for a wider examination of the existing legal entities Charities and Community/Voluntary Groups operate under. The Wheel would welcome a submission by the CLRG to the Department of Community, Rural, and Gaeltacht affairs encouraging it to avail of the learnings from best international practise in this area.”

4.11 The Company Law Review Group’s work on a new *Companies Bill* is ongoing and its proposals in relation to DACs are not yet known. However, it is clear that the DACs will come within the remit of the *Companies Acts* regulatory system.

**(4) Establishing a Modern Statutory Framework for Charities**

4.12 In 2003, the Department of Community, Rural and Gaeltacht Affairs issued a public consultation on the modernisation of charity law.<sup>8</sup> In relation to a new form of incorporation for charities the paper stated that:

“ ... there could now be a window of opportunity for the charities sector to liaise with the Department of Enterprise, Trade and Employment in the development of a new legal structure for charities and designed with their requirements in mind: That Department has begun work on the preparation of legislation in response to the recommendations in the 2002 *Company Law Review Group* report.”

The Group recommended, *inter alia*, that there would be a new legal vehicle for bodies wishing to maintain clearly identified objects – they would become known as designated activity

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<sup>6</sup> *Company Law Review Group Second Report 2002-2003.*

<sup>7</sup> The Wheel is a network of organisations and individuals working in the Community and Voluntary sector.

<sup>8</sup> *Establishing a Modern Statutory Framework for Charities* Department of Community, Rural and Gaeltacht Affairs, December 2003.

companies (DACs). It might be possible for a special form of DAC – a charitable designated activity company (CDAC) – to be created specifically and exclusively for charities; and existing charities could have the option of converting to this new legal structure.”<sup>9</sup>

4.13 Out of a total of 85 submissions, including a number of joint submissions, received by the Department in response to the public consultation, 11 contained reference to the question of a legal structure for charities.

4.14 The external Report on the public consultation<sup>10</sup>, which was published by the Department of Community, Rural and Gaeltacht Affairs in September 2004, addressed comments made in submissions on the question of a CDAC as follows:

“The submissions received voiced strong support for the incorporation into company law reform legislation, currently under review by the Department of Enterprise, Trade and Employment, of a legal vehicle tailored to the specific needs of the charity sector.”<sup>11</sup> As to how concrete effect could be given to this support, in terms of shaping the content of this legislation, a number of respondents felt that the Department or Caradas [a suggested name for the Charities Regulator] should lead the way on the development of the CDAC on behalf of the charity sector. One rationale offered for this viewpoint was that, given the absence of a representative sectoral voice, the sector lacked the capacity to avail of the window of opportunity now existing to engage with the Department of Enterprise, Trade and Employment. Other respondents made a similar request of the Department but were silent as to their reasons.”

4.15 The report noted that:

“There was broad consensus on the Consultation Paper’s proposal to avoid dual reporting obligations for registered charities. However, opinions diverged on how this objective could be best achieved. Some respondents considered that the Companies Registration Office should continue to receive charitable company annual returns, which Caradas [a suggested name for the Charities Regulator] would then recognise as satisfying its standards

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<sup>9</sup> *Establishing a Modern Statutory Framework for Charities*, p 17.

<sup>10</sup> Department of Community, Rural and Gaeltacht Affairs, September 2004.

<sup>11</sup> At Appendix 5, Issues raised in submissions falling within the Statutory Functions of Other Government Departments, p 37. (Both the Consultation Paper and the External Report are available at <http://www.pobail.ie/en/CharitiesRegulation/>)

without requiring further filing by charities; others believed it would be better for Caradas to be the lead body with regard to all charity returns such that submission to Caradas would fulfil the requirements of the Companies Registration Office as regards the filing of returns.”<sup>12</sup>

4.16 CORI<sup>13</sup> offered the following proposals regarding the new legal structure for charities, to the effect that it should:

- be a corporate body, with separate legal personality distinct from its members;
- provide limited liability for those running and involved in the charity;
- remove the burden of dual registration and regulation with the Companies office, the Revenue Commissioners and the proposed Charities Regulator;
- provide a cheap and efficient mechanism to allow charitable companies limited by guarantee convert to this new legal structure by special resolution of its members.

4.17 In its response to the Department, PLANET<sup>14</sup> stated that:

“Many groups have to go down the road of becoming a company limited by guarantee with all the necessary paperwork to go with it. Many individuals involved, do not have the time or capacity to fulfil the requirements needed. There has to be a simple legal and administrative structure for voluntary groups to work within that would fulfil the objectives of the state’s concerns but also those of the charity/voluntary body.”<sup>15</sup>

4.18 FLAC<sup>16</sup> agreed that the establishment of a new form of incorporation solely for charities should be considered. They were of the view that all existing charities whether unincorporated associations, trusts or companies limited by guarantee, could convert to this form of legal structure, if they wished, and all new charities which wished to avail of the advantages of incorporation would in future be required to adopt this legal structure.

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<sup>12</sup> External Report on the Consultation, at p 24.

<sup>13</sup> Conference of Religious of Ireland – see [www.cori.ie](http://www.cori.ie).

<sup>14</sup> PLANET - The Partnerships Network, is the representative voice of the 38 area-based Partnerships in Ireland, who work to promote social inclusion through the development of disadvantaged areas and communities.

<sup>15</sup> See [www.planet.ie](http://www.planet.ie)

<sup>16</sup> Free Legal Advice Centres, see [www.flac.ie](http://www.flac.ie).

They considered that the registration body for this new form of incorporation should be the proposed new regulatory body and not the Companies Registration Office.

4.19 FLAC outlined the advantages of a separate legal vehicle specifically geared towards the non-commercial needs and aims of charities and operated by the new regulatory body as follows:

- It would do away with the need for multiple registrations, regulation and reporting for charities (to the Companies Registration Office/Director of Corporate Enforcement, Revenue Commissioners and the proposed new body) thereby cutting costs and administration;
- All trustees/directors *etc* of bodies adopting this form of legal structure would be subject to the same statutory standard;
- All charities incorporated under the new vehicle would have separate legal personality;
- All trustees/directors would have limited liability.<sup>17</sup>

4.20 The Wheel pointed out that:

“...the current legal structures for charities are not suited to the nature of charitable entities and that for future development the new regulatory body could explore changes to the legal structures with the Department of Enterprise, Trade and Employment.”<sup>18</sup>

4.21 In the Commission’s view, these extracts indicate that within the voluntary sector there is a perceived need for a new legal structure for charities.

### **C Does Ireland need a New Legal Structure for Charities?**

4.22 It is generally recognised that none of the existing legal structures is ideally suited to the nature of charitable entities and none were devised with charities in mind. Each structure has a number of different requirements and obligations and each has its own advantages and disadvantages.<sup>19</sup>

4.23 The advantages of having a separate legal structure for charities are most acutely highlighted by considering and contrasting a possible new

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<sup>17</sup> <http://www.pobail.ie/en/CharitiesRegulation/SubmissionsonConsultationPaperonCharitiesRegulation/Free%20Legal%20Advice%20Centres.pdf>.

<sup>18</sup> See [www.wheel.ie](http://www.wheel.ie).

<sup>19</sup> See Chapter 1 above.

structure with the main corporate format currently used by charities, that is, the company limited by guarantee. As noted earlier, the principal reason why charities opt for incorporation are to avail of the protection provided by limited liability. In other cases incorporation proves necessary because certain grants are only available to incorporated organisations.

4.24 In the Commission's view, it is clear that companies were not designed to cater for not-for-profit organisations, in fact, quite the opposite is the case. Companies were designed as structures to cater for entrepreneurial activity and to meet the needs of commercial businesses. They generally operate to earn profits for their shareholders. By contrast, the ethos of charities is radically different. Charities exist to carry out a particular purpose and not to make a profit for their members.

4.25 Companies must currently register with the Register of Companies. With the proposed advent of a Charities Regulator<sup>20</sup>, it is envisaged that all charitable organisations would have to register with a regulatory body. This could lead to the possibility of dual requirements in the case of charities operating as companies. Apart from registration, other administrative requirements such as reporting and the filing of accounts that are currently required of companies may also be a feature of the new charity regulation regime. A separate legal structure for charities would eliminate the burden of dual registration and administrative requirements.

4.26 Under existing legislation every company must have at least two directors.<sup>21</sup> However, the Company Law Review Group (CLRG) has recommended that private companies limited by shares (the new model company envisaged by the group) need only have one director.<sup>22</sup> This recommendation has been incorporated into the general scheme of the CLRG's draft *Companies Bill*.<sup>23</sup> It is not yet clear whether companies limited by guarantee will also be able to operate as single member companies. As noted earlier, the Revenue Commissioners require a minimum of three trustees or officers or directors if a charity is to be granted charitable status and related tax exemptions. The Commission has also provisionally recommended that there be a minimum of three trustees or officers or directors.<sup>24</sup>

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<sup>20</sup> See paragraphs 2.17 to 2.20 above.

<sup>21</sup> Section 174 of the *Companies Act 1963*.

<sup>22</sup> *Company Law Review Group First Report* (31 December 2001) at paragraph 11.8.11.

<sup>23</sup> See [www.clr.org](http://www.clr.org).

<sup>24</sup> See Law Reform Commission *Consultation Paper on Charitable Trust Law: General Proposals* (LRC CP 36-2005), paragraphs 1.24 and 1.25.

4.27 At present, charity trustees may be personally liable for losses incurred by the charity even though they are acting as volunteers. The Revenue Commissioners do not regard the provision of insurance as a charitable object.<sup>25</sup> The lack of indemnity insurance for personal liability may act as a deterrent to volunteering as a charitable trustee. By contrast, a company may purchase and maintain for any of its officers or auditors insurance in respect of liability.<sup>26</sup>

4.28 As company law becomes more complex, it is becoming increasingly difficult for organisations to be confident that they are compliant. The directors of a charitable company may be personally liable under the fraudulent or reckless trading provisions of the *Companies Acts 1963 to 2005*<sup>27</sup> even though acting in a purely voluntary capacity. If the Charities Regulator is responsible for the regulation of all charities this will lead to dual regulation in the case of charities operating through companies. Alternatively, there may be two different regulatory regimes

4.29 The current corporate governance scheme is not necessarily tailored to fit the “trustee” nature involved in the governance of charities. There is legal uncertainty as to how the fiduciary duties of directors (now to be put on a statutory footing in the CLRG’s draft *Companies Bill*) interact with the fiduciary duties of charity trustees. While the duties of a director may in some ways be analogous to those of the trustees of a charity, they are by no means identical.

4.30 Some charities do not have a membership structure and the trustees are both directors and members. This can lead to some “artificial” decision making where the trustees have to act in different capacities merely to facilitate the requirements of the *Companies Acts*. A further difficulty, in the Commission’s view, is that there is confusion as to whether a company holds its property as trustee. A charitable company may hold particular property, as distinct from the general property of the company, on trust for specific charitable purposes.

4.31 Apart from providing an alternative to incorporation as a company, a new legal structure may also compare favourably with the other main structures currently in use, that is, the charitable trust and the unincorporated association. Neither of these structures confers limited

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<sup>25</sup> See Revenue Commissioners’ precedent number APP 11332 – 2 February 1995 which states that “the provision of insurance is not a charitable object”.

<sup>26</sup> Section 56 *Companies (Auditing and Accounting) Act 2003*.

<sup>27</sup> These regulatory oversight provisions are mainly geared towards commercial activity. For example, section 150(3) *Companies Act 1990* provides that a restricted person may act as a director of a company where the nominal value of the allotted share capital of the company is (i) in the case of a public limited company, at least £250,000 or (ii) in the case of any other company, at least £50,000.

liability and while, in some circumstances, trustees or committee members may be absolved for breaches of duty, there is no guarantee of such an outcome and trustees or committee members may find themselves personally liable to the charitable fund.

4.32 Charitable trusts are subject to the general law of trusts. Trust law is a body of law which has generally derived from case law as developed by the courts over many centuries. Such law is generally not easily accessible to members of the public who must therefore invariably engage professionals to assist them. Many charities have no - or only limited funds - available to spend on professional advice and therefore it is important that the law relating to them is as clear and readily understandable as possible.

4.33 The Commission is also conscious that, since there are no formal requirements for unincorporated associations, such groups may frequently develop in a casual and unorganised fashion. Difficulties may arise when such an organisation grows in size without having in place rules for the organisation's proper administration and operation. Where assets are being held for public benefit, the Commission is strongly of the view that such organisations should be subject to regulation based on transparency and accountability.

4.34 As noted in Chapter 3, Charitable Incorporated Organisations (CIOs) are being introduced in England and Wales and in Scotland and are also being recommended in Northern Ireland. From a cross-jurisdictional point of view there may be benefits to having a similar type structure in Ireland. This would facilitate the mutual recognition of charities and assist charities which are currently operating in a number of different jurisdictions. This would also facilitate the concerns expressed at EU level concerning the potential for misuse of charitable and voluntary organisations, in particular in terms of money laundering.<sup>28</sup>

4.35 On the other hand, it could be argued that the range of currently available legal forms is adequate and that adding to it would simply cause confusion among charities. But from the point of new charities wishing to establish, the Commission considers that the option of a tailor-made structure would suit them unless they had some specific reason for opting for one of the other structures. As regards existing charities, the Commission is confident that any confusion between existing structures and the new structure could be easily remedied by way of appropriate guidelines which could be issued by the Charities Regulator.

4.36 The fact that there is currently no statutory body for the regulation of charities in Ireland means that some of the problems which became apparent in England such as dual registration, reporting and regulation have

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<sup>28</sup> See paragraphs 3.29 - 3.31, above.

not yet surfaced in Ireland. But, as noted in Chapter 2, the advent of a Charities Regulator appears to be imminent and this may give rise to precisely the same set of problems experienced in England.

#### **D A proposed CIO structure for Ireland**

4.37 While there has been no comprehensive study undertaken on the appropriateness of the existing legal structures for charities, the Commission's survey of the available literature as outlined in this Paper indicates a broad view that there is a need for a structure tailored to fit the needs of charities. One of the difficulties is that the charity sector in Ireland has lacked the ability to undertake capacity-building initiatives on behalf of the sector. This can be contrasted with the situation in other countries where one finds many umbrella bodies for the charity sector for example in Northern Ireland, Scotland, England and elsewhere.

4.38 The Charities Regulation Study Group<sup>29</sup> was of the view that this shortcoming in relation to representation for charities could jeopardise the sector's ability to respond to the current initiatives in relation to charity law. The study group noted that:

“The Consultation Paper<sup>30</sup> observes that the preparation of new company law by the Department of Enterprise, Trade and Employment “could now be a window of opportunity for the charities sector”. The study group is concerned about the capacity of the charity sector to avail of this window of opportunity given the absence of representative structures to speak on behalf of the sector. The absence of a representative structure for the charity sector in Ireland has been noted elsewhere in this submission and we regard it as an issue which needs to be addressed urgently.

The study group considers that Caradas [a suggested name for the Charities Regulator] should have a key role in preparing a legal vehicle for all charities, taking the views of all key stakeholders into account. This would be consistent with one of its proposed statutory functions namely: “(g) advising the Minister on charity legislation, its own functions, and on matters relating to charity generally; and informing the public as appropriate or necessary”. In England and Wales, the Charity Commission is playing this

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<sup>29</sup> This group was formed in early 2004 for the purpose of preparing a submission to the Department of Community, Rural and Gaeltacht Affairs on the Department's 2003 Consultation Paper *Establishing a Modern Statutory Framework for Charities*: see paragraphs 2.17 ff, above.

<sup>30</sup> *Establishing a Modern Statutory Framework for Charities*.

role where the concept of a Charitable Incorporated Organisation is being considered as the legal template for all charities.”<sup>31</sup>

4.39 The Commission agrees with the view that the lack of a comprehensive umbrella body<sup>32</sup> representing the charity sector should not disadvantage the sector as a whole and that, in the absence of such representation, it may be appropriate for the Charities Regulator to take the lead in relation to consulting with the sector regarding the format of a new legal structure for charities.

4.40 In relation to charities operating through companies, the Department’s 2003 Consultation Paper did not directly address the question of who the appropriate Regulator for such charities should be or precisely how the new regulatory body would interact with existing regulatory bodies.<sup>33</sup> The Department’s 2004 Report on the Public Consultation refers to submissions which raised issues lying outside the competence of the Department of Community, Rural and Gaeltacht Affairs.<sup>34</sup> The question of a new Charitable Designated Activity Company (CDAC) is listed as one such area and it would seem that any submissions made on this issue were passed to the Department of Enterprise, Trade and Employment. As already noted,<sup>35</sup> it seems clear therefore that even if a CDAC were to be introduced, it would form part of company law and would be subject to regulation under the *Companies Acts*. The Commission is concerned that, as a result of this reality, it seems that the discussion of a new legal structure for charities may to some extent fall outside the remit of the Department’s consultation process on the regulation of charities. The Commission has concluded that it would be preferable if the issue of the appropriate legal structure for charities was dealt with in tandem with the proposed legislation on the regulation of charities. In light of the general consensus on the need for a structure tailored for the charity sector as outlined in this Paper the Commission provisionally recommends that such a structure should be established.

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<sup>31</sup> <http://www.pobail.ie/en/CharitiesRegulation/SubmissionsonConsultationPaperonCharitiesRegulation/Charities%20Regulation%20Study%20Group.pdf>.

<sup>32</sup> There are, of course, numerous umbrella bodies serving particular sub-sectors or shared concerns within the charity sector. These include, for example, the Irish Charities Tax Reform Group, Dochas, The Wheel, Disability Federation of Ireland, National Youth Council of Ireland and the Conference of Religious of Ireland.

<sup>33</sup> The Department’s Consultation Paper indicated (at page 13) that charities which are companies limited by guarantee would not be subject to dual filing requirements.

<sup>34</sup> Appendix 5, available at [www.pobail.ie/en/CharitiesRegulation/](http://www.pobail.ie/en/CharitiesRegulation/).

<sup>35</sup> See paragraph 4.11 above.

4.41 *The Commission provisionally recommends the introduction of a new form of legal structure for charities, to be called the Charitable Incorporated Organisation (CIO).*

## **E Should the proposed CIO structure be confined to charities?**

4.42 Apart from charities, the not-for-profit sector includes many other community and social enterprise groups. These bodies may also suffer the same problems as charities in relation to the suitability of current corporate structures. The question therefore arises as to whether any new legal structure for charities should also be available to other not-for-profit bodies.

4.43 The UK Company Law Review Steering Group considered whether charities and other not-for-profit bodies should both be in a position to avail of the new corporate vehicle. The group was of the view that there should be legislation for a distinct form of incorporation for charities but not for other third sector bodies.<sup>36</sup> They considered that public interest groups did not face the same problem of dual regulation which charities did. The other main difficulty with providing the same legal structure for charities and public interest groups was the danger that it might cause a blurring in the public mind of important conceptual distinctions between charitable and non-charitable bodies. The Commission is equally concerned at the potential risk of confusion in the minds of the public if the new legal structure was also made available to non-charitable bodies.

4.44 A separate vehicle, the Community Interest Company (CIC), has now been made available to community and other social enterprises in the UK.<sup>37</sup> The CICs will be easy to set up, with all the flexibility and certainty of the company form, but with some special features to ensure they are working for the benefit of the community. CICs will report to an independent regulator on how they are delivering for the community and how they are involving their stakeholders in their activities. An organisation cannot be both a CIC and a charity. CICs will be more lightly regulated than charities but will not have the benefits of charitable status, even if their objects are entirely charitable in nature. The Commission sees the general merits in this approach but, for present purposes, has not considered this wider issue and has confined itself to consideration of the appropriate legal structures for charities.

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<sup>36</sup> *Modern Company Law for a Competitive Economy: Developing the Framework* (Interim Report of the CLRSG March 2000), paragraphs 9.19 and 9.28-9.30. *Modern Company Law for a Competitive Economy: Completing the Structure* (Interim Report of the CLRSG November 2000), paragraph 9.3, and *Modern Company Law: Final Report* (Final Report of the CLRSG July 2001) paragraph 4.63.

<sup>37</sup> Part 2 of the *Companies (Audit, Investigations and Community Enterprise) Act 2004* and the *Community Interest Company Regulations 2005*.

4.45 *The Commission provisionally recommends that the need for a separate legal vehicle for community interest groups in Ireland requires further consideration.*

## **F The form of the proposed CIO structure**

4.46 The Commission's proposed Charitable Incorporated Organisation (CIO) should be designed specifically to meet the needs of charities and to counteract the disadvantages associated with the existing legal structures. It is clear that there has been a great deal of agreement in the form of the proposals emanating from considerable public consultation which has taken place in other jurisdictions and which is set to produce legislative reform in the near future.<sup>38</sup> In the Commission's view, those proposals should form the basis for reform in this jurisdiction.

4.47 The proposed CIO structure should provide:

- A separate legal entity for its members and
- There should be a minimum number of 3 charity trustees;
- There should be limited liability for members;
- The proposed CIO structure may be one-tier, where the members act as charity trustees, or two tier for charities with charity trustees and members;
- A model constitution should be designed in consultation with the charity sector;
- The charity trustee's duty of care should be consistent with that contained in the proposed legislation on the regulation of charities.

4.48 The Commission also provisionally recommends that the proposed legislation on the regulation of charities should also contain provisions relating to:

- the simple conversion of existing charities to the proposed CIO structure;
- the amalgamation of charities;
- the transfer of property, rights and liabilities to another similar organisation;
- winding-up, insolvency or dissolution;

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<sup>38</sup> See the discussion of the reforms in England and Wales and in Scotland, and the proposed reforms in Northern Ireland, discussed in Chapter 3 above.

- the amendment of the constitution of a charity.

4.49 *The Commission provisionally recommends the following features for the CIO:*

- *The proposed CIO structure should provide a separate legal entity for its members;*
- *There should be a minimum number of 3 charity trustees;*
- *There should be limited liability for members;*
- *The proposed CIO structure may be one-tier, where the members act as charity trustees, or two tier for charities with charity trustees and members;*
- *A model constitution should be designed in consultation with the charity sector;*
- *The charity trustee's duty of care should be consistent with that contained in the proposed legislation on the regulation of charities.*

4.50 *The Commission provisionally recommends that the proposed legislation on the regulation of charities should also contain provisions relating to:*

- *the simple conversion of existing charities to the proposed CIO structure;*
- *the amalgamation of charities;*
- *the transfer of property, rights and liabilities to another similar organisation;*
- *winding-up, insolvency or dissolution;*
- *the amendment of the constitution of a charity.*

## **G Charities and trading activities**

4.51 A further question arises as to whether charities carrying on trading activities should be able to avail of the proposed CIO structure. Currently, a charity can avail of exemption from tax on trading activities if they satisfy the following Revenue Commissioner conditions.

4.52 The main requirement is that the profit of the trade must be applied solely for the purposes of the charity. In addition, one or other of the following conditions must also be satisfied:

- the trade must be exercised in the actual carrying out of a primary purpose of the charity (an example would be a religious

organisation selling religious books or magazines to facilitate the main object of the organisation) or

- the trade must be carried on by the beneficiaries of the charity (an example would be the sale of goods produced by people with disability through a shop or mail order catalogue.)<sup>39</sup>

4.53 The Commission considers that any charity which carries on trading activities which satisfy these requirements should be allowed to avail of the proposed CIO structure. But where a charity sets up a company for trading purposes which does not satisfy these requirements it should not be in a position to avail of the proposed CIO structure and would be obliged to register as a company under the *Companies Acts*.

4.54 As already noted<sup>40</sup> one of the functions of the proposed Charities Regulator would be to ensure the public accountability of charities. Charities established under the Commission's proposed CIO structure should not be subject to less rigorous standards than would apply if they were established as companies. It is envisaged that under the monitoring programme of the Charities Regulator, each charity will be obliged to prepare an annual report and to make an annual return to the Charities Regulator.<sup>41</sup> The submission of an annual return will give the general public a greater insight into the charity's activities and will thereby enhance the public accountability of charities. This annual return should include both financial information and an activity statement. Given the diversity in terms of the size of charities and the activities they undertake, it may be appropriate for the Charity Regulator to set different annual return and audit requirements depending on the size of the charity involved.<sup>42</sup> Many charities undertake different activities under separate structures or may operate in various jurisdictions. Where a charity is operating through a number of subsidiary undertakings the Commission would envisage that consolidated accounts should be submitted in addition to the individual charity's accounts.

4.55 *The Commission provisionally recommends that charities carrying on trading activities directly related to their charitable purposes should be allowed to avail of the proposed CIO structure.*

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<sup>39</sup> See *Applying for Relief from Tax on the Income and Property of Charities* (CHY 1, May 2003) and *Charities Manual* July 2001 at p.13 available at [www.revenue.ie](http://www.revenue.ie)

<sup>40</sup> See paragraph 2.17 above.

<sup>41</sup> The precise reporting requirements for charities are likely to be developed between the Charities Regulator and the charity sector.

<sup>42</sup> For example, in England and Wales, a trustee's annual report and accounts must be filed by all charities with gross income or total expenditure of over £10,000, see Part VI *Charities Act 1993* and applicable Regulations.

## **H            Should the New Legal Structure be Mandatory?**

4.56        The Commission has also considered whether the new legal structure should be available as an additional option to existing methods of incorporation or be mandatory.

4.57        The Commission acknowledges that it would not be feasible to prevent charities from setting up as trusts or unincorporated associations. This is particularly so in view of Article 40.6 of the Constitution which guarantees the right of citizens to form associations and unions. Of course such entities could be denied charitable status and related tax exemptions but this might lead to a category of “unofficial charities” which would remain outside the regulatory regime. This would clearly be undesirable in an era where the aim is to ensure public confidence by the proper supervision of charities.

4.58        Many existing charities constituted as trusts or unincorporated associations might benefit from a more structured constitution, and more certainty about the powers and duties of their trustees and members in addition to the protection afforded by limited liability status. In many instances trusts and unincorporated associations are compelled into a corporate structure if they wish to avail of grants and funding. The Commission has concluded that it would be preferable, certainly in the immediate future, that the proposed CIO structure should be available as an optional structure for existing charities.

4.59        *The Commission provisionally recommends that existing trusts and unincorporated associations should be given the option of converting to the proposed CIO structure and that conversion should be capable of being achieved in a simple, cost effective, manner.*

4.60        With regard to charities registered as companies under the *Companies Acts* three scenarios may be envisaged:

- All existing incorporated charities would be obliged to convert to the new structure and new charities wishing to incorporate would only be allowed to use the new structure;
- Existing incorporated charities would be given the *option* of converting to the new structure but the new structure would be mandatory for new charities wishing to incorporate;
- Existing incorporated charities would be given the option of converting to the new structure and new charities would also have the option of choosing the new structure or other legal status.

4.61        As regards the first option, while it might be legally possible to prevent new charities from incorporating under the *Companies Acts*, it might prove more difficult to require conversion of existing companies. Requiring

existing charities to convert to the new structure might entail some additional costs and upheaval for charities which are well established in their existing categories. However, as noted above the Commission is of the view that conversion should be capable of being achieved in a simple cost effective manner.

4.62 As regards the second option, it could be regarded as inequitable to allow existing charities the option of converting to the new structure while denying new charities the option of using existing structures. Again the spectre of some form of “unofficial charities” would be unacceptable.

4.63 It appears to the Commission that, at least at the outset, the third option would be the most appropriate course of action. As with any new legal entity it may take some time for the new type of structure to “settle down” and some adjustments may be required before a final workable format is in operation. Until public confidence in the proposed CIO structure is established, the idea of an exclusive regime might meet with resistance. For this reason the Commission has concluded that it would not be appropriate to insist from the beginning that all incorporated charities adopt the new format.

4.64 *The Commission provisionally recommends that the proposed CIO structure should be an additional option for incorporated charities and that the other existing methods of incorporation should continue to be available.*

4.65 As noted earlier,<sup>43</sup> in England it is proposed that a review of the situation will take place after 5 years following the introduction of the CIO, at which stage consideration will be given to whether other forms of incorporation should continue to be available for charities.

4.66 In its Consultation Paper, the Department of Community, Rural and Gaeltacht Affairs has recommended that the reforms to be introduced in its proposed charity legislation would be subject to review after 5 years in operation. In the Commission’s view this would also appear to be a reasonable period for the review of the operation of the proposed CIO structure.

4.67 *The Commission provisionally recommends that the operation of the proposed CIO structure should be reviewed after a period of 5 years from its introduction, at which point consideration may be given to whether other methods of incorporation for charities should continue to be available.*

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<sup>43</sup> See paragraph 3.16 above.



## **CHAPTER 5      SUMMARY OF PROVISIONAL RECOMMENDATIONS**

5.01      The Commission provisionally recommends the introduction of a new form of legal structure for charities, to be called the Charitable Incorporated Organisation (CIO). [Paragraph 4.41]

5.02      The Commission provisionally recommends that the need for a separate legal vehicle for community interest groups in Ireland requires further consideration. [Paragraph 4.45]

5.03      The Commission provisionally recommends the following features for the CIO:

- The proposed CIO structure should provide a separate legal entity for its members;
- There should be a minimum number of 3 charity trustees;
- There should be limited liability for members;
- The proposed CIO structure may be one-tier, where the members act as charity trustees, or two tier for charities with charity trustees and members;
- A model constitution should be designed in consultation with the charity sector;
- The charity trustee's duty of care should be consistent with that contained in the proposed legislation on the regulation of charities. [Paragraph 4.49]

5.04      The Commission provisionally recommends that the proposed legislation on the regulation of charities should also contain provisions relating to:

- the simple conversion of existing charities to the proposed CIO structure;
- the amalgamation of charities;
- the transfer of property, rights and liabilities to another similar organisation;

- winding-up, insolvency or dissolution;
- the amendment of the constitution of a charity.

[Paragraph 4.50]

5.05 The Commission provisionally recommends that charities carrying on trading activities directly related to their charitable purposes should be allowed to avail of the proposed CIO structure. [Paragraph 4.55]

5.06 The Commission provisionally recommends that existing trusts and unincorporated associations should be given the option of converting to the proposed CIO structure and that conversion should be capable of being achieved in a simple, cost effective, manner. [Paragraph 4.59]

5.07 The Commission provisionally recommends that the proposed CIO structure should be an additional option for incorporated charities and that the other existing methods of incorporation should continue to be available. [Paragraph 4.64]

5.08 The Commission provisionally recommends that the operation of the proposed CIO structure should be reviewed after a period of 5 years from its introduction, at which point consideration may be given to whether other methods of incorporation for charities should continue to be available. [Paragraph 4.67]