

## RECENT DEVELOPMENTS IN THE *CY PRES* PRINCIPLE

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1. It is encouraging when statute law harmonises with the common law and pleasing when different legal systems reach similar conclusions despite differing traditions. It suggests that the relevant law contains a measure of common sense. Two recent developments in the *cy pres* principle are therefore very welcome, the first being the coming into force on 18 March 2008<sup>2</sup> of ss 15-18 of the Charities Act 2006, and the second the Opinion (decision) of Lord Drummond Young in the Outer House of the Court of Session on the *Petition of Austin and Others*<sup>3</sup>.

2. The *cy pres* principle is a large subject, and this article will concentrate on circumstances where the need for a scheme arises after the charity has been established and is actually operating, rather than attempting to comment in any detail on the less common situation where a charitable purpose fails or is shown to be unworkable at the outset<sup>4</sup>. Nor will it consider the changes in the law and practice relating to permanent endowment<sup>5</sup>. The writer apologises in advance for any errors dues to an imperfect understanding of Scots law.

3. Until 1961, the *cy pres* principle in England and Wales as well as Scotland was governed entirely by the common law, and the Charity Commission when making schemes expected to be satisfied that the existing trusts had failed before they would consider a scheme to provide for a *cy pres* application, which would

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<sup>2</sup> See the Charities Act 2006 (Commencement No 3, Transitional Provisions and Savings) Order 2008 (SI 751).

<sup>3</sup> [2008] ScotCS CSOH\_116.

<sup>4</sup> E.g. cases of initial failure under wills and schemes under ss 14 and 14A of the Charities Act 1993 as amended/inserted by ss 16-17 of the Charities Act 2006.

<sup>5</sup> E.g. total return orders and the powers conferred by ss 75-75B of the 1993 Act as amended/inserted by s 43 of the Act of 2006.

have to be as close as possible to the founder's expressed intentions (a concept referred to throughout s 13 as 'the spirit of the gift'). The Charities Act 1960 did not directly affect the choice of new purposes but set out for the first time<sup>6</sup> the occasions on which a *cy pres* scheme could be made (whether by the Court or by the Charity Commission<sup>7</sup>), making clear that actual failure in the sense of impossibility was sufficient but not necessary to trigger the jurisdiction. The provisions of s 13 were repeated in s 13 of the Charities Act 1993.

4. In practice the Charity Commission, by whom the vast majority of schemes were made, retained some of its previous habits for many years after the 1960 Act came into force, with staff continuing routinely to refer to the need for the 'failure' of a trust before a *cy pres* scheme would be considered. When pressed, however, the Commission would generally acknowledge that the term 'failure' was used in a sense which included everything implied by s 13.

5. In addition to expanding the circumstances in which a *cy pres* scheme might be offered, that section also had an indirect effect on the nature of the resulting schemes. At first, the Commission kept rigidly to the 'as near as possible' standard, paying the utmost attention to the founder's expressed intention and tending to alter relatively detailed provisions such as the area of benefit of a charity in preference to amending the scope of the overall charitable purpose. If, for example, a local charity for poor widows received a greatly increased income, e.g. due to the sale of land, the Commission would normally be more inclined to enlarge the area of benefit and extend the beneficiary class to all poor persons resident there but to retain the charity's purpose of relieving poverty (though expressing it in more modern language<sup>8</sup>) than to extend the purposes to include other types of charitable purpose for the benefit of the original area.

6. During this period, which coincided with a period of high inflation, the decision in *Re Lepton's Charity*<sup>9</sup> usefully encouraged the Commission to take a broader approach to the interpretation of the original trusts, enabling a division of income between different purposes described in the original trusts by reference to specified amounts to be updated by reference instead to stated proportions of the income, where this seemed appropriate. Thus, if a trust provided for (say) £50 a year out of the income to be applied for poor widows of the parish and the rest for the support of the local school, the Commission would be willing to take account of the fact that the total income at the time of the gift was originally a fixed amount of

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<sup>6</sup> See Charities Act 1960 s 13, especially subsection (1)(a) to (e).

<sup>7</sup> See *ibid.* s 13(4) and 18(1)(a).

<sup>8</sup> A standard provision entitled 'relief in need' was used in schemes regulating local charities for the relief of poverty, replacing the previous standard provision entitled 'general benefit of the poor'.

<sup>9</sup> [1972] Ch 276.

£100 when deciding, after the income had grown to £2,000, that the new scheme should provide for the income to be divided equally between the modern equivalents of the two purposes.

7. The Charities Act 1985 introduced new provisions which enabled very small, unincorporated charities, having no land held for charitable use, which had been in existence for at least 50 years, to dispense with a scheme by permitting alterations to a charity's objects, or the transfer of its assets to another charity, to be effected by unanimous resolution of the trustees with the concurrence (i.e. consent) of the Charity Commission. It is significant that the 1985 Act paraphrased the *cy pres* principle in somewhat relaxed terms both in making it a condition that the trustees should form the opinion, before seeking to alter the objects, that the existing objects could 'fairly be considered obsolete or lacking in usefulness, or impossible of achievement', having regard to various matters<sup>10</sup>, and in specifying that the proposed new objects must be, in the trustees' opinion, 'not so far dissimilar in character to those of the original charitable gift that this modification of the charity's trusts would constitute an unjustifiable departure from the intentions of the founder... or violate the spirit of the gift.'<sup>11</sup>

8. In the case of the transfer of assets between charities, the assumption was made that the transfer to another charity of the assets of a charity of the transferor's size was desirable in itself. However, the condition was that the trustees should form the opinion that the transferee's objects were not excessively dissimilar in character from those of the transferor, using very similar words<sup>12</sup>.

9. Following the Report of Sir Philip Woodfield, which led to the White Paper, 'A Framework for the Future', which heralded the Charities Acts of 1992 and 1993, the Charity Commission carried out a consultation exercise into the practical operation of the *cy pres* principle. As a result, the Commission's policy was slightly relaxed<sup>13</sup> although no legislative changes were made in the re-enactment of s 13 of the 1960 Act. In the late 1990s a decision of the Court of Appeal<sup>14</sup> in a case involving s 13(1)(e) underlined the flexible nature of that provision. A Hindu sect had suffered an internal division within its congregation. Rather than seeking to determine via expert evidence which of the two groups held more faithfully to the original doctrines, the Court took the view that the overriding purpose was to

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10 'the period that has elapsed since the charity was founded, the social and economic changes that have taken place in that period and other circumstances (if any) relevant to the functioning and administration of the charity': see s 2(2)(a).

11 Section 2(2)(b).

12 Section 3(2)(b).

13 See the Charity Commissioners' Annual Report for 1989, para 54 onwards.

14 *Varsani v Jesani* [1999] Ch 219, upholding Carnwath J.

provide a place of worship for all the members of the relevant community, and that it was preferable to divide the assets between them by a *cy pres* scheme. (Unfortunately it later proved extremely difficult to agree the terms of the new scheme.)

10. Although there was no overt change in s 13, the 1993 Act<sup>15</sup> reflected the increased flexibility which had been adopted as a matter of policy by other means. It incorporated and modified the provisions of the 1985 Act, increasing the gross income limit to £5,000, reducing the voting requirement to a two-thirds majority of the votes cast, and extending the provisions capable of being amended to include provisions ‘relating to any of the powers exercisable by the charity trustees in the administration of the charity, or... regulating the procedure to be followed in any respect in connection with its administration.’<sup>16</sup> The latter expression has never been judicially defined but the Commission has tended to interpret it as roughly equivalent to the type of changes which might be effected by an ‘administrative’, rather than a *cy pres*, scheme.

11. In addition, the conditions on which the trustees were able to pass a resolution to transfer the assets of a charity or to alter its purposes were expressed in different terms. The trustees had to be satisfied that the existing purposes ‘had ceased to be conducive to a suitable and effective application of the charity’s resources’ and that either the purposes of the transferee charity, or the new purposes which the trustees proposed to adopt for the subject charity in place of the existing purposes, must be were ‘as similar in character to the original purposes as is practical in the circumstances’<sup>17</sup>. This indicates, if anything, a slight relaxation both of the occasions on which either type of resolution might be passed and of the choice of transferee charity or scope of the new purposes.

12. The 2006 Act has amended both the 1993 Act provisions relating to *cy pres* schemes as such and the provisions deriving from the 1985 Act. In relation to all the changes which can be effected by resolution, more detailed provision is now made, with the three types of changes being dealt with in separate sections. The income threshold for the use of trustee resolutions to transfer the assets<sup>18</sup> or change the purposes<sup>19</sup> of a charity has been increased to £10,000, and has been removed altogether in relation to the power to alter provisions relating to procedures or the

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15 See s 74.

16 Section 74(2)(d).

17 Unamended s 74(4)(b) and (5)(b).

18 Sections 74, 74A and 74B of the 1993 Act as substituted/inserted by s 40 of the 2006 Act.

19 Ibid s 74C.

trustees' powers<sup>20</sup>, in respect of which charities having land held on trust for charitable use are also included. For a transfer of assets or change of purposes it remains necessary for the resolution to be passed by a two thirds majority vote, but, under s 74D, a simple majority vote suffices unless the charity has a membership, in which case the trustees' resolution requires ratification by a two thirds majority vote of the members in general meeting.

13. In addition, the occasion for change and similarity test is expressed differently. For a transfer of assets, the trustees need only be satisfied that the proposed transfer is 'expedient in the interests in furthering' the original purposes and the transferee charity's purposes must be 'substantially similar' to those of the transferor<sup>21</sup>. Where the purposes are to be altered the trustees need only be satisfied that it is 'expedient in the interests of the charity' (wording also used in s 26 of the 1993 Act) that that the purposes be replaced, and the new purposes must consist of or include purposes of a 'similar character'.

14. The amendments to the 1993 Act brought about by ss 13 and 18 of the 2006 Act broaden both the circumstances in which a *cy pres* scheme may be made and the scope of the new purposes which may be provided. The expression 'the spirit of the gift' in s 13 is replaced by a new term, 'the appropriate considerations', defined to include both the spirit of the gift and the social and economic conditions prevailing at the time of the proposed alteration<sup>22</sup>. This will have the effect of enabling *cy pres* schemes to be made where previously the Commission or the court might have declined on the basis that the founder's intention could still be carried out, albeit in differing conditions from those the founder envisaged. In addition, a new section is inserted<sup>23</sup> which amends the common law rule regarding the closeness of the new purposes to the original.

15. This new provision expressly applies to *cy pres* schemes which either amend the existing trusts by altering the original purposes directly or achieve a similar result by providing for the assets of a charity to be transferred to another charity. In both cases, the Commission (or the Court) must consider what is appropriate having regard to 3 considerations<sup>24</sup>: (1) the spirit of the gift; (2) the 'desirability' (i.e. not a strict obligation) of securing the application of the charity's property for purposes which are 'close' (i.e. not 'as close as possible') to the original purposes; and (3) the 'need' (a stronger term than 'desirability') for the charity 'to have purposes which are suitable and effective in the light of current social and economic conditions'.

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<sup>20</sup> Ibid s 74D.

<sup>21</sup> Ibid s 74(4).

<sup>22</sup> See s 15 of the 2006 Act.

<sup>23</sup> Section 14B of the 1993 Act, inserted by s 18 of the 2006 Act.

<sup>24</sup> Ibid s 14B(3).

This language is more flexible than the approach of the Charity Commission since the 1993 Act came into force, in that it gives more weight to social and economic circumstances and somewhat less weight to the founder's intention. It will be of considerable interest to observe to what extent charity trustees and the Commission's staff take advantage of the additional leeway it seems to provide.

16. In addition, s 14B provides<sup>25</sup> that, when a scheme authorises the transfer of assets to another charity, it may also place an obligation on the transferee charity to 'secure that the property is be applied for purposes which are, so far as is reasonably practicable, similar in character to the original purposes.' The difference between 'similar in character'<sup>26</sup> and 'substantially similar',<sup>27</sup> a pair of expressions also found in ss 74 and 74C as mentioned above<sup>28</sup>, is not obvious, but presumably both expressions enable a broader view of the similarity to be taken than if the word 'similar' were unqualified. This provision may enable a charity's assets more easily to be transferred to another charity with substantially wider objects, without permitting undue departure from the original purpose, where there are other reasons, organisational or otherwise, which make this desirable.

17. By contrast to the position in England and Wales, the Court of Session in Scotland has continued to apply the *cy pres* principle at common law. This has until recently been supplemented by specific statutory provisions relating to educational charities<sup>29</sup> and to trusts<sup>30</sup>. Those statutory provisions have now been replaced by new powers, in the Charities and Trustee Investment (Scotland) Act 2005, for schemes for the reorganisation of charities, including the alteration of their purposes, to be made by the Office of the Scottish Charities Regulator (OSCR)<sup>31</sup>.

18. One of the consequences is that, owing to the expense involved as well as to the relatively small number of charities operating exclusively in Scotland, *cy pres* schemes in that jurisdiction have been relatively rare. It was therefore newsworthy when, on 13 August 2008, the *Petition of Austin and Others* was decided by the

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25 Section 14B(4).

26 As in s 74C(4)(b).

27 As in s 74(11).

28 See paragraph 12.

29 Under the Education (Scotland) Act 1980.

30 Under the Law Reform (Miscellaneous Provisions) Scotland Act 1990

31 Charities and Trustee Investment (Scotland) Act 2005 ss 39-43 and the Charities Reorganisation (Scotland) Regulations 2007, which came into force on 31 May 2007. OSCR has published guidance on the operation of these provisions ("Charity reorganisation guidance", OSCR, October 2007).

Outer House of the Court of Session. A grant-making charitable trust<sup>32</sup> was established by Mr R S Macdonald in 1978, with shares in a public company producing Scotch whisky<sup>33</sup> forming its endowment. The income, and (only in exceptional circumstances having regard to an express proviso that the trustees should preserve its value intact) the capital, was applicable at the Trustees' discretion to or for the benefit of 6 named charities<sup>34</sup> and any other charity operating in Scotland as should include among its principal objects one or more specified purposes similar to the objects of the named charities<sup>35</sup>. Mr Macdonald died in 1995 leaving the remainder of his shareholding, then worth £17m, to the Trust. The shares subsequently increased in value as a result of a takeover bid, and were eventually sold in 2004 for nearly three times their 1995 value.

19. After the Truster's (Founder's) death the Trustees found increasing difficulty in coping with the numerous applications for grants, and in determining whether applicant charities were qualified for assistance. The references to 'spastics' caused particular difficulty since the Trustees received medical advice that the expression refers not to a specific disease but to the type of movement among those suffering from either cerebral palsy or a range of other conditions. Further, the work and objects of 4 of the named charities<sup>36</sup> had altered in significant ways since the establishment of the Trust.

20. Accordingly the Trustees sought a scheme to update the objects of the Trust, remove or relax some of the express restrictions and also to modernise the Trustees' powers. This was designed to provide much greater flexibility in the selection of charities for benefit and thereby to widen the scope of the Trust to a considerable degree. Evidence (including expert evidence) and argument were presented not only on behalf of the Trustees but also on behalf of the respondent, SSPCA, which opposed the scheme.

21. Lord Drummond Young, in his Opinion, analysed the authorities, beginning with the well-known dictum of Lord Westbury in the leading case of *Clephane v*

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32 The R S Macdonald Charitable Trust ('the Trust'), a recognised charity.

33 Which later changed its name to Glenmorangie PLC.

34 The Scottish Council for Spastics (now Capability Scotland), the Royal Blind Asylum, the RNLI, the Royal Scottish Society for the Prevention of Cruelty to Children (now CHILDREN 1ST), the Scottish Society for the Prevention of Cruelty to Animals and Guide Dogs for the Blind Association.

35 The care and welfare of spastics and/or the blind, research into the causes or prevention or treatment of blindness and/or spastic conditions, the prevention of cruelty to children and the prevention of cruelty to animals.

36 Capability Scotland, the Royal Blind Asylum, CHILDREN 1ST and the SSPCA.

*Magistrates of Edinburgh*<sup>37</sup>: ‘...You look to the charity<sup>38</sup> which is intended to be created, that is to say, that benefit of the beneficiary, and you distinguish between the charity and the means which are directed to the attainment of that charity.....the means originally intended may become inadequate to that end. And the Courts...always exercise the power of varying the means...according as by that variation they can secure more effectively the great object of the charity... You may substitute for a particular charity, which has been defined and which has failed, another charity *ejusdem generis*, or which approaches it in its nature and character, but...you cannot take a charity which was intended for one purpose, and apply it altogether to a different purpose.’<sup>39</sup> He commented that this approach permitted quite radical changes in the method of carrying out the charity’s basic objectives, whether the original means had failed or merely become impractical.

22. He next contrasted the position where a specific charitable object had become impossible, where a *cy pres* scheme could be made only if there were a general charitable intention (a doctrine which in English law is now applied only in cases of initial failure). Tracing subsequent case-law, he then examined various decisions in some of which a more restrictive approach had been taken. He observed that more recent decisions, albeit often made under the statutory provisions rather than being governed by the common law, tended to be more liberal, whether they were concerned with charitable objects as such or the powers of trustees. Lord President Hope in *Mining Institute of Scotland Benevolent Fund Trustees*<sup>40</sup>, had indicated that the *nobile officium*<sup>41</sup> was available to establish a *cy pres* scheme where a compelling case of expediency, falling short of impossibility, was made out.

23. Placing the *cy pres* principle in a broader context, Lord Drummond Young went on to point to the public interest in ensuring that ‘funds dedicated to providing public benefit are efficiently employed. The public interest extends beyond the mere wishes of the truster. It follows that trustees should not be tied strictly to forms of wording used by the truster, or particular administrative arrangements set up by him, if those forms or wording or administrative arrangements get in the way of a rational application of the funds for the broad public objectives identified by the truster.’ He therefore affirmed the approach taken in *Clephane* and rejected the respondents’ argument to the effect that it was necessary to demonstrate failure or unworkability and that expediency was not a sufficient ground for a *cy pres* scheme. A sufficiently compelling case had been made in this case.

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<sup>37</sup> (1869) 7 M (HL) 6.

<sup>38</sup> i.e. the underlying charitable object.

<sup>39</sup> At p. 15.

<sup>40</sup> [1994] SLT 785.

<sup>41</sup> i.e. the jurisdiction of the Court of Session.



24. After analysing the Trustees' expressed difficulties<sup>42</sup>, Lord Drummond Young held that they should be treated as cumulative, and were serious in that they impeded the Trustees' activities to a substantial degree. He went on mention 3 other specific problems<sup>43</sup> which also required resolution under the scheme, which he held should provide largely as the Trustees had proposed.

25. Interestingly, however, he declined to remove the limitation to charities operating in Scotland, citing *Glasgow Society for the Prevention of Cruelty to Animals v National Anti-Vivisection Society*<sup>44</sup> for the 'proposition that funds directed to objects within Scotland should only in exceptional cases be diverted to objects carried out in other parts of the world', and holding that no compelling case had been made for the change on grounds of expediency, given Scotland's outstanding record in scientific, technical and medical research and the probability that the Truster wished to support that tradition. He also held that, whilst there were always borderline issues, the expression 'charities operating in Scotland' had a reasonably clear core meaning.

26. It would thus appear that in contrast to the elaborate statutory provisions in the 1960, 1993 and 2006 Acts, in which the attempts have been made to develop and broaden the *cy pres* principle as applied in England and Wales, using highly nuanced language, a very similar resulting approach has been found to be applicable in Scotland in reliance on the enlightened judicial interpretation of a decision of the House of Lords dating from 1869, and drawing comfort from decisions relating to changes under modern statutory provisions which were ultimately based on the same principle.

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<sup>42</sup> Briefly: excessive funds, having regard to evidence that the maximum amount considered reasonable for a charitable grant was currently £40,000 in one year; the changes in some of the individual charities' approach to their work in response to developing views of what was most effective; and the way in which research establishments tended now to be set up, with a much wider range of activities than previously, making it difficult to identify their 'principal objects'.

<sup>43</sup> The fact that the term 'spastic' was outdated; the equation in modern medical practice of blindness with sight impairment; and the fact that the prevention of cruelty to children or animals was now expressed in a positive way as promoting their welfare.

<sup>44</sup> [1915] SC 757.