

CHARITABLE COMPANIES AND THE CHARITIES ACT 1992

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Anomalous Position of Charitable Companies

Charities have been adopting the legal structure of a company limited by guarantee since the structure first appeared in the Companies Act 1862. Ever after, charitable companies have occupied an anomalous position in law, sitting uncomfortably between charity law, based on trust law, and company law designed for commercial, not philanthropic, organisations. Indeed, it was not until 1989 that a definition of "company" was inserted in the Charities Act 1960. The anomalous position of the Charitable company is further highlighted by the position it occupies 'analogous to that of a trustee' in relation to its corporate assets.²

Charitable companies are subject to the control and supervision of both the Charity Commissioners and the Registrar of Companies. The White Paper, however, far from regarding this as double protection, took the view that the companies legislation did not permit the Attorney-General and the Charity Commissioners to exercise their full supervisory role - "Charities: A Framework for the Future", Cm 694 para 5.21. Accordingly, the Charities Act 1992 contains provisions restricting the powers of charitable companies and extending the powers of the Commissioners. Charitable companies had previously been the subject of legislation in the Companies Act 1989 and some of the 1992 provisions are amendments of the 1989 legislation.

Companies Act 1989

The Companies Act 1989 abolished the doctrine of ultra vires for companies by inserting a new s.35 in the Companies Act 1985 giving companies full capacity as regards third parties. The same Act also inserted a new s.35A in the 1985 Act which removed limitations on the powers of directors in favour of third parties. The result of these provisions for charitable companies would have been to make it far more difficult to ensure that property was retained for charitable purposes.³ No longer would it be possible simply to avoid a contract or disposition for non-charitable

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² *Liverpool and District Hospital for Diseases of the Heart v Attorney-General* [1981] 1 All E.R. 994; see also, Warburton, *Charitable Companies* [1984] Conv 112.

³ See, Warburton, *Charitable Companies and the Ultra Vires Rule*, [1988] Conv 275.

purposes on the grounds that it was ultra vires.⁴

Consequently, the 1989 Act introduced a new s.30B into the Charities Act 1960 which prevents ss.35 and 35A of the Companies Act 1985 applying to charitable companies except in three situations. First, a person who gives full consideration in money or money's worth and has no knowledge of the lack of capacity or authority can enforce a contract against a charitable company which is beyond the capacity of the company or its directors. Secondly, a person who does not know at the time the act was done that the company is a charity is protected and, thirdly, anyone who subsequently obtains title to property for full consideration without notice of the original invalidity cannot be required to return the property on the grounds that the original transfer was void. Thus, after 1989, commercial transactions beyond the capacity of a charitable company or the powers of its directors are binding.⁵ As an additional safeguard, s.30B(4) of the Charities Act 1960 provides that an ultra vires contract cannot be ratified under s.35(3) of the 1985 Act without the written consent of the Charity Commissioners.

The Companies Act 1989 also contained provisions restricting the right of a charitable company to alter its objects and requiring such companies to publicise their charitable status. Both these provisions have, to varying degrees, been amended by the Charities Act 1992.

Alteration of Objects

The Companies Act 1989 s.110(2) made it far easier for companies to alter their objects by substituting a new s.4 in the Companies Act 1985. That section allows the objects clause to be altered by special resolution; no longer are specific reasons or the consent of the court required. This would clearly have made it easier for charitable companies to divert property to non-charitable purposes. Although in law only after-acquired property can be used for any new non-charitable objects,⁶ the only requirement was for a company to inform the Charity Commissioners once an alteration of objects had taken place. Accordingly, s.30A(2) was inserted in the Charities Act 1960 which requires a charitable company to obtain the prior written consent of the Commissioners before the objects clause in the memorandum of association can be altered. On the basis of previous practice, the Charity Commissioners are unlikely to consent to a proposed alteration if they consider that, by a fundamental change in the objects, the real intentions of the public who

⁴ For the effectiveness of the ultra vires rule in protecting charity property see *Rosemary Simmons Memorial Housing Association Ltd v United Dominions Trust Ltd* [1987] 1 All E.R. 281 and Warburton, *Unauthorised Acts by Charities* [1987] Trust L & P 46, 48.

⁵ For a more detailed consideration of these provisions see, Warburton, *Charitable Companies and the Companies Act 1989* [1990] Trust L & P 78.

⁶ Charities Act 1960 s.30A(1).

contributed to the charity are likely to be defeated.⁷

Restrictions on the use of property held by a charitable company may appear otherwise than in the objects clause in the memorandum. For example, specific property may be required to be held for separate purposes by a clause in the memorandum or articles of association. To ensure that all property is retained for charitable purposes, the Charities Act 1992 s.40 amends s.30A(2) of the 1960 Act to require the prior written consent of the Charity Commissioners to be obtained for the alteration of any provision directing or restricting the manner in which property of a charitable company may be used or applied. The dual supervision of charitable companies is confirmed by the requirement in s.30A(3) for a copy of the Charity Commissioners' consent to be sent to the Registrar of Companies when notifying the alteration.⁸

Powers of Directors

The removal of limitations on the powers of directors in favour of third parties was potentially damaging for charitable companies and several restrictions were introduced by the Companies Act 1989 and the Charities Act 1992 in an endeavour to prevent outflow of funds and property for non-charitable purposes.⁹ In addition to restricting the operation of s.35A of the Companies Act 1985 to essentially commercial contracts,¹⁰ s.30B(4) of the Charities Act 1960 provides that an act of the directors which is beyond their powers because of the objects of the company can only be ratified with the prior written consent of the Charity Commissioners. Similar consent is required before an unauthorised transaction between a charitable company and one of its directors or his associate, which would otherwise be void under s.322A of the Companies Act 1985, can be ratified.

The Charities Act 1992 imposes further restrictions on specified transactions between a charitable company and its directors. Essentially, by s.30BA of the Charities Act 1960, any transaction which involves a transfer of assets or funds to a director requires the prior written consent of the Charity Commissioners even if it is a transaction which is within the powers of the company. The specified transactions, which in any other company would simply need the approval of the company, are as follows (together with the relevant section of the Companies Act 1985):

- (a) acquisition of assets by or from a director or his associate, s.322(2)(c);
- (b) payment to a director in respect of loss of office or retirement, s.312;
- (c) payment to a director in respect of loss of office or retirement in connection

⁷ See [1971] Ch. Comm. Rep. paras 26-29.

⁸ Failure to submit the Charity Commissioners' consent is an offence - Charities Act 1960 s.30A(4).

⁹ See, for example, the NCVO Report, "Malpractice in Fundraising for Charity", para 5.39 (captive charities and the diversion of funds into the hands of directors).

¹⁰ See the text above at fn.5.

- with the transfer of undertaking or property of the company, s.313(1);
- (d) the incorporation in a director's service contract of a term whereby his employment may continue for more than 5 years, s.319(3);
 - (e) an arrangement whereby assets are acquired by or from a director or person connected with him, s.320(1); and
 - (f) the provision of funds to meet certain expenses incurred by a director, s.337(3)(a).

Recent pronouncements by both the Charity Commissioners¹¹ and the courts¹² as to the desirability of trustees and others concerned with charities remaining unpaid, indicate that consent will only be forthcoming in exceptional circumstances.

Publication of Name and Charitable Status

The property of a charitable company is protected in the event of an unauthorised transaction if the other contracting party knew that the company was a charity.¹³ To ensure that people are aware that they are dealing with a charitable company the Companies Act 1989 inserted s.30C in the Charities Act 1960 which requires that a charitable company which does not have the word "charity" or "charitable" in its name must state the fact that the company is a charity in English in legible characters on the following documents:

¹¹ [1988] Ch. Comm. Rep. para 38.

¹² *Smallpiece v Attorney-General* [1990] Ch. Comm. Rep. App D.

¹³ Charities Act 1960 s.30B(1), and see the text above at fn.4.

- (a) all business letters of the company;
- (b) all its notices and other official publications;
- (c) all bills of exchange, promissory notes, endorsements, cheques and orders for money or goods purporting to be signed on behalf of the company;
- (d) all conveyances¹⁴ purporting to be executed by the company; and
- (e) bills rendered by it and in all its invoices, receipts and letters of credit.

The publication provisions are strengthened by the Charities Act 1992 which requires that a charitable company must publish its name¹⁵ on the same documents, save conveyances, even if it is exempted from the general requirements as to publication of name by s.30(7) of the Companies Act 1985. The provision becomes s.30BB of the Charities Act 1960.

Winding-up

The White Paper pointed out, at para 5.21, that, whilst the Attorney-General could present a petition for a charitable company to be wound up, the Charity Commissioners could not. That defect in the Charity Commissioners' powers is remedied by s.10 of the Charities Act 1992 which adds five new subsections to s.30 of the Charities Act 1960.

The Charity Commissioners now have power to present a winding-up petition but only after they have instituted an inquiry under s.6 of the 1960 Act. Further, the Commissioners must be satisfied either that there is or has been misconduct or mismanagement in the administration of the charity or that it is desirable or necessary to act for the purpose of protecting the property of the charity or securing a proper application for the purposes of the charity of that property or property coming to the charity. If the Commissioners have not undertaken a s.6 inquiry, a petition may still be presented by the Attorney-General.¹⁶

The Commissioners are also given power by s.30(3) of the 1960 Act, as amended, to apply to the court under s.651 of the Companies Act 1985 for a declaration that the dissolution of a charitable company which has already taken place is void. Any such application should normally be made within two years of the dissolution. If a dissolution is declared void, proceedings may then be taken as if the company had not been dissolved, thus permitting assets to be recovered. It should be remembered that although the winding-up of a charitable company is dealt with under the Insolvency Act 1986, regard must be had to any specific directions in the memorandum of the

¹⁴ "Conveyance" means any instrument creating, transferring, varying or extinguishing any interest in land - Charities Act 1960 s.30C(2).

¹⁵ i.e., it must comply with Companies Act 1985 s.349(1) and failure to comply with the Section is an offence - Charities Act 1960 s.30C(3).

¹⁶ Charities Act 1960 s.30(1).

company.¹⁷ The usual direction is that surplus assets are to be transferred to some other charity. Accordingly, any assets recovered after a dissolution has been declared void will be dealt with *cy-près*.

If the name of a charitable company has been struck off the register of companies as defunct under s.652 of the Companies Act 1985, the Charity Commissioners are empowered to make an application under s.653(2) of that Act for the company's name to be restored to the register.¹⁸ An application must be made within 20 years of the publication of the striking off notice in the Gazette. This provision will also enable the Charity Commissioners to recover property which has been misapplied by a charitable company. The power, like that of applying to declare the dissolution of a charitable company void, can only be exercised with the consent of the Attorney-General.

Conclusion

The provisions in the Companies Act 1989 and the Charities Act 1992 place charitable companies more closely under the supervision of the Charity Commissioners, whilst leaving them still subject to company law. At the same time, the 1992 Act imposes on other charities new obligations, many of which are derived from company law, for example, the power of the Charity Commissioners to order a charity to change its name. Although based on company law, some of the new provisions do not apply to charitable companies, for example, the requirements as to submission and auditing of accounts: charitable companies remain subject to the provisions of the Companies Act 1985 in relation to submission and auditing of accounts.

The present duality of supervision of charitable companies is not only unduly burdensome for the charities but also leads to unnecessary complications. Thus a new separate accounting regime may have to be issued for charitable companies under s.257 of the Companies Act 1985 to ensure that charitable companies are subject to the same accounting provisions as unincorporated charities. Has the time not now been reached when a uniform set of provisions for supervision and control should be applied to all charities regardless of their legal structure?

¹⁷ *Liverpool and District Hospital for Disease of the Heart v Attorney-General* [1981] 1 All ER 994.

¹⁸ Charities Act 1960 s.30(4).