

**CHAPTER 4:****EXEMPT CHARITIES****1. Proposal**

- 1.1 This Regulatory Impact Assessment (RIA) examines the impact of the measures to be included in the Charities Bill on charities that are exempt from registration with the Charity Commission. These are covered by the Charities Act 1993 in Sections 3(5A)(a), 3(5A)(b), 3(5B)(a)(i), 3(5B)(a)(ii), 24(8), 25(2) and in Schedule 2. In certain respects, the contents of this RIA go beyond the provisions included on the face of the Bill. The decision to include the additional material has been taken in order to enable the reader to gain a more complete understanding of the proposals.

**Purpose and intended effect*****Objective***

- 1.2 Proposals for changes to the arrangements governing exempt charities are set out in "Private Action, Public Benefit" a report by the Prime Minister's Strategy Unit. One of the main themes of the report was that charities need to demonstrate greater accountability and transparency if public trust in charities is to be maintained. The objective of the proposed changes to exempt charities is to promote confidence in the integrity of charitable status by providing for all exempt charities to be subject to the same accountability and transparency requirements as charities which are registered with the Commission. Those organisations which will be affected are exempt charities, the existing regulators of those charities and the Commission.
- 1.3 The Strategy Unit made the following recommendations which the Government accepted.
- The monitoring regimes to which housing associations, universities and colleges as exempt organisations are subject should be adapted to cover basic charity law requirements.
  - The reports and accounts of exempt charities should clearly set out the voluntary funds they hold and how they use them. The same level of information about exempt charities as is required of charities should be made accessible on or via the Commission website.
  - The Commission should be given the power to investigate exempt organisations on the request of their 'principal regulator'.
  - Larger exempt charities without a 'principal regulator' should be registered with the Commission.

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1.4 The table below lists the currently exempt charities and their proposed principal regulator:

<b>Provision</b>	<b>Description</b>	<b>Proposed regulator</b>
<b>Section 3 of the 1993 Act</b>		
Section 3(5A)(a)	Higher education corporations	Higher Education Funding Council for England
Section 3(5A)(b)	Further education corporations	Learning and Skills Council
Section 3(5B)(a)(i)	Foundation and voluntary schools	Charity Commission
Section 3(5B)(a)(ii)	Education Action Forums	Charity Commission
Section 24(8)	Common investment funds	Charity Commission
Section 25(2)	Common deposit schemes	Charity Commission
	Common deposit funds	Charity Commission
<b>Paragraph of Schedule 2</b>		
(a)	Several universities	Higher Education Funding Council for England
	Property falling within the Methodist Church Funds Act 1960	Charity Commission
	The representative body of the Welsh Church and property vested in or administered by it	Charity Commission
	Property within the Church Funds Investment Measure 1958	Charity Commission
(b)	Universities of Oxford, Cambridge, London, Durham and Newcastle	Higher Education Funding Council for England
	Colleges and halls in the universities of Oxford, Cambridge and Durham	Charity Commission
	Queen Mary and Westfield College in the University of London	Higher Education Funding Council for England
	The colleges of Winchester and Eton	Charity Commission
(c)	Any university, university college or institution connected with a university or university college which Her Majesty declares by Order in Council to be an exempt charity for the purposes of the Charities Act 1993	Higher Education Funding Council for England (universities in England), Charity Commission (universities in Wales and university colleges and institutions connected with a university in England and Wales)

(d)	[Repealed]	
(da)	The Qualifications and Curriculum Authority	Department for Education and Skills
(e)	[Repealed]	
(f)	The Qualifications, Curriculum and Assessment Authority for Wales	Welsh Assembly Government
(g)	[Repealed]	
(h)	[Repealed]	
(i)	A successor company to a higher education corporation (within the meaning of section 129(5) of the Education Reform Act 1988) at a time when an institution conducted by the company is for the time being designated under that section	Higher Education Funding Council for England (organisations in England) and the Charity Commission (organisations in Wales)
(j)	[Repealed]	
(k)	Victoria and Albert Museum	Department for Culture, Media and Sport
(l)	Science Museum	Department for Culture, Media and Sport
(m)	Armouries	Department for Culture, Media and Sport
(n)	Royal Botanic Gardens, Kew	Department for Environment, Food and Rural Affairs
(o)	National Museums and Galleries on Merseyside	Department for Culture, Media and Sport
(p)	British Museum	Department for Culture, Media and Sport
	Natural History Museum	Department for Culture, Media and Sport
(q)	National Gallery	Department for Culture, Media and Sport
(r)	Tate Gallery	Department for Culture, Media and Sport
(s)	National Portrait Gallery	Department for Culture, Media and Sport
(t)	Wallace Collection	Department for Culture, Media and Sport
(u)	Imperial War Museum	Department for Culture, Media and Sport
(v)	National Maritime Museum	Department for Culture, Media and Sport

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(w)	Any institution which is administered by or on behalf of an institution included above and is established for the general purposes of, or for any special purpose of or in connection with, the last named institutions	As for the parent institution except students' unions who would be required to register with the Charity Commission
(x)	The Church Commissioners and any institution which is administered by them	Charity Commission
(y)	Any charitable registered society within the meaning of the Industrial and Provident Societies Act 1965	Housing Corporation for RSLs, Charity Commission for others
	Any charitable registered society or branch within the meaning of the Friendly Societies Act 1974	
(z)	Museum of London	Department for Culture, Media and Sport
(za)	British Library	Department for Culture, Media and Sport
(zb)	Community Fund	Department for Culture, Media and Sport

1.5 So far we have established that there are 47 Higher Education corporations, approximately 400 Further Education Corporations, and approximately 8,000 Foundation and Voluntary schools. We believe that the vast majority of these schools will exceed the £100,000 threshold. The Joint Committee that scrutinised the draft Charities Bill recommended that the Government should designate a principal regulator for foundation and voluntary schools. However, it has not been possible to identify a principal regulator for the voluntary and foundation schools. There are approximately 8,000 Industrial and Provident Societies and Registered Friendly Societies and the Financial Services Authority have estimated that approximately 1,000 of those might be charitable. Nearly all the Industrial and Provident Societies which are registered social landlords will have an income in excess of £100,000.

1.6 The following is the list of key principles of charity regulation as drawn up by the Charity Commission (the Commission) and agreed by the Home Office. Monitoring by proposed principal regulators would have to achieve the following:

- a) cover all assets of a charity regardless of their source;
- b) have the objective of ensuring that the assets of a charity are applied solely for the purpose of furthering its objects, which must be for the public benefit;
- c) have the objective of ensuring that the governance arrangements of a charity are adequate for the effective and efficient furtherance of its objects, and are followed in the administration of the charity;
- d) have the objective of ensuring that changes are made to a charity's objects or governance arrangements when they are necessary for it to continue to operate effectively;
- e) have the objective of ensuring that the charity complies with all relevant legal requirements, for example in relation to the raising of funds from the public;
- f) require the charity to provide to all stakeholders adequate financial information about the use and application of the resources entrusted to it;
- g) provide appropriate machinery for effective debt management, and for the reconstruction or dissolution of the charity including the application of any assets, after the settlement of all liabilities, for suitable alternative charitable purposes; and
- h) be based on the principles of good regulation.

### **Background**

- 1.7 Exempt Charities enjoy the status and the fiscal benefits accorded to other charities. Like all charities, they are required to comply with the key principles of charity law but since 1992 they have not been allowed to register with the Commission and they fall outside the monitoring and investigative powers of the Commission, though not of their advice giving powers. The grounds for their exemption from the requirement to register with the Commission has been that they are adequately supervised by another Government department or public authority. However, while it is true that they are regulated in respect of other activities and functions which they undertake, there is no mechanism for monitoring their compliance with charity law. They do not have to demonstrate that they continue to merit the considerable benefits, both fiscal and in terms of public esteem, which flow from having charitable status.
- 1.8 It is vital that public trust and confidence in the charitable sector should be maintained and if possible increased. Many charities rely heavily for

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their survival and growth on income from fundraising and on the work of volunteers. Without continued public goodwill and support, the activities of charities are likely to be significantly curtailed. Research indicates that, while overall levels of public trust in charities are high, the public has concerns about the quality of information available about charities and about their degree of accountability. Failure to ensure that information about exempt charities is readily available to the public and that those charities are held to account could result in the public having doubts about the probity and effectiveness of charities.

- 1.9 Many exempt charities, such as universities and housing associations, are subject to regulation but currently there is no mechanism for the independent monitoring of their compliance with the principles of charity law. The Prime Minister's Strategy Unit found that some of those organisations were unaware of the requirements of charity law regarding, for example, governance arrangements and stewardship of funds. A lack of awareness of charity law and/or a lack of charity focussed regulation creates a risk that charitable assets will be lost or misapplied. While the public can obtain certain information about the affairs of exempt charities, it is more limited and less readily available than that for registered charities.
- 1.10 The 69 responses to the Strategy Unit proposals on this issue showed a clear acceptance, from both exempt charities and others, of the principle that all organisations enjoying the advantages of charitable status should, in return for those advantages, comply with the basic principles of charity law.
- 1.11 The Government's aim with these proposals is to establish arrangements that secure greater accountability and compliance with charity law by exempt charities, while imposing the minimum of extra bureaucracy.

### **Risk assessment**

- 1.12 The public sees charities as being value-driven and tends to have much higher expectations of charities than of non-charitable organisations. Charities rely on having a good reputation in order to stay in business. The absence of an effective mechanism for monitoring the compliance of exempt charities with the principles of charity law poses threats to the public perception of the integrity of charitable status, a threat which might not be confined to exempt charities but could extend to the whole of the charitable sector. A loss of public confidence in charities would be likely to result in a drop in charitable giving and a reduction in the number of volunteers which they would attract to work for them. As a consequence charities would become very much less effective. Since a dynamic and vibrant charitable sector makes a vital contribution to the economy of the UK

and to wider society, it is important that measures should be put in place to maintain public trust in the integrity of charities.

- 1.13 Research published by the National Council for Voluntary Organisations in 1998 “Blurred Vision, Research Quarterly” 1<sup>st</sup> January, indicated that overall the level of trust in charities is high but it identified concerns about the accountability of charities and about the quality of information available about them. Exempt charities are not held to account for their compliance with charity law and, although an exempt charity is obliged to provide information to a member of the public on demand, that information consists solely of basic accounts. A decision to retain the status quo for exempt charities would not address the public concerns identified in the research.
- 1.14 Exempt charities which do not have a clear understanding of charity law and which are not complying with it could find their failures exposed publicly with dire consequences for the future of the charity through the loss of public confidence in it. Adverse publicity could have a negative impact on the charitable sector as a whole.
- 1.15 There is a potential risk that the charitable funds and assets of an exempt charity might be being erroneously applied or even lost but, in the absence of a monitoring mechanism, that might never be identified or identified too late for the funds to be safeguarded.
- 1.16 A failure on the part of Government to address the lack of regulation for exempt charities would give rise to serious complaint from the very large number of charities who are required to register with the Commission. Registered charities see no rationale for exempt charities being allowed to continue in their present state of unaccountability. They see it as an unjustified privilege which puts the integrity of the whole sector potentially in jeopardy. In 2001 the National Council for Voluntary Organisations in their consultation document on charity law reform, “For the public benefit” identified the anomalous position of exempt charities and referred to evidence which they had received which indicated that some exempt charities did not comply with charity law principles in all respects.

### **Options**

- 1.17 We have identified 2 options for reforming the law on exempt charities so as to provide greater accountability. Those options are considered below together with the option to maintain the status quo.

#### **Option 1 – leave the relevant legislation unchanged**

- 1.18 That would not meet the objectives set out in paragraph 1.2 to 1.3 and would leave unaddressed the concerns identified at 1.12 to 1.16

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### **Option 2** – make all exempt charities register with the Commission.

- 1.19 That would meet the objectives of delivering increased accountability and transparency but there is also a risk involved of excessive regulation.
- 1.20 The Government is aware that in some sectors exempt charities are already highly regulated, for example, Higher Education Institutions (HEIs). The Better Regulation Task Force concluded in 2002 that HEIs were in some respects overburdened with bureaucracy.
- 1.21 For those exempt charities where there is a principal regulator requiring them to register also with the Commission could give rise to a significant duplication of regulation. Many exempt charities are, for example, already required to produce detailed financial accounts for their existing regulators. Creating an entirely new additional regulatory regime could in those circumstances place an unnecessary regulatory burden on those exempt charities. Charities could end up collecting and providing two lots of very similar information and simply presenting it in different formats for two regulators.

### **Option 3** – implement the Strategy Unit proposals contained in "Private Action, Public Benefit" and which are set out in paragraph 1.3 of this document and those recommendations of the Joint Committee, which the Government has accepted.

- 1.22 The adoption of this option would meet the objective of providing greater accountability and transparency with the minimum possible regulatory burden placed upon exempt charities.
- 1.23 There are some risks involved in this option. It is possible that members of the public and other charities might contend that charities are not being regulated properly unless they are registered with the Commission, the regulator of charities, and that there is not a 'level playing field' throughout the sector. However, as the bodies which would be performing the principal regulator role would all be ones of standing and as the same level of information would be available to the general public in respect of exempt charities as would be available for registered charities, that contention would have less weight.
- 1.24 A principal regulator is unlikely to have expertise in charity law and costs would arise for the regulator in obtaining training in charity law and in devising the form of regulation they would apply. However, many of the principles of good governance are common to both charitable and non charitable organisations and principal regulators would be able to call upon the Commission for advice and guidance on how best to carry out the monitoring role. The Commission have begun a round of discussions with the principal regulators about the regulatory mechanisms to be employed. The mechanism would be

different in the case of each regulator. Principal regulators and the Commission working together would be able to identify the gaps in expertise and deficiencies in existing mechanisms and decide how to remedy them.

- 1.25 It is probable that changes would be required to legislation applying to some principal regulators to give them the necessary powers to carry out their monitoring role. The regulators are in discussion with their legal advisers and would report expect to be in a position to let us have information shortly about the legislative changes which would be needed. Clause 13 of the Bill enables those changes to be made by regulations.
- 1.26 There will be some inconsistency as different regulatory regimes would apply to universities in England and Wales. In England they would be regulated for their compliance with charity law by HEfCE but in Wales they would be regulated by the Commission. While there is scope for confusion in this it should, in practice, be kept to a minimum by effective liaison between regulators to produce consistent communication and application of regulatory requirements.

### **Benefits**

**Option 1** – retaining the status quo.

- 1.27 No new regulatory burden would be imposed.

**Option 2** – make all exempt charities register with the Commission.

- 1.28 There would be several benefits. This option would deliver the Government's aim of accountability and transparency through monitoring and provision of information. There would be consistency and a 'level playing field' which is desired by many in the charitable sector.
- 1.29 Every charity would be directly regulated by the Commission, the organisation which has the best understanding of and greatest expertise in charity law and which has significant powers of investigation and intervention. There would be no need to train principal regulators in charity law.
- 1.30 It would not be necessary to amend the legislation governing principal regulators to give them the necessary powers to carry out the monitoring role.

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**Option 3** — implement the strategy unit proposals set out in "Private Action, Public Benefit" as amended by those recommendations of the Joint Committee, which the Government has accepted.

- 1.31 Exempt charities would be regulated in regard to charity law and the same levels of information about them would be available to the general public as is currently available about registered charities.
- 1.32 The principal regulator, if it had concerns about a charity, would be able to invite the Commission to exercise its powers of investigation and intervention. As a result of the Joint Committee's recommendation the Commission would be required to consult with the principal regulator before using any of its enforcement powers in relation to an exempt charity. That consultation requirement would be a requirement on the Commission to explain to the principal regulator what action it intended to take, and why; and to take account of the principal regulator's views. However, the principal regulator would not have the right to veto the proposed action.
- 1.33 It is probable that exempt charities which have a principal regulator would not face a dramatic change in what is expected of them. They should already be complying with charity law. Information required for compliance in many cases would not be significantly more than is already expected by their existing regulator in terms of annual returns, though there would undoubtedly be some increase in regulatory burden due to the requirement to provide charity specific information.
- 1.34 Proposed principal regulators would already have a working knowledge of the exempt charities they would be regulating and should be able to devise a mechanism which would be customised to the circumstances of the charity and would be proportionate, targeted and focussed on risk.
- 1.35 Principal regulators would be able to assess compliance with charity law as part of their usual monitoring processes, using existing forms and reporting mechanisms adjusted to include charity law requirements. That should reduce the bureaucratic burden compared with that in Option 2.

### **Equity and fairness**

- 1.36 Option 1 would continue the current situation whereby exempt charities, unlike registered charities, are not monitored for their compliance with charity law although they receive the fiscal benefits associated with being a charity. Option 2 could disproportionately affect those exempt charities which already undergo heavy regulation, for example the higher education sector. Conversely, registered charities could argue that exempt charities are unjustifiably being accorded special treatment if option 3 were to be adopted. Many

registered charities, e.g. Barnardos, are multiply regulated because of the range of services they provide.

- 1.37 Consideration has been given to the impact of these proposals on minority groups. It is not considered that these proposals would have a disproportionate impact on such groups.

### **Business sectors affected**

- 1.38 Higher Education Institutions, Museums and Galleries, Further Education Corporations, Foundation and Voluntary Schools, Church Commissioners, Registered Social Landlords, Industrial and Provident Societies, Registered Friendly Societies, Common Investment/ Deposit Funds/Schemes.

### **Costs**

- 1.39 We have tried to estimate the costs to charities' principal regulators and the Commission of each of the 3 options put forward. We are restricted, however, by a lack of information and the costing remains speculative. Notwithstanding that, we have established, as far as is possible that:

- although the number of Foundation and Voluntary schools fluctuates somewhat, the current figures indicate that there are 4,720 Church of England schools, 2,074 Roman Catholic, 33 Jewish and 4 Muslim as well as a small number of schools from other faiths. As it currently stands, it is anticipated that the vast majority of these schools will exceed the £100,000 annual income threshold over a period of 5 years.
- the number of charitable Industrial and Provident Societies and Registered Friendly Societies, has been estimated at 1,000. We believe that nearly all the Industrial and Provident Societies which are registered social landlords will have an income in excess of £100,000, but we do not know the income level of other members of this group as that information is not held centrally.

- 1.40 As explained above, there are major gaps in our knowledge, which are set out below.
- We do not know anything about the extent to which exempt charities currently comply with charity law and there is no easy or obvious way to obtain the information. For the purposes of this exercise we have assumed that they do currently comply, as they should under current legislation. One of the benefits of Option 3 is that it would enable the principal regulators or the Commission to confirm whether the charities have been complying with charity law and to offer advice and guidance where non-compliance has been identified.

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- Full details of the changes required to the principal regulators' monitoring arrangements, so that they cover basic charity law requirements, are yet to be finalised. Work is continuing to establish the extent of the changes required, and it would be for the principal regulators to develop procedures for regulating charity law compliance of the charities within their jurisdiction.
- We do not know how much training in charity law principal regulators would need to make them effective. That would be established at meetings between the Commission and principal regulators.
- We do not know how often the Commission may be called upon to intervene in the affairs of a charity where there is cause for concern and how protracted and complex such intervention might be. However, the Commission investigates around 1 in every 500 out of the 166,129 principal charities on the register in a year. The costs to the charity involved are extremely varied, depending on the nature of the investigation and the measures taken by the Commission. Investigations are expected to benefit the charity involved by providing better governance and preventing the improper use of charitable assets. Given the fact that the vast majority of exempt charities have been subject to regulatory regimes of some sort before and that 80% of them are involved in the same sector, the Commission anticipates that the incidence of investigation would, if anything, be lower.

### **Option 1** – retaining the status quo.

- 1.41 That would generate no obvious costs to charities, principal regulators or the Commission. The principal cost is the continued risk to public confidence in charities.

### **Option 2** – make all exempt charities register with the Commission.

- 1.42 If Option 2 was adopted, charities might be involved in duplicate work with attendant costs. It is probable that they already collect for the principal regulator some of the same information that the Commission would require. Charities might be involved in submitting similar information but in a slightly different format to two regulators. There might similarly be an overlap between the principal regulator and the Commission in monitoring the information supplied.
- 1.43 We have been unable to come up with substantiated figures which would set out the costs, either financial or in terms of time, to individual exempt charities. To date, there has been no research done on how long it takes charities to gather the information required by the Commission. The amount of extra work required would vary depending on the amount of information exempt charities already gathered. Under

charity law exempt charities, like any other charity, have a responsibility to produce some form of accounts.

- 1.44 The Commission has produced figures on the costs to charities of filling out their Annual Return form and these are summarised in the following table. The figures contained in the table are taken from the Compliance Cost Assessment which accompanied the Charities (Annual Return) Regulations 1997. The Standard Information Return, a measure affecting charities of over £1 million annual income, has not been taken into account. This has yet to be fully developed by the Commission but it is expected that it will not increase the costs for large charities by more than 25%.

<b>Type of Charity</b>	<b>First Year Costs</b>	<b>Subsequent Year Costs</b>
Light touch Charities (under £10,000 annual income)	£4.16	£1.80
Smaller Charities (Simple accounts): income between £10,000-£100,000.	£8.33	£6.00
Smaller Charities (Accrual accounts): £10,000-£100,000.	£14.60	£12.20
Larger Charities	£31.75	£23.80

In terms of time spent, the Commission estimate that it would take about 10 minutes for charities only updating the public record and half-an-hour for other charities to complete the annual return. That would increase to just over three-quarters of an hour for the larger charities as more sections of the annual return would be relevant to them<sup>1</sup>.

- 1.45 The following table sets out theoretical costs should the Commission act as the regulator for all exempt charities. They would have to register and regulate a substantial number of charities. They would not have to register or incorporate in their routine pro-active monitoring system those with an income under £100,000. However, they would have investigative and intervention powers which they would be called upon to exercise should a charity give cause for concern. The costs for these are included in the continuing annual Commission costs.

<sup>1</sup> There is generally a positive correlation between the cost of completing an annual return and the size of a charity. That is because as a charity's income grows it is likely that more of the sections on the Annual Return will be relevant to it.

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Area of work undertaken	Costs incurred
Registration (one off cost)	£900,000
Exercise of Legal Authority and giving of guidance	£234,000
Evaluations and Investigations	£49,500
Monitoring	£19,500
Referrals to legal	£29,000
Referrals to Financial Regulation.	£22,700
<b>Total Costs</b> (+/- 30% cost incurred to allow for inaccuracies):	One-off costs: <b>£630,000-£1,170,000</b>  Continuing: <b>£250,000-£450,000</b>  Combined: <b><u>£880,000-£1,620,000</u></b>

These costings are based on figures supplied by the Commission. A break-down of the figures can be found in **Annex A**.

**Option 3** — implement the Strategy Unit proposals set out in "Private Action, Public Benefit" and those recommendations of the Joint Committee, which the Government has accepted.

- 1.46 The costs of those proposals remain difficult to quantify. Costs would vary from one principal regulator to another. The regulatory regime which is devised must monitor compliance with charity law effectively but it does not have to mimic the Commission model. Existing systems should be adapted and built on and a risk focussed approach adopted to reduce the administrative burden. The principal regulators would devise the mechanism in discussion with the Commission.
- 1.47 The Higher Education Regulation Review Group has requested that further work be undertaken to assess the costs to exempt charities of complying with the monitoring processes established by principal regulators. The principal regulators would devise the monitoring mechanisms in discussion with the Commission and the Home Office. The input of exempt charities and their representative bodies will be sought in the development of these monitoring processes, and in identifying any costs to exempt charities for meeting them.

- 1.48 In the table below the costs to regulators have been calculated on the basis of adding 30% to the highest figures and subtracting 30% from the lowest figures of the anticipated costs based on the figures provided by the Commission. That has been done to reflect the greater degree of uncertainty around the information available on which to base our calculations. The figures are based on the assumption that approximately 1,200 charities would be monitored by an existing principal regulator. For this purpose the difference between the Commission costs for options 2 and 3 was taken and used to provide a rough estimate of possible costs.

<b>Area of work undertaken</b>	<b>Costs incurred</b>
Exercise of legal authority and giving of guidance	£19,250-£35,750
Evaluations and Investigations	£3,850-£7,150
Monitoring	£1,680-£3,120
Referrals to legal	£1,925-£3,575
Referrals to Financial Regulation.	£1,610-£2,990
	Total: £28,315-£52,585
<b>Total Costs</b> (+/- 30% cost incurred to allow for inaccuracies):	Total Continuing Costs:  <b><u>£19,820-£68,360</u></b>

Again, the figures are based on those figures provided by the Commission, a break-down of which can found in **Annex A**

- 1.49 The Commission would have the costs of providing advice and guidance to principal regulators and of investigating any serious concerns/malpractice in charities if invited to do so. They would have to register and regulate exempt charities with an income over £100,000 which do not have a principal regulator. In the case of charities with an income of less than £100,000 which do not have a principal regulator the Commission would not have to register them but they would be subject to the Commission's investigation and intervention powers in the usual way. The Commission would also have the cost of the advisory and guidance roles as well as the formal powers they are able to use in order to assist charities.

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- 1.50 The costs to the Commission are set out in the table below. The basis of the calculation are the figures supplied by the Commission and can be seen in **Annex A**.

Area of work undertaken	Costs incurred
Registration (1 <sup>st</sup> year only)	£780,000
Exercise of legal authority and giving of guidance	£206,500
Evaluations and Investigations	£44,000
Monitoring	£17,100
Referrals to legal	£26,250
Referrals to Financial Regulation.	£20,400
<b>Total Costs</b> (+/- 30% cost incurred to allow for inaccuracies):	First Year: <b>£546,000-£1,014,000</b> Continuing: <b>£220,000-£408,500</b>  Total: <b>£786,000-£1,422,500</b>

- 1.51 There would be additional costs to exempt charities in being monitored for charity law compliance but it is impossible to accurately quantify them. As yet the fine details of the potential regulatory regimes have not been worked out. Until they are, it is difficult to quantify the cost to charities of the proposals. The costs to the exempt charities required to register with the Commission would be as outlined at paragraph 1.43.
- 1.52 We remain committed to working out the fine details with each of the proposed principal regulators and the Commission. However, the circumstances for each individual regulator would vary, as each regulator may wish to adopt different approaches. Any figures that were produced would be highly unsubstantiated, not least because the figures are not available on how much it would cost charities to be regulated by the Commission (see paragraph 1.43).

### **Competition Assessment**

- 1.53 The proposals would impact on a wide variety of charitable institutions including Higher Education Institutions, Museums and Galleries, Further Education Corporations, Foundation and Voluntary schools, Church Commissioners, Registered Social Landlords, and charitable Industrial and Provident Societies.

- 1.54 Whilst the activities of some charities may mirror those of non-charitable organisations in the business world, there are significant differences in the use charities may make of their resources. Charity law prescribes that their resources may be used only in furtherance of their charitable objects. They may undertake trading which is directly connected to, or is ancillary to, furthering their charitable purposes. However, if charities wish to undertake substantial trading which is not in direct pursuit of its purposes, it must set up a separate trading company to do so. Neither the proposed changes to exempt charities nor any other proposals in the Charities Bill would in anyway affect that position.
- 1.55 To the extent that any charity might be said to compete with another e.g. for public funds, the impact of these proposals may in fact aid competition. It could be argued that exempt charities at present have an advantage over registered charities in that they are not at present subject to monitoring to check whether they are complying with charity law.
- 1.56 These proposals should not require a detailed assessment of the competitive impact, particularly in that they do not change the existing requirement that exempt charities must comply with charity law. Nor do they affect the legislation concerning trading.

#### **Small Firms' Impact Test**

- 1.57 The views of the Small Business Service have been sought as part of the consultation process. They had two specific concerns. Those were that Registered Social landlords should not face heavy additional regulatory burdens and that the more onerous accounting requirement for charities compared with those applying to small businesses might prove a burden. These concerns are satisfactorily addressed, however, by the fact that Registered Social Landlords would be monitored by the Housing Corporation using appropriately adapted existing mechanisms, thus reducing the administrative burden. The Small Business Service has accepted that stakeholders legitimately have a greater desire for more information about charities than they do about small businesses.

#### **Enforcements and Sanctions**

- 1.58 As the proposed principal regulators already carryout various regulatory functions most will already have certain powers to ensure compliance. It is the intention that they would be given additional powers where there are gaps. The Commission already possesses powers of enforcement and their locus in respect of exempt charities would be extended by the proposals.
- 1.59 The proposals would impose a new burden on principal regulators. The Home Office would need to transfer funds to the relevant other

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Government department's to cover the additional costs initially. Thereafter the expectation is that those costs would be part of the baseline funding received by the other Government departments. The Commission would continue to bid for funding direct from HM Treasury to cover the additional duties arising from the proposals.

- 1.60 Criminal sanctions could be applied in respect of breaches of charity law by exempt charities but no new offences are created by these proposals and Department for Constitutional Affairs has expressed no concern about them.

### **Monitoring and Review**

- 1.61 The Government might wish to review these measures after a period of approximately five years. The £100,000 registration threshold is intended to ease the transition for the Commission and for the smaller exempt charities. After five years this transitional period would effectively be complete and a review of the threshold level would be appropriate and could lead to a lower figure being introduced. Exempt charities without a principal regulator that are below the £100,000 threshold would effectively become excepted charities with immediate effect and so the five year review would cover charities that are currently exempt and excepted under the £100,000 threshold.

### **Consultation**

- 1.62 The consultation on the recommendations contained in "Private Action, Public Benefit" was carried out between 25 September to 31 December 2002. 1,087 written responses were received. A breakdown of the respondents by respondent type is contained in ANNEX A of "Charities and Not-for-Profits: A Modern legal Framework", the Government's response to the consultation, published in July 2003.

### **Summary and Recommendation**

- 1.63 Our clear preference is for Option 3. It best meets the objective of providing an effective mechanism for monitoring the compliance of exempt charities with charity law while ensuring that the regulatory regime is not unduly burdensome to charities or the proposed regulators. The costs and benefits for each option are summarised in the table below.

Option	Benefits	Costs
1. Retain the status quo	No additional benefits	<ul style="list-style-type: none"> <li>▪ No additional costs</li> <li>▪ A large number of charities would not be monitored for their compliance with charity law, although they would continue to receive the fiscal benefits awarded to the charitable sector.</li> </ul>
2. Make all exempt charities register with the Charity Commission	<ul style="list-style-type: none"> <li>▪ All exempt charities would be regulated for their compliance with charity law by the Commission, as the regulator for charities.</li> <li>▪ It would create a level playing field across the sector.</li> <li>▪ Increased public confidence in charities.</li> </ul>	<ul style="list-style-type: none"> <li>▪ One-off cost to the Commission in terms of registration of between <b>£630,000 and £1,170,000</b>.</li> <li>▪ Continuing annual costs to the Commission of between <b>£250,000 and £450,000</b> per annum.</li> <li>▪ Costs to the exempt charities of dual accounting and reporting requirements.</li> </ul>
3. Implement the Strategy Unit proposals as amended by the recommendation of the Joint Committee which the Government accepted.	<ul style="list-style-type: none"> <li>▪ All exempt charities would be regulated for their compliance with charity law.</li> <li>▪ Increased public confidence in charities.</li> <li>▪ The regulatory burden would be reduced for the exempt charities for which a principal regulator has been identified.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Continuing annual costs to the proposed principal regulators of between <b>£19,820 and £68,360</b> per annum.</li> <li>▪ One-off cost to the Commission in terms of registration of between <b>£546,000 and £1,014,000</b> per annum.</li> <li>▪ Continuing annual costs to the Commission of between <b>£220,000 and £408,500</b> per annum.</li> <li>▪ Increased costs for the charities of preparing annual returns and reports and submitting other documentation to the Commission. Costs of completing the annual return £31.75 in the first year and £23.80 in subsequent years. Costs of preparing additional material to the principal regulator, if required.</li> </ul>

## CHAPTER 4

### ANNEX A:

#### Commission Costs in RIA on Proposals For Exempt Charities

To begin with some notes on context and underlying assumptions.

**Numbers.** a round figure of 10,000 exempt charities was used. This seemed a reasonable figure leaving aside the uncertainties of the number of charities falling within paragraph (w) of the table after paragraph 1.4 of the RIA. While we have information in relation to students' union, we have not been able to locate figures for the other charities falling within this paragraph.

**Voluntary and Foundation Schools.** This is by far the biggest category of the 10,000 being c8,300 of them (c900 Fdn and c7,400 Vol). Based on discussions we have had with the Church of England and the Roman Catholics we understand that virtually all voluntary schools would have incomes in excess of the £100,000 threshold in the first few years.

**Ranges.** Having calculated a figure it is used as the mid point of a range, plus/minus 30% to allow for the many variables and uncertainties.

**Costs.** The basic unit costs and number of actions upon which the figures are based are taken from the Commission targets for 2003/4.

There are two types of costs. The estimated costs of registration would be a one-off cost (possibly spread over several years). The other costs would occur annually.

#### Options.

**Option 1:** Being no change it hasn't been costed.

**Option 2:** All charities register with the Commission and so within their normal jurisdiction

**Option 3:** Those with an acceptable principal regulator do not have to register and the Commission would only use their investigative/protective powers on request. As it is currently understood such requests would be infrequent. Information on charities with a principal regulator is made available on or via the Commission website.

Each aspect has been looked at from two angles:

**Simple Costs.** It has been assumed that, proportionately, currently exempt charities that have to register will produce the same amount of work as other charities.

**Adjusting our Proportion and Risk Thresholds ("Adjusted Costs").** In some areas there is also the option of reducing additional costs by adjusting

the Commission's approach to regulatory and support work (very broadly speaking, spread the Commission's resources more thinly).

The registration costs have not been adjusted here - if 9,000 charities become registrable for the first time the Commission is obliged to register them.

In other areas there is more flexibility. The Commission take a proportionate, risk based approach to their regulatory and advisory work, concentrating resources on areas of greater risk.

Risk assessments could be adjusted to contain elements of the additional work within current resources. For example, the Commission determines the criteria for opening a full investigation and/or for keeping investigations open.

The Commission could do this to varying degrees. For illustrative purposes the effect of reducing the impact on areas of flexibility by 50% has been shown.

Having noted that this approach could reduce additional costs to the Commission, it would also increase the risks of charitable assets being lost/misapplied, charities getting into difficulties and so on. More generally these increased risks for individual charities would also increase the risk of public confidence being undermined.

It should also be noted that, while the Commission is generally able to take operational decisions along these lines, it would be dependent on acceptance by bodies responsible for the external scrutiny of the Commission. For example, if the NAO criticised us for the increased risks inherent in this approach, it could not be sustained.

### **Benefits/Balance**

#### **Two further points:**

The costs of registering currently exempt charities will be far less than the long term savings that result from raising the general registration threshold.

The changes are not about regulation for its own sake. Charities benefit in a number of ways from being fully within the Commission's jurisdiction (registered or not). The Commission's investigative and protective powers can put charities back on a proper footing and ensure that charitable assets are protected and properly applied. Access to their advisory powers and guidance will benefit charities in a variety of ways.

## CHAPTER 4

### **Calculations**

#### **Registration**

A round figure of £100 pounds per registration has been used. This is based on the Commission target figure for staff cost per registration, adjusted to reflect the assumption that there will be little doubt about the charitable status of most of the currently exempt charities, so reducing the number of rejected/not proceeded with applications arising from the proposals.

#### **Cost to Commission**

##### **One-off costs**

**Option 2:** Estimate that 90% of charities will have to register: 9,000 @ £100 = £900,000

**Option 3:** Estimate 1,200 of above figure will have principal regulator (Universities, Further Education Institutions, Museums, currently exempt RSLs etc): 7,800 @ £100 = £780,000

This is the same for both Simple Costs and Adjusted Costs.

##### **Annual Costs**

###### Assumptions:

- That all 10,000 exempt charities will have an income over £100,000
- Work with principal regulators is covered partly within current work with outside bodies and partly within the range of costs that relate to guidance, evaluation and investigation.
- Costs of annual return process and mailing costs of adding to the register are taken to be covered by the +30% element of activities that arise from scrutiny (evaluations and so on).
- Costs of information provision regarding charities with principal regulator are difficult to estimate but likely to be relatively small and able to be contained within the scope for variation in the ranges.
- Under option 3 it has been estimated that 12% of charities will be under a principal regulator. Some costs are therefore reduced by 12% but investigation and evaluation costs reduced by 10% to allow for some action at request of the regulator.
- For adjusted costs it has been assumed that the exercise of legal authority will remain the same but reduced other figures by 50%.

**Simple Costs**

Costs in the following areas:

**Exercise of Legal Authority and giving of guidance**

**Option 2: £334,000**

**Option 3: £294,000**

**Evaluations and Investigations**

**Option 2: £99,100**

**Option 3: £88,000**

**Monitoring**

**Option 2: £38,900**

**Option 3: £34,200**

**Referrals to Legal**

**Option 2: £58,000**

**Option 3: £52,500**

**Referrals to Financial Regulation**

**Option 2: £45,400**

**Option 3: £41,000**

**Adjusted Costs**

**Exercise of Legal Authority and giving of guidance**

**Option 2: £234,000**

**Option 3: £206,500**

**Evaluations and Investigations**

**Option 2: £49,500**

**Option 3: £44,000**

## CHAPTER 4

### **Monitoring**

**Option 2:** £19,500

**Option 3:** £17,100

### **Referrals to Legal**

**Option 2:** £29,000

**Option 3:** £26,250

### **Referrals to Financial Regulation**

**Option 2:** £22,700

**Option 3:** £20,400

### **Benefits**

As mentioned above, there are benefits for charities and their beneficiaries. Investigations can identify and deal with problems in charities so protecting and/or releasing charitable assets for proper application.

Similarly, the Commission advice and guidance helps charities to operate in accordance with charity law and standards of best practice. This applies not only in a general sense but also in particular cases where Commission assistance – often involving the use of their formal powers – can help charities in many ways.

### **Overall**

The above would give us the following:

#### **A. Simple Costs**

##### **Option 2:**

One-Off Registration Costs: A figure of £900,000 leading to a range of £630,000 - £1,170,000 (+/- 30% with a bit of rounding where appropriate)

Continuing Annual Costs: £575,000 leading to £400,000 – £745,000

##### **Option 3:**

Registration: £780,000 leading to a range of £546,000 - £1,014,000

Annual Costs: £510,000 leading to £357,000 – £663,000

**B. Adjusted Costs**

**Option 2:**

Registration: As Above: £630,000 - £1,170,000

Annual Costs: £250,000 – 450,000

**Option 3:**

Registration: As above: £546,000 - £1,014,000

Annual Costs: £220,000 – £408,500

