

BRIEFING NOTE:

25 July 2017

Charity Governance Code – publication of 3rd edition

At a glance:

- Following a public consultation, the 3rd edition of the Charity Governance Code was published on 12 July 2017 - <https://www.charitygovernancecode.org/en>
- Charity Commission confirms its support and endorsement of the Code
- What does this mean for charities and their trustees?

Please see our February 2017 briefing note on the draft Code for background details: [http://filanthropia.co.uk/Briefing_note_draft_revised_Charity_Governance_Code_and_Charity_Commission%27s_Revised_Regulatory_Statement_\(Feb_2017\).pdf](http://filanthropia.co.uk/Briefing_note_draft_revised_Charity_Governance_Code_and_Charity_Commission%27s_Revised_Regulatory_Statement_(Feb_2017).pdf)

Contents of the finalised Code

Governance principles

As with the draft Code, the final version begins with the underlying “Foundation Principle” that all trustees:

- are committed to their charity’s cause and have joined the board because they want to help the charity deliver its purposes most effectively for public benefit;
- recognise that meeting their charity’s stated public benefit is an ongoing requirement;
- understand their roles and legal responsibilities and, in particular, they have read and understand:-
 - o the Charity Commission’s guidance CC3 *The Essential Trustee, what you need to know, what you need to do* <https://www.gov.uk/government/publications/the-essential-trustee-what-you-need-to-know-cc3>¹; and
 - o their charity’s governing document; and
- are committed to good governance and want to continue to their charity’s continued improvement.

¹ CC3 sets out the six key legal duties and responsibilities of charity trustees together with best practice recommendations. We have produced an introductory guidance on such legal duties and responsibilities (based on CC3). If you would like a copy please contact Sarah Chiappini: sarah@filanthropia.co.uk

Following the Foundation Principle there seven specific governance principles (again, which are the same as those in the draft). These fall under the headings of:-

1. Organisational purpose
2. Leadership
3. Integrity
4. Decision-making, risk and control
5. Board effectiveness
6. Diversity
7. Openness and accountability

The Code sets out under each of the seven principles the rationale for the particular principle; an expectation of key outcomes; and various recommended practice.

Justification regarding re-appointment where a trustee has served for nine years

The final Code reflects the provisions of the draft Code in that where a trustee has served for nine years, any further re-appointment should be subject to a particularly rigorous review; takes into account the need for progressive refreshing of the board; and is explained in the trustees' annual report.

In theory this is sound, but in practice with the bar being set ever higher for charities and their trustees in terms of what is expected of them, trustee recruitment (and indeed retention) may become an issue. Consequently, long serving trustees could well become increasingly valuable to the stability and effectiveness of the trustee board.

Two Codes: one for larger and one for smaller charities

The draft Code used a colour scheme to indicate which specific aspects of the Code would apply in particular to charities with staff (highlighted in blue) and larger, more complex charities (highlighted in pink). However, this distinction did not find its way into the finalised Code. Instead, two Codes have been produced: one for larger charities with a typical annual income over £1m which takes it over the audit threshold and one for smaller charities whose income is below the audit threshold.

The two versions only differ slightly in relation to some of the recommended practice. It is not immediately apparent at a glance what the differences are but, in general, larger charities are expected to publish more information in their annual report and/or elsewhere (ie their website) in relation to, for example, the charity's approach to risk; how trustees' performance is evaluated; and the process of setting remuneration of senior staff.

What the final Code does not contain

In its response to the consultation, the Charity Commission noted that the draft did not appear to cover a charity's relationship with trading subsidiaries or members of any group structure – this is not covered in the final Code.

In our view, it would have been helpful if there was at least a brief reference to the Code of Fundraising Practice but there is no such reference in the final Code.

In its response to the consultation, the Charity Law Association recommended that the Code is produced in a "tick-box" format which would make it easier for trustees to record their charity's engagement with the Code's governance principles. However, this suggestion was not carried over to the final version.

Lack of clarity regarding what trustees MUST do and what they SHOULD do

The draft Code highlighted in a small section at the end of each principle the relevant underlying legal and regulatory context. During the consultation process it was suggested, by the Charity Commission amongst others, that there was scope in the Code for greater clarity and cross referencing to trustees' legal duties and responsibilities. However, despite this, rather surprisingly the sections highlighting the legal and regulatory context have been removed altogether from the final Code.

The introduction to the final Code provides that:

“The Code is not a legal or regulatory requirement. It draws upon, but is fundamentally different to, the Charity Commission’s guidance. Instead, the Code sets the principles and recommended practice for good governance and is deliberately aspirational.”

This is confusing as there are some aspects in the “Recommended Practice” sections under the various principles that are legal requirements rather recommended best practice. For example:-

- principle 2 (leadership) – includes the recommended practice that the trustee board takes collective responsibility for its decisions: however, it is a matter of law (not best practice) that trustees are ultimately and collectively responsible for the control and management of the administration of their charity;
- principle 3 (integrity) – includes the recommended practice that:-
 - o trustees maintain the charity’s reputation and deal appropriately with conflicts of interest and loyalty: however, trustees have a legal duty to act in the best interests of their charity and this duty is relevant in these two scenarios; and
 - o the board ensures that the charity follows the law: however, compliance with the law is not a best practice issue!

In our view, the lack of distinction/clarity in the final Code between what charities MUST do as a matter of law and what they SHOULD do as a matter of best practice, could lead to trustees failing to comply with their legal duties and responsibilities. We will be reviewing the Code in detail with a view to producing greater clarity and practical guidance in this regard. We will also analyse where the Code overlaps with the Charity Commission’s core guidance CC3.

The Charity Commission’s stance

When the draft Code was published the Charity Commission acknowledged that it would not “own” the Code, but confirmed that it would endorse and promote it as a standard of good governance practice to which all charities and their trustees should aspire. This is echoed in the Commission’s blog relating to the final Code:

“The bottom line is, good governance is no longer an optional extra...The Charity Governance Code represents a standard of good governance practice to which all charities should aspire. We encourage all charities to read, follow and apply it proportionate to their circumstances. And if you sign up to the code, go public about it on your website or your annual report.”

However, the above blog did not provide any further clarification, as requested during the consultation process, as to the possible consequences if charities do not apply the Code (so far as is relevant). It is presumed, therefore, that the Commission’s stance as indicated in its response to the draft Code remains unchanged:

“We will consider further how we can take account of charities’ consideration and application of the Code in our regulatory interactions with them and in the requirements and expectations for reporting.”

It is hoped that greater clarity will emerge on this issue in due course but until such time, it appears, as observed in our briefing note on the draft Code, the reality may well be that *“Charities and their trustees will ignore the Code at their peril.”*

What next?

As mentioned above, we will be producing more detailed guidance on the Code but, in the meantime, we recommend that charities and their trustees note the following:-

1. identify which Code is relevant to their charity – ie is your charity a larger or smaller charity?
2. read the relevant Code and note which elements are or might be relevant to their charity;
3. prepare an action plan: prioritise accordingly;
4. *“apply or explain”*: the Code encourages charities to meet the principles and outcomes of the Code by either *applying* the recommended practice or *explaining* what they have done instead or why they have not applied it. Carefully minute decisions made in this regard;
5. charities that adopt the Code are encouraged in the Code to publish a brief statement in their annual report explaining their use of the Code;
6. consider whether it would be appropriate to establish a governance committee to deal with the above; and
7. take expert advice as considered necessary/appropriate.

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This note provides a general summary only and it does not constitute legal advice. It is recommended that specific advice is sought in relation to the particular facts of a given situation.

If you have any queries regarding any aspect of this note or you would like us to assist you with a governance review and/or assist with the preparation of any relevant documentation please do not hesitate to contact Sarah Chiappini.