

How does the Charity Commission's guidance relate to legacies?

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CHARITIES AND LITIGATION – HOW DOES THE CHARITY COMMISSION'S GUIDANCE RELATE TO SUCCESSION AND TRUST DISPUTES?

INTRODUCTION

Over the summer the Charity Commission released new guidance, [Charities and litigation: a guide for trustees](#).

The guidance is accompanied by (i) a [checklist of key actions for trustees](#) when considering or faced with litigation and (ii) a [Legal underpinning](#) aimed largely at professional advisors which sets out the Charity Commission's view of the law 'underpinning' the guidance.

The Charity Commission identifies two reasons for being interested in charities and litigation:

The Charity Commission (or the court) must authorise litigation known as '*charity proceedings*'.

Litigation (whether the charity is bringing or defending the proceedings) '*can present significant risks*' for charities.

'Charity proceedings' concern the internal administration of a charity, such as the removal of a trustee. It is the second reason that is relevant in the legacy context.

The Charity Commission is also concerned to protect the reputation of charities. The legacy context has given rise to (usually ill informed) criticism of charities for pursuing certain court cases.

CHARITY TRUSTEES AND THE DECISION TO LITIGATE – EXISTING GUIDANCE

All charities have the power to take or defend legal action – this is done in the name of the charity for charitable companies, Royal Charter bodies and CIOs, or in the name of the charity trustees for unincorporated associations and trusts.

Charity trustees must balance conflicting duties – the duty to safeguard charity assets may mean that charity trustees should take legal action to recover assets (including legacies), or that they should not take legal action, for example because of the costs relative to the amount at stake involved.

Charity trustees must ensure that any decision to initiate or defend legal proceedings are taken in accordance with their legal duties. See the Charity Commission's updated (July 2015) guidance, [The essential trustee: new guidance on trustees' responsibility](#).

The Charity Commission's [It's your decision: charity trustees and decision making](#) provides helpful guidance. In summary, trustees should be properly informed, have considered all reasonable options, seek professional advice where needed and have managed any conflicts of interest or loyalty.

On occasion, the Charity Commission is robust in the stance it takes over recovery of charity assets. In particular see [The Charity Commission's policy on restitution and the recovery of charitable funds misappropriated or lost to charity in breach of trust](#).

The Charity Commission's new guidance '*...explains what charity trustees need to know when thinking about taking or defending legal action generally...*'

It sets out general principles which should guide trustees including:

- trustees have a duty to protect or secure charity assets and, where necessary, to recover assets belonging to the charity – legal action may allow the trustees to do this.
- a decision to take or defend legal action must be made exclusively in the best interests of the charity and charity trustees should be able to explain and justify that decision.
- unless the charity has appropriate in-house expertise, charity trustees will usually need to take appropriate professional legal advice.
- trustees should consider alternative dispute resolution methods, such as mediation, and whether this would be an appropriate way of resolving the dispute.

'Trustees have a general duty to act in the best interests of their charity. They have a duty to protect, and where necessary, to recover, assets belonging to the charity. The decision whether or not to initiate or defend a legal action must only be made in the best interests of the charity and be balanced against the risks and consequences that any legal action could bring.'

In the original draft, the trustee's duty to protect charity assets did not appear prominently. The Charity Law Association Working Party which reviewed that draft submitted:

'We consider that this duty should take more prominence in the guidance – it is because of this duty that charity trustees may be considering litigation. A full and proper consideration of the duty to protect the charity's assets is central to any decision about whether to commence or defend proceedings. We appreciate that there is a balance to be struck in reaching such decisions between avoiding the cost and risk of litigation and pursuing or defending litigation to secure charity assets.'

'At present, the draft guidance is weighted heavily in favour of avoiding litigation at any cost. We consider that there needs to be recognition that there are likely to be cases where the only way of achieving a favourable outcome by settlement or otherwise is by showing serious intent... A rebalancing of the advice relating to the duty to protect charity assets would enable trustees to make proper and informed decisions about all aspects of their duty.'

Costs

In exceptional circumstances, charity trustees may be personally liable for any costs associated with litigation. The Charity Commission uses '*some circumstances*':

'in some circumstances, the trustees may be liable for pay any legal costs personally, for example if:

- *the court considers that the costs have not been properly and reasonably incurred*
- *trustees are not able to demonstrate that they have considered all the relevant principles in making their decision'*

The guidance could be clearer that if costs have been properly and reasonably incurred, ie the charity trustees act in accordance with their legal duties, have made any decisions properly and after consideration of all the relevant issues, charity trustees are not going to be personally liable.

Although note the trustees of a charity without limited liability, such as a trust or unincorporated association, are personally liable for all liabilities of the charity irrespective of the merits of their actions. This is subject to the trustees' right to indemnify themselves out of trust assets for liabilities properly incurred.

ALTERNATIVE DISPUTE RESOLUTION

'If trustees find themselves faced with taking or defending legal action, the commission will expect them to have thoroughly explored and, if appropriate, ruled out all other reasonable ways of resolving the issue beforehand.'

The Charity Commission's guidance places a strong emphasis on seeking a resolution to a dispute outside of court. Whilst this reflects the courts' approach, and in many cases requirement, that alternative dispute resolution is explored before or whilst litigation proceeds, the guidance perhaps misses the necessary nuances. Alternative dispute resolution is not appropriate in all cases and requires the cooperation of both parties – if the other side refuses to engage in alternative dispute resolution, the charity trustees have not failed in any way. There is recognition that

'unless time constraints for bringing or responding to an action prevent it, the commission will expect trustees to explore and, if appropriate, rule out all other reasonable options open to them to resolve the issue, such as alternative dispute resolution or agreeing a legal compromise'

The original draft version of the guidance placed such a strong emphasis on charities avoiding litigation and settling disputes. The Charity Law Association working party was concerned that opposing parties could use the guidance to force charities to concede or settle unfavourably. In its submission the working party stated:

'We agree that litigation should be avoided. But the tone of the guidance appears to suggest that litigation should be avoided at all costs; this may, perhaps, reflect media comment following some recent high profile charity legacy disputes. Whilst the Working Party (and we suspect the sector as a whole) fully endorses guidance that reflects the seriousness of litigation for charities, we are concerned that the tone does not fully reflect the

different types of litigation in which a charity may be involved and that charity trustees have an overarching duty to protect charity assets. We also consider that the stress on alternative dispute resolution and compromise is too emphatic. Generally, the overall tone of the guidance could put additional pressure on charity trustees...

Take, for example, a case in which an employee brings a claim against the charity for constructive dismissal. Picking up this guidance, the overall impression that trustees are likely to form is that charities should avoid litigation at all costs. Accordingly, the charity may be put in a weaker position...in that the charity trustees may feel pressurised into compromising a claim immediately, rather than waiting to see whether [that] party has a meritorious argument against the charity.'

Following comments from the working party, the emphasis on the overriding importance of compromise was significantly amended and the revised guidance takes a more balanced approach.

The working party also made the point that:

'... there is a distinction between charity proceedings and proceedings with third parties. It is an established principle that charity funds should not be frittered away on internal disputes. The emphatic judicial statements referred to in the guidance occurred primarily in the context of charity proceedings. In relation to third parties, it is for the trustees to exercise their discretion (acting in the best interests of the charity) to decide whether the charity should pursue or defend litigation. This important principle is entirely obscured in the current draft.'

We are still concerned that the tone of the guidance does not fully reflect the different types of litigation in which a charity may be involved and the fundamental difference between litigation a charity voluntarily commences and litigation which is thrust upon them.

Confusingly, the Commission appears to regard 'negotiation', 'mediation' and 'legal compromise' as different forms of dispute resolution. However, it is helpful in making clear that alternative dispute resolution does not mean running up the white flag:

'Trustees should take care to ensure they secure as favourable a settlement as reasonably possible in the interests of the charity, taking account of all relevant factors.'

REPUTATION

The reference in the guidance to reputation is in the context of compromise:

'Considerations may include how entering into the compromise could affect the charity's reputation and whether the course of action could affect the charity's position in other disputes.'

Unfortunately the Legal Underpinning perpetuates the lack of clarity by citing judicial dismay in an inter charity dispute.

'Legal proceedings involve a greater or lesser degree of risk and the consequences of losing a case can be very expensive, not only financially, but also in terms of damaged reputation and disappointed donors. These consequences may arise even if the charity concerned wins the case.'

'Prospective donors may share the dismay expressed by Robert Walker J, in British Diabetic Association v Diabetic Society Ltd [1995] 4 All ER 812 at 816, who described a passing off action between charities as:

"a deplorable, even scandalous thing to occur. Charities solicit donations from the public (and for a charity such as the association fund-raising is quite big business, as its accounts show) in the expectation that donations will be spent on furtherance of the charity's purposes."

Regrettably the Commission did not appear to take on board the Working Party comment that:

'[Robert Walker J's] outrage was at two similar charities litigating against each other, rather than the defence of charity interests in general.'

In RSPCA v Sharpe, Neuberger LJ did not criticise the RSPCA for pursuing the litigation. In fact, he was critical of the judge at first instance who had criticised the RSPCA.'

Reputation management is a relevant factor. But, to take an easy example, concerns that a disappointed relative might write to the Daily Mail would not excuse failure to take steps to secure the charity's entitlement to an estate.

PRACTICAL POINTS

The Commission makes clear it:

'expects trustees to be able to show that they have applied the principles of this guidance where their charity is involved in legal action'

Whilst the new guidance is called 'a guide for trustees', it is important to management, in house legal teams and legacy teams as it provides a useful aid for anyone involved in a charity considering or faced with litigation.

The Charity Law Association Working Party urged the Commission to take on board the reality of pressures on decision making:

'We consider that some trustees when reading the current draft (especially those without any legal background) are likely to be too concerned and too cautious about bringing / defending litigation. This makes it difficult for those advising them, because at the time when clear thinking and a quick but informed decision is needed, it may slow the process down and actually result in more costs being incurred. We fear that there may be a division of opinion of trustees leading to inertia rather than a clear decision...

...In some circumstances, charity trustees will not have the time to consider the extensive factors set out in [the guidance], for example due to strict limitation periods or court deadlines. Third parties bringing or threatening claims against trustees, make take advantage of the time taken by trustees to reach decisions if it suits their needs.'

Lawyers will be cheered by the following:

'unless a charity has the necessary in house expertise, in order to make a proper decision it will usually be appropriate to take and consider professional legal advice, as well as whatever other specialist advice they might need to inform their decision.'

The requirement for necessary in house expertise will not be satisfied by a charity trustee who happens to be a solicitor and / or general counsel. They will need to have an appropriate degree of expertise in the litigation involved. The value that trustee or general counsel brings will be in the assessment of what is appropriate for the charity to do informed by the specialist advice.

Caution should be exercised about the following however:

'transparency about the reasons for taking legal action is very important in explaining why the trustees decided on this course of action – the trustees must be able to justify their decision because the charity's actions may have an impact on the charity's reputation and supporters.'

Care needs to be taken because any proper cost/ benefit assessment will assess risks – and thus be a document that must not fall into the wrong hands

Similarly, to the extent that decisions to litigate are debated at trustee level or elsewhere within the charity and are properly informed they should not take place in a forum to which supporters and other members of the public have access.

CONCLUSION

There is a risk that the documents may be used selectively to criticise charities for bringing or defending claims. But there is emphasis on the obligation to protect assets:


'The trustees' duty to protect and secure the charity's assets applies equally in compromising a claim as it does in taking or defending legal action.'


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