

# CollinsBensonGoldhill Legal Briefing

## CHARITABLE COMPANIES CHANGES UNDER THE COMPANIES ACT 2006



BE PROACTIVE

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Since the full incorporation of the Companies Act 2006 on 1 October 2009, there are a number of changes which will affect the charitable companies limited by guarantee.

BE PROACTIVE

<b>Articles of Association</b>	<ul style="list-style-type: none"> <li>• Ask CBG review your articles so we can tell you where you can benefit from company law changes</li> <li>• For existing charitable companies, ensure that the current charitable objects are relevant for your circumstances</li> </ul>
<b>Directors</b>	<ul style="list-style-type: none"> <li>• Ensure that your company has at least one natural (i.e. not corporate) director prior to 1 October 2010.</li> <li>• Ensure that all of the directors of the company are fully briefed on the new codified duties to ensure that they do not fall foul of the law</li> <li>• Ask CBG to complete forms if directors wish to remove their residential addresses from the public records at Companies House</li> </ul>
<b>Written Resolutions</b>	<ul style="list-style-type: none"> <li>• Take advantage of the new company law legislation governing written resolutions.</li> <li>• Make sure you include the necessary information on your written resolutions to ensure that they are validly passed within in the given timeframe.</li> </ul>

#### CONSTITUTION

Charitable companies are governed by the twin legislation of company law and charity law. While a general commercial company will have wide commercial objects and a charitable company must

have objects which are considered charitable under the law of England and Wales. As a charitable company's objects will be much more restrictive than the objects for a commercial company, the charity's directors have a duty to act within the charitable objects of his/her company and will be considered to be in breach of this duty and potentially personally liable if he/she acts outside the scope of these objects.

### Memorandum and Articles for a Charitable Company

As with all private limited companies, a charitable company incorporated under the 2006 Act will simply be required to state in its memorandum who the subscribers will be and that they agree to become members of that company (section 8, 2006 Act). The company's articles of association will now become the key constitutional document and will contain the provisions formerly seen in the memorandum (such as the objects, trustees' powers, provisions regarding a trustee benefits and the winding up of the company).

Please note that existing charitable companies will not be required to change their memorandum and articles of association to conform to the new model because as of the 1 October 2009 those provisions which should now be contained in the articles will be treated as if they were so (section 28 2006 Act).

### Model Articles

Any charitable company limited by guarantee that is incorporated under 2006 Act, on or after the 1 October 2009, may adopt some or all of the provisions of the model articles for private companies limited by guarantee under the 2006 Act. If such a company is incorporated without adopting any particular articles then the model articles will be construed as their own. Therefore for any new charitable company should specifically exclude the model articles as they are not suitable (for example – they allow directors to be remunerated as a matter of course and they do not provide as to how the company's assets will be dealt with on dissolution) and would not be acceptable to the Charities Commission. Please note that the Charities Commission provide standard memorandum and articles of association.

### Amending your Memorandum and Articles

A charitable company governed by the 1985 Act may decide that it would be beneficial to change its constitution, where, for example, it can no longer pursue its original aims effectively or the administrative provisions in the articles need to be modified to enable trustees to act with greater efficiency – which various provisions of the 2006 Act can assist with.

The Charities Act 2006 changes certain provisions of the Charities Act 1993 in relation to the amendment of a charitable company's memorandum and articles.

Under the 1993 Act, the Charity Commission's prior written consent is required to change:

- a charitable company's objects as set out in its memorandum
- any other provision of its memorandum, or any provision of its articles, which directs or restricts the manner in which company's property may be used or applied

The Charities Act 2006 amends the law so that the Charity Commissions prior written consent is only required for regulated alterations (unless the articles of association say that the Charity Commissions consent is required for all proposed changes). These regulated alterations are as follows :

- any alteration of the objects clause in the memorandum
- any alteration of any provision of the memorandum or articles directing the application of property on the company's dissolution
- any alteration of the memorandum where alterations would provide authorisation for any benefit to be obtained by the company's directors or members or persons connected with them.

There is an apparent discrepancy between Section 28 of the Companies Act 2006 and Section 31 of the Charities Act 2006. Section 31 of the Charities Act provides that any amendments to the memorandum (with the exception of amendments to the charitable objects) will only require the Charity Commission's consent if they relate to the way in which property is applied on a company's dissolution. It is not clear, however, how the reference to the objects clause being in the memorandum shall be interpreted now the 2006 Act provisions regarding the memorandum and articles have come into force – bearing in mind that a charitable company's objects will now be considered to form part of its articles. This would appear to preclude section 31 of the Charities Act 2006 from applying to such companies as the objects will no longer be treated as being in the memorandum. Guidance from the Charity Commission expressly states that any changes to the statement of the objects of the charity needs to get their prior written approval (regardless of whether these are contained in the articles of association or the memorandum).

In any event alterations generally require a special resolution in order to come into effect. In practice this means obtaining members' consent at a general meeting. Where any change to the articles of association are approved, a signed copy of the resolution and the amended articles must be sent to the Charity Commission and Companies House within 15 days of it being made.

With the exception of a change to the statement of objects an amendment to a charitable company's articles will take effect from the date the special resolution is passed (provided Charity Commission's written approval is obtained). Changes to statement of objects only comes into effect once they are registered at Companies House – and a charitable company can only start acting under these new objects after that date.

#### MEETINGS AND RESOLUTIONS

The 2006 Act will have the following impact on meetings and resolutions.

##### Meetings

Under 2006 Act, private companies (which include charitable companies) no longer need to hold an annual general meeting (AGM), unless the articles so require.

In many charitable companies because the members are the same individuals as the directors the removal of the requirements to hold an AGM may be seen as helpful. However, some charitable companies may have a wider membership body distinct from their directors. Where this is the case,

then the AGM may be a useful governance tool and it would be prudent to retain the requirement to hold an annual general meeting.

Under 1985 Act ten percent (10%) of the voting members were required to consent if members wish to require the directors to call a general meeting. Under the 2006 Act if more than 12 months have passed since the last time the members required the directors to call a general meeting; the required percentage is five percent (5%) (Section 303 of the 2006 Act). The 2006 Act also contains a new power for the members to call a meeting at the company's expense when the directors fail to do so, with the cost to be recouped from the company (Section 305 of the 2006 Act).

These provisions are only likely to be useful to charitable companies in the situations where:

- the articles do not contain a requirement to hold an AGM
- considerable time has passed since the charitable company's last general meeting
- the directors refuse to call a general meeting

Under the 2006 Act, private companies (including charitable companies) are not required to lay accounts before their members in the general meeting. However, all companies including charitable companies are still required to circulate their accounts to members.

### Resolution

Under 2006 Act a charitable company may now pass any resolution using the written resolution procedure with the exception of a resolution to remove a director or an order served before the expiration of his period of office.

The rules have changed on the way in which written resolutions can be passed. Previously the 1985 Act provided that written resolutions had to be signed by all members and would only be passed if there was unanimity. Now, written resolutions can be passed as either special resolutions (with a majority of at least 75%) or as ordinary resolutions (with a simple majority) as the situation requires.

The written resolution may either be proposed by directors or by at least 5% of the voting members. Written resolutions must be circulated to all members of who are eligible to vote. A proposed written resolution will lapse if it is not passed before the end of this period specified for its purpose in the articles; or if the articles do not specify, the period of 28 days beginning with the date on which the resolution was circulated. A failure to return a signed resolution by the lapse counts as a vote against the resolution.

Charitable companies with a large membership may wish to consider amending their articles to extend the 28 day period to allow members extra time to respond.

## MEMBERS

Charitable companies will need to be aware of the following changes:

### Inspection of the Register of Members

Under the 1985 Act it was possible for any member to inspect the register without charge or for any other person to inspect the register on payment of a fee.

To stop vexatious request for copies of the register and to avoid members being contacted for an improper purpose, access to the register of members will be subject to a “proper purpose” test under 2006 Act. This means that a request to inspect or receive a copy of the register of members must include:

- information about the purpose for which the information will be used
- details of person to who the information will be disclosed and the purposes for which any such person will use the information

The company must then comply with the request within five working days or apply to the Court. If the Court is satisfied that the inspection of the register of members is not being requested for a proper purpose, it must direct the company not to comply with the request and may order the person who made the request to pay the company’s costs in whole or in part.

At this stage there is no precise definition of what a “proper purpose” would be however, should you require advice on this point then it would be worth contacting your solicitor for any news on advancement in case law.

## DIRECTORS

Charity trustees are the persons having the general control and management of the administration of a charitable company. Therefore the charitable company’s charity trustees are its directors.

### Identity of Directors

The 2006 Act has introduced a new requirement for companies to have at least one director who is a natural person. This requirement came into force on 1 October 2008 although there is a grace period until October 2010 for any company which did not have at least one director who is a natural person on 8 November 2006. Therefore in future a company cannot be the sole director of a charitable company and a charitable company cannot be the sole director of its trading subsidiary.

With the effect from 1 October 2009, all directors may provide a service address on the company’s register of directors, rather than giving their residential address. Directors are still required to give Companies House their residential address but it will be kept on a separate secure register that will not be available to the general public.

When applying to register a charity with the Charities Commission, trustees are required to provide a residential address but residential addresses are not displayed on the charity’s entry on the

register of charities held by the Charity Commission. Therefore it is now possible for directors of charitable companies to keep their residential addresses confidential.

### Director's Duties

Directors of charitable companies have duties both as charity trustees (under charities legislation and also common law fiduciary duties) and as company directors. Please see the schedule attached to this article which sets out the full codified duties of directors which has been introduced by the Companies Act 2006.

A summary of these codified duties and their ramifications for charitable company directors are as follows:

**A duty to act within the powers of the company.** As above, this means that the directors must act in accordance with the company's constitution (and objects). For a charitable company this means that power can only be exercised in furtherance of the charities charitable objects.

**A duty to promote the success of the company.** For a director of a charitable company it would be inconsistent for him to act for the benefit of the members. So, accordingly, all references to promoting a successful charitable company will refer to the achievement of its charitable purposes rather than the benefit of the members.

The financial years beginning on or after 1 October 2007 all charitable companies "except small charitable companies" must include a business review in the director's report in accordance with the 2006 Act. The financial years beginning before 6 April 2008, a small company is, broadly, a company which satisfies two of the following conditions in a given financial year:

- A turnover of not more than £5.6m;
- A balance sheet total of not more than £2.8m; and
- No more than 50 employees.

A turnover and balance sheet thresholds are increased to £6.5m and £3.26m respectively the financial years beginning on or after 6 April 2008.

Under the 2006 Act the business review is given a statutory purpose which is to inform the members and assist them in assessing how the directors have fulfilled their duty to promote the success of the company. This business review must contain a fair review of the company's business and a description of the principal risks and uncertainties facing the company. In practical terms, for charitable companies the business review will contain the same information as that contained in the annual report which charities are required to submit to the Charities Commission but the requirement to identify risk and uncertainties is new and directors will need to consider this.

**A duty to exercise independent judgment.** In the context of charitable companies established by commercial entities as part of a corporate social responsibility programme, there may be an overlap between the directors of the charitable company and the directors of the commercial entity. Those directors serving on both the board of the commercial entity and the charity will need to be

especially careful that the decisions taken in relation to the charity are genuinely independent and are not influenced by their involvement in the commercial company.

**A duty to exercise reasonable care, skill and diligence.** This is essentially a codification of the existing common law position. A professional person who is a director of a charity will therefore be subject to a higher duty of care than non-professionals. The directors may take legal or other professional advice to enable them to discharge their duty of care.

**A duty to avoid conflict of interests.** A director must avoid a situation in which he has, or can have, a direct or indirect interest which conflicts or may conflict with the company's interests. There are specific provisions relating to charitable companies:

- the duty does not apply to a conflict of interest arising in relation to a transaction or arrangement with a charitable company if or to the extent the articles allow that duty to be disapplied.
- the directors of a charitable company may only authorise a conflict of interest arising in relation to a transaction or arrangement if the charity's constitution allows this.

These additional provisions are put in place to be consistent with existing charity law.

There is a new power in the Charities Act 2006 which will allow a charity to remunerate a charity trustee for the provision of goods or services to the charity and this may apply to a charity if amongst other things there is no express restriction on the remuneration of its directors. Please note that the memorandum usually does contain such an express restriction and removal of this would require the Charity Commission's prior consent.

**A duty not to accept benefits from third parties.** Charitable companies should consider keeping a register of benefits and hospitality received to ensure transparency in the charity's governance.

**A duty to declare an interest in a proposed transaction or arrangement.** Unlike with non-charitable companies, a charitable company may not authorise a transaction or arrangement which is likely to constitute a breach of the duty to avoid conflicts of interest unless the articles specifically allow those duties to be disapplied. Please note that it is unlikely that a charitable company's articles would allow the members to authorise such a conflict.

#### Transaction with Directors

As of 1 October 2007 the following transactions between a charitable company and a director require members' approval:

- A director's service contract in more than two years in duration (previously five years under the 1985 Act);
- A transaction between a company and director or a connected person in relation to a non cash asset which either exceeds £100,000 in value or exceeds 10% of the company's asset value and is more than £5,000 (previously £2,000 under the 1985 Act); and
- Loans of more than £10,000 made by a company to a director (under previous law loans to directors were prohibited apart from certain loans for less than £5,000).

Any members' approval of a transaction between a charitable company and a director is ineffective without the Charity Commission's prior written consent.

Please note that the requirement for members' approval under 2006 Act also extends the transactions between a company and persons connected to the director. The category of persons falling within the definition of a member of a director's family has been increased so it now covers:

- (a) the director's spouse or civil partner;
- (b) any other person with whom the director lives as partner in an enduring family relationship, as long as that person is not the director's relative;
- (c) the director's children or step-children;
- (d) children or step-children of a person with whom the director lives as partner in an enduring family relationship, as long as they live with the director and not obtain the age of 18; and
- (e) the director's parents.

#### Director's Service Contract

A director of a charitable company may not be remunerated unless this is authorised by the memorandum or by the Charity Commission or the court. If remuneration is authorised the company must give a copy of every director's service contract available for inspection by the members without charge.

#### Company Name

With effect from 1 January 2007, a company must mention its name on all order forms and on its websites as well as on letters, notices, receipts, invoices and other such documents. The company must also on websites business letters and order forms details of its place of registration, registered number, registered office and if the company is exempt from using the word "limited" in its name the fact that it is a limited company. Penalty for non compliance is a fine.

#### Company Secretary

With effect from 6 April 2008, a private company may, but need not have a secretary. To preserve governance in charitable companies it may be preferable not to dispense with the office of company secretary in such companies unless another person has been identified to fulfil the role.

If you have any questions regarding this article or would like to know more about a specific area regarding charitable companies, then please feel free to contact a member of our Business Services Team:

**DAVID MORRISON**

Email: [dm@cbqlaw.co.uk](mailto:dm@cbqlaw.co.uk)

**ED HARRIS HUGHES**

Email: [ehh@cbqlaw.co.uk](mailto:ehh@cbqlaw.co.uk)

Switchboard: 0207 436 5151

**COMPANIES ACT 2006 – DIRECTORS DUTIES****171 Duty to act within powers**

A director of a company must—

- (a) act in accordance with the company's constitution, and
- (b) only exercise powers for the purposes for which they are conferred.

**172 Duty to promote the success of the company**

(1) A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to—

- (a) the likely consequences of any decision in the long term,
- (b) the interests of the company's employees,
- (c) the need to foster the company's business relationships with suppliers, customers and others,
- (d) the impact of the company's operations on the community and the environment,
- (e) the desirability of the company maintaining a reputation for high standards of business conduct, and
- (f) the need to act fairly as between members of the company.

(2) Where or to the extent that the purposes of the company consist of or include purposes other than the benefit of its members, subsection (1) has effect as if the reference to promoting the success of the company for the benefit of its members were to achieving those purposes.

(3) The duty imposed by this section has effect subject to any enactment or rule of law requiring directors, in certain circumstances, to consider or act in the interests of creditors of the company.

**173 Duty to exercise independent judgment**

(1) A director of a company must exercise independent judgment.

(2) This duty is not infringed by his acting—

- (a) in accordance with an agreement duly entered into by the company that restricts the future exercise of discretion by its directors, or
- (b) in a way authorised by the company's constitution.

**174 Duty to exercise reasonable care, skill and diligence**

(1) A director of a company must exercise reasonable care, skill and diligence.

(2) This means the care, skill and diligence that would be exercised by a reasonably diligent person with—

- (a) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the functions carried out by the director in relation to the company, and
- (b) the general knowledge, skill and experience that the director has.

**175 Duty to avoid conflicts of interest**

(1) A director of a company must avoid a situation in which he has, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company.

(2) This applies in particular to the exploitation of any property, information or opportunity (and it is immaterial whether the company could take advantage of the property, information or opportunity).

(3) This duty does not apply to a conflict of interest arising in relation to a transaction or arrangement with the company.

(4) This duty is not infringed—

- (a) if the situation cannot reasonably be regarded as likely to give rise to a conflict of interest; or
- (b) if the matter has been authorised by the directors.

(5) Authorisation may be given by the directors—

- (a) where the company is a private company and nothing in the company's constitution invalidates such authorisation, by the matter being proposed to and authorised by the directors; or

(b) where the company is a public company and its constitution includes provision enabling the directors to authorise the matter, by the matter being proposed to and authorised by them in accordance with the constitution.

(6) The authorisation is effective only if—

- (a) any requirement as to the quorum at the meeting at which the matter is considered is met without counting the director in question or any other interested director, and
- (b) the matter was agreed to without their voting or would have been agreed to if their votes had not been counted.

(7) Any reference in this section to a conflict of interest includes a conflict of interest and duty and a conflict of duties.

**176 Duty not to accept benefits from third parties**

(1) A director of a company must not accept a benefit from a third party conferred by reason of—

- (a) his being a director, or
- (b) his doing (or not doing) anything as director.

(2) A "third party" means a person other than the company, an associated body corporate or a person acting on behalf of the company or an associated body corporate.

(3) Benefits received by a director from a person by whom his services (as a director or otherwise) are provided to the company are not regarded as conferred by a third party.

(4) This duty is not infringed if the acceptance of the benefit cannot reasonably be regarded as likely to give rise to a conflict of interest.

(5) Any reference in this section to a conflict of interest includes a conflict of interest and duty and a conflict of duties.

**177 Duty to declare interest in proposed transaction or arrangement**

(1) If a director of a company is in any way, directly or indirectly, interested in a proposed transaction or arrangement with the company, he must declare the nature and extent of that interest to the other directors.

(2) The declaration may (but need not) be made—

- (a) at a meeting of the directors, or
- (b) by notice to the directors in accordance with—
  - (i) section 184 (notice in writing), or
  - (ii) section 185 (general notice).

(3) If a declaration of interest under this section proves to be, or becomes, inaccurate or incomplete, a further declaration must be made.

(4) Any declaration required by this section must be made before the company enters into the transaction or arrangement.

(5) This section does not require a declaration of an interest of which the director is not aware or where the director is not aware of the transaction or arrangement in question.

For this purpose a director is treated as being aware of matters of which he ought reasonably to be aware.

(6) A director need not declare an interest—

- (a) if it cannot reasonably be regarded as likely to give rise to a conflict of interest;
- (b) if, or to the extent that, the other directors are already aware of it (and for this purpose the other directors are treated as aware of anything of which they ought reasonably to be aware); or
- (c) if, or to the extent that, it concerns terms of his service contract that have been or are to be considered—

- (i) by a meeting of the directors, or
- (ii) by a committee of the directors appointed for the purpose under the company's constitution