

The Spirit of Charity

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1. Introductory

- 1.1. It is, of course, an immense privilege for anyone to stand before an audience such as this to deliver a professorial lecture. As someone who is passionate about the work of charitable organisations, I am delighted that the University has seen fit to designate a *Chair in Charity Studies*, and I am honoured to be speaking today on that basis. Professors specialising in this sector are still a rarity, though I follow in the footsteps of several colleagues at other universities with titles such as “Professor of Voluntary Sector Management”. But I make no great claims for my work, except as a student of charities, hoping to persuade you that this is an important and worthwhile area for academic research and teaching.

2. The Third Sector

- 2.1. I’ve called this lecture *The Spirit of Charity* because my aim is to offer a broad assessment of the state of charity and the charity sector in the UK at the present time. In particular, I want to ask whether the underlying spirit behind what is formally classified as “charity” is alive and well as we approach the end of this first decade of the 21st century. In doing so I will mention some research where I have been personally involved – but much of what I am saying is drawing heavily on the work of others.
- 2.2. Before talking about charities specifically, I want to start with the “third sector” more generally – in particular, I want to try to define some terminology. Nevertheless, I realise that others have written extensively on these definitions¹, so I hope you will excuse my over-simplifications.
- 2.3. Charities are, of course organisations – it is not normally possible to have a charity which comprises a single person². Charities exist first and foremost because people have come together with some sense of common cause and are willing to accept some common rules in order to advance that cause. But first, let’s think about organisations more generally – and traditionally in this field we divide the world of organisations into three sectors:

¹ E.g. Kendall (2003); Reichardt et al (2008).

² It is, of course, possible to have a charity with a single member, but that member will need to appoint a number of people to act as trustees: in England and Wales the Charity Commission will not normally register a new charity with fewer than three individual trustees. Alternatively a charity can sometimes have a single corporate body as the sole trustee, but even so, a number of people will normally share in the governance of that corporate body. There are a few cases where a Corporation Sole (i.e. a corporate body consisting of a single person) is recognised in law as a charity – for example, an incumbent of an Anglican parish, in respect of a consecrated building – but even so, the building is established for the benefit of the wider public: without this it would not be charitable.

- First, are those organisations established primarily to generate private profit – what is often called the “commercial sector”³. This sector ranges from the largest publicly-listed companies to the smallest owner-managed businesses. I stress that when I refer to “profit” I do not imply that this is in any way wrong – on the contrary, over the centuries very substantial amounts of charitable funds have arisen from the philanthropy of those who have created wealth in business. Nor do I suggest that profit is the sole motive – many commercial organisations have excellent standards of social responsibility. I acknowledge, too, that many in this sector are far from wealthy – indeed, self-employed people struggling to make ends meet may well be candidates for charitable help.
 - But, as early human communities grew, the need for systems of law emerged, establishing common forces to defend the community – and gradually other services too – with systems of taxation to support them. This required organisations of governments and public service provision – the “public sector” as we call it today. Public sector organisations cannot make a private profit – any surplus is retained for ongoing public purposes – so we normally describe them as “not-for-profit” organisations. But such not-for-profit organisations which are part of the state are very different from third sector bodies.
 - So my definition of the “third sector” is very simple – I simply say that it comprises all organisations which are established on the dual basis of being non-profit-distributing, and which are not part of the state. Third sector organisations are essentially private organisations in that there is nothing to compel people support them or to take part in their activities.
- 2.4. Of course, this leaves plenty of borderline cases where we could argue where an organisation fits – universities are themselves a classic grey area, in that they are charities with their own boards of governors, yet subject to a great deal of state control (for example, in their degree-awarding powers)⁴. On balance, I believe universities are part of the third sector, given that they can appeal for charitable gifts in the same way as other charities and given that tertiary education is not (as yet!) imposed on everyone – but I know others disagree.
- 2.5. However, if you want a more inclusive definition of the third sector, I am fairly content with the key sentence in the Government’s own definition: *Organisations in the third sector share the common characteristics of being non-governmental organisations which are value-driven and which principally reinvest their surpluses to further social, environmental or cultural objectives.*⁵
- 2.6. In a moment I will look at the distinction within the third sector between charitable and non-charitable organisations, but first I want briefly to say something about *social enterprise*, which plays an increasingly important role in the third sector. I have seen occasional references to the third sector as comprising “charities and social enterprises” as though these are two distinct forms of organisation – and this overlooks the many third sector organisations which do not fit either of these categories. Social enterprise is *not* in my view a type of organisation – it is a type of *activity*, where a trading venture is undertaken primarily with a social aim: such as running a community bus, or providing employment for people with special needs. Social enterprise activities can be undertaken by organisations in *any* of the three sectors.
- Some social enterprises have shareholders or other investors who take a share of the profits – so even though the organisation’s main aim is social rather than profit-making. So, on the three sector model I would class them as being part of the first

³ This is seen as the “first sector” as it was arguably the first form of organisation when early humans developed systems of farming and started to trade with one another.

⁴ Some people would also raise the fact that most universities still receive substantial amounts of funding from the state – but many small charities are funded mainly by public sector grants and contracts, so I do not see this as a barrier.

⁵ Cabinet Office (2007).

sector. Social enterprises in this category for me include those Community Interest Companies (CIC) which allow a return to shareholders⁶ – and, personally, I would also include subsidiary companies owned by charities to undertake non-charitable trading⁷.

- Secondly, some activities undertaken by the public sector where fees and charges account for most of the income – for example a local authority-run sports centre – would also, in my view, count as a form of social enterprise.
- Then there are the many third sector organisations running social enterprises. This includes those organisations structured specifically as not-for-profit social enterprises, using structures like the CIC but with a provision that all profits must be retained for the future development of the work. However, it also includes many trading activities undertaken directly by charities themselves (as opposed to by subsidiary companies). Occasionally one hears comments like: “We started as a charity but nowadays we are more of a social enterprise” – but this is missing the point. It’s not an either/or. A social enterprise activity run directly by a charity within the framework of charity law is *still a charity* – but it is *very different* from a non-charitable social enterprise possibly governed by paid directors, and perhaps paying a significant return to investors.

2.7. So, I am not planning to say anything more today specifically on the term “social enterprise” – but as I talk further about “charities” please remember that I am consciously including many social enterprise activities undertaken by organisations with charitable status.

2.8. So, within the third sector, I now want to focus on what makes an organisation a charity.

3. The Origins of ‘Charity’

3.1. The English term “charity” derives from the Latin word “caritas”⁸ which was used by St Jerome, in the Vulgate (the Latin Bible) to translate the Greek word “αγαπη” (which nowadays is more usually translated as “love”). In fact, of the four Greek words used for love, αγαπη is the most profound: it refers the absolute willingness to give everything for the sake of another. St Paul, in a letter to the church at Corinth⁹ – after talking about all the ephemeral aspects of life which fall away – famously wrote “These three remain: faith, hope and love. But the greatest of these is love”¹⁰. However, for centuries, many people were more familiar with the Authorised Version¹¹, which, through the influence of the Vulgate¹², translated Paul’s words “πίστις, ελπίς, αγαπη” as “faith, hope, and charity”. That was the basis on which the word “charity” found its way into the English legal system.¹³

3.2. So “charity” has been seen from the earliest days of Christianity as one of the central tenets of the Christian faith. It encompasses a central obligation to put others first – even, where that means significant self-sacrifice – but it certainly wasn’t a new idea. Many of the Old Testament prophets had spoken of the need to abandon unjust ways and put others first –

⁶ The new legal structure of the *Community Interest Company* (CIC) is specifically designed for social enterprises. CICs were established by the Companies (Audit, Investigations and Community Enterprise) Act 2004 and the first CICs were registered from July 2005. Although the *majority* of any profit made by a CIC must be retained in the organisation, the Act permits CICs to be established where up to 35% of their profits could be distributed.

⁷ Although these are *owned* by charities, and normally transfer all their profits back to the charity, they are legally separate entities, established to make a profit. So (although this is not a popular view) I believe we must therefore regard charities’ trading subsidiary companies as part of the first sector – the commercial sector. Charity trustees who fail to observe the proper distinctions between a charity and its non-charitable subsidiary can easily find themselves subject to a Charity Commission inquiry.

⁸ Collins English Dictionary, 2nd edn 1986.

⁹ Written around the year 54AD – dating by Barclay, J in Barton & Muddiman (eds) (2000, p1109).

¹⁰ Bible - 1 Corinthians 13:13 (NIV translation).

¹¹ Also known as the King James Version (1611), though much of the content drew on the Tyndale translation (1526).

¹² The traditional translation of the Bible into Latin,

¹³ Although the text I have quoted is the most famous use, the word “charity” is actually used some 26 times in the AV translation of the New Testament – Young, Robert (undated, 19C) *Analytical Concordance to the Holy Bible* (7th edn revised by Stevenson, WB).

for example, Micah¹⁴, famously answered the question “What does the Lord require of you?” in the simple answer: “To act justly and to love mercy and to walk humbly with your God”¹⁵. Even before that, the law of Moses had one particular command “You shall love your neighbour as yourself”¹⁶ was subsequently seen as summing up the entire law in terms of human behaviour. The love of one’s neighbour is the basis of nearly all activity which has been traditionally described as charity.

- 3.3. But there is a difference between “charity” as a mode of human behaviour, and “charity” in an organised sense under which people act together for charitable purposes. In many case this requires a system of financial giving – and responsible people (trustees as we now call them) who will administer this giving and ensure it is spent on the relevant purposes. On this basis acts of charity can take place even when the donor and beneficiary are thousands of miles apart, or may not even be alive at the same time.
- 3.4. The law of Moses prescribed a formal system of tithes, under which the people of Israel were commanded to set aside 10% of all their produce to be given as an “offering to the Lord”¹⁷ – for use (at least in part) for the support of the poor and needy – this is arguably one of the earliest formal systems of charitable giving. Many Christians and Jewish people continue to follow this principle that 10% of one’s income is given to charity. The concept of Zakat, under which Muslims set aside 2.5% of their wealth each year for needy causes¹⁸, stands in the same moral tradition. However, clearly many people give to charity for reasons completely unconnected to religion¹⁹. Charitable giving is an important theme for research and I will say a bit more about it in due course.
- 3.5. In England, the principle of “charity” was thus firmly embedded from the middle of the first millennium AD, as Christianity took hold. But it was some time before we needed a system of charity law. As the leading charity law academic, Peter Luxton, comments, “No legal machinery is needed to enable a donor to put alms into the hands of a beggar or for a Good Samaritan to come to the aid of an injured traveller.”²⁰ “Charity” in that sense, does not require any organisational system.
- 3.6. However, once someone wishes to extend their charitable giving beyond direct help to a specific individual into helping a wider group of people²¹, not all of whom may be known to the donor, the trustees of such gifts are under more than just a moral obligation to carry out the donor’s wishes. Indeed charitable gifts often arise from legacies when, by definition, the donor has no direct control on their use. So we need a mechanism to be confident that charitable gifts will be used for the purposes intended²².
- 3.7. This is not a recent problem. One of the earliest disputes around a charitable gift is reported the Venerable Bede from around the year 650. King Oswin had given Bishop Aidan a top quality horse to assist him on his missionary travels around the North of England spreading the Christian faith²³. But soon, Aidan meets a beggar asking for alms, and Aidan has no cash so he gives the beggar this A-grade royal horse with all its accessories! King Oswin gets to hear about it and is not pleased – “If you wanted to give horses to the poor,” he says, “we have plenty of ordinary horses which would be good enough”. In terms of charity law, as it developed 1000 years later, Aidan was effectively the trustee of a horse given for the

¹⁴ Dating by Williamson, H G M in Barton & Muddiman (eds) (2000, p595).

¹⁵ Bible – Micah 6:8 (NIV translation). Dated around 700BC.

¹⁶ Bible – Leviticus 19.18 (NRSV translation). Although the book of Leviticus only reached its final form around the middle of the first millennium BC, it is widely accepted by scholars that key precepts such as this are much earlier in origin – e.g. Grabbe,

L L in Barton & Muddiman (eds) (2000, p91). Hebrew text: אֱתֵת לְעֵרְכֶךָ.

¹⁷ E.g. Numbers ch 18.

¹⁸ Islamic Relief (2008). The zakat obligation does not arise until someone’s disposable wealth as held for at least a year reaches the value of 3oz of gold (approx £1000). There are also other charitable obligations in Islam, in addition to zakat.

¹⁹ See, for example, Todd & Lawson (1999); Sargeant et al (2004).

²⁰ Luxton (2001, p3) – quotation abbreviated..

²¹ Luxton (2001, p4).

²² See, for example, Bucheit & Parsons (2006)

²³ Bede (731, Book III Ch 14).

charitable purpose of *the advancement of religion* but he redirected it for the charitable purpose of *the relief of poverty*. Although both purposes are charitable, he had committed a breach of trust. Fortunately, King Oswin thought things over: he told Aidan, that he would not enquire how Aidan used any future gifts from the King's bounty. In other words, Oswin declared that Aidan could treat any further charitable gifts from him as *unrestricted donations* – to use the modern language of the Charities SORP²⁴.

- 3.8. Of course, over the years, various more elaborate systems of charity were established under Church auspices²⁵ and more generally as the law of trust developed. Many charitable trusts were established long before the State established a system of charity law – in fact the oldest active charity on the Charity Commission register was established in the year 597!
- 3.9. But gradually it became clear that trust law alone was not sufficient to protect charitable gifts as it required legal action by beneficiaries. And, as gifts came to be made for more secular purposes, it was no longer appropriate to see the Church as the protector of charity.
- 3.10. So, the regulation and definition of charities as institutions, effectively began from the famous Statute of Charitable Uses Act of 1601²⁶. The body of the Act has long been repealed, but the preamble to the 1601 Act has remained, interpreted by the Courts and Charity Commission²⁷ – right up to this week – in assessing what is and what is not to be regarded as charitable²⁸.
- 3.11. From the outset, one of the key planks of charity law has been the principle of voluntary trusteeship – that is, that those who are entrusted with charitable funds should apply them to advance the charity's objects without seeking personal benefit and charity trustees can only be paid in very exceptional circumstances. The Charities Act 2006 has slightly extended those circumstances²⁹, but the principle remains. It is estimated today that over a million people in the UK are charity trustees³⁰. I believe this willingness by such large numbers of people to take on considerable responsibility as trustees or board members of charities, with no payment other than reimbursement of expenses, is a very positive sign for the *spirit of charity*.
- 3.12. I do not have time today to trace the developments of charity law over the last four centuries, so I propose now to leap directly to the present day. But the timing of this lecture is particularly fortuitous, because this week we are marking a monumental change. As from two days ago, on 1 April 2008, a new definition of "charity" has come into effect, replacing the 400 year tradition from 1601.
- 3.13. To be a charity, an organisation has to meet two tests: charitable purposes and public benefit. Those tests remain³¹, but are now defined in completely new ways. The new charitable purposes are as shown here.

²⁴ *Accounting and Reporting by Charities: Statement of Recommended Practice* (Charity Commission 2005).

²⁵ Indeed during medieval times wealthy donors were encouraged to be generous to the Church in the hope of entering the kingdom of heaven (Luxton 2001, p6).

²⁶ Strictly speaking it began four years earlier with a 1597 Act which was re-enacted in 1601 (Luxton 2001, p6).

²⁷ Especially the important case of *Commissioners for the Special Purposes of the Income Tax v Pemsel* [1891] AC 531 – which led to the famous judgement of Lord Macnaghten defining the four heads of charity as currently understood (prior to the Charities Act 2006) i.e.: the relief of poverty, the advancement of education, the advancement of religion; and other purposes beneficial to the community (Luxton 2001, p112).

²⁸ Strictly speaking, the Charities Act 2006 does not actually remove the former criteria given that new head (m) in s2 (see box below) includes any purposes which were charitable under existing charity law prior to the 2006 Act.

²⁹ The provisions of the 2006 Act allowing fees to trustees for specific services (outside their normal duties as trustees) took effect from 18 March 2008. Four tests have to be met before such payments can be made.

³⁰ Charity Commission figures 2006.

³¹ Under sections 2 and 3 of the Charities Act 2006 – which took effect from 1 April 2008.

New Heads of Charity in section 2 of Charities Act 2006

(Slightly Paraphrased)

- (a) The prevention and relief of poverty**
- (b) The advancement of education**
- (c) The advancement of religion**
- (d) The advancement of health or the saving of lives**
- (e) The advancement of citizenship or community development** (including rural or urban regeneration, and the promotion of civic responsibility, volunteering, the voluntary sector or the effectiveness or efficiency of charities)
- (f) The advancement of arts, heritage, culture or science**
- (g) The advancement of amateur sport**
- (h) The advancement of human rights, conflict resolution or reconciliation or promotion of religious or racial harmony or equality or diversity**
- (i) The advancement of environmental protection or improvement**
- (j) The relief of those in need by reason of youth, age, ill-health, disability, financial hardship or other disadvantage**
- (k) The advancement of animal welfare**
- (l) The promotion of the efficiency of the armed forces of the Crown or the emergency services**
- (m) Any other purpose which may reasonably be regarded as analogous to above including existing charity law.**

- 3.14. This represents a big increase from four heads of charity previously, to thirteen now – in fact more than that if you include the sub-headings – but it doesn't necessarily represent a huge change, because most of the new heads have been accepted for some time by the Charity Commission under the original fourth head of "other purposes beneficial to the community". But I do believe that this new definition is important for the *spirit of charity*. The fact that a 400-year-old definition has been brought up to date with effect from 2008 is, I would argue, a sign that the concept of charity remains alive and important and relevant.
- 3.15. But many types of activity which have, until recently struggled to get charitable recognition are now included directly on the face of the Charities Act, and I believe this is incredibly important – particularly in areas such as sport³², environment, and community development.
- 3.16. However, this extension of the heads of charity is coupled with a tighter understanding of "public benefit". Until now, most charities³³ were presumed to operate for the benefit of the public unless proven otherwise. That has now changed³⁴ and *all* charities will now have to be explicit about how the public benefits from their work – in fact from this financial year (2008/09) charity annual reports will have to say how the charity's work has benefited the public³⁵.

³² In the past, sports organisation could usually only achieve charitable status if they could persuade the Charity Commission that their objects were essentially about health or education or provision of recreational facilities – but there were quite a few hurdles. The fact that "the advancement of amateur sport" is now directly listed as one of the new heads of charity means that, within the third sector as a whole, we may soon see a big increase in the number of sports organisations recognised as charities. An intermediate status of *Community Amateur Sports Club* (CASC) was introduced by the Finance Act 2002 s58 which allows certain sports organisations to access some of the tax benefits of charities. Currently 4685 organisations are currently registered as CASCs (HMRC 2008). But the full status of "amateur sport" as a charitable purpose under the 2006 Act offers much more than CASC status.

³³ Those established under the three main original heads – poverty, religion and education.

³⁴ Under s3 of the Charities Act 2006.

³⁵ Charities (Accounts and Reports) Regulations 2008 (SI 2008/629) Reg 40(2)(b).

- 3.17. This new requirement prompted the largest amount of Parliamentary debate on the Charities Bill (which is now the Charities Act 2006)³⁶. In the end, the public benefit requirement in the Act is worded in very vague terms and the Charity Commission has had to steer its way through a minefield in drafting the all-important guidance³⁷ which trustees must consider.
- 3.18. But personally, I believe the outcome of this is also good for the *spirit of charity*: I argue³⁸ that the new emphasis on public benefit will have a positive value in getting charity trustees discussing the ultimate beneficiaries of their work – rather than focusing on the means to the end.³⁹ So, I do not believe well run charities which focus on their objects have anything to fear from the public benefit requirement.⁴⁰
- 3.19. So, the key issue in all this, is that the definition of which organisations are and are not charities is determined by these two simple tests: an organisation is a charity if:
- it established for exclusively charitable purposes (within the 13 heads of charity); *and*
 - those purposes are carried out for the benefit of the public.
- 3.20. If those two tests are satisfied, then the organisation *is* a charity. If one (or both) of them is not satisfied, then it *is not* a charity. The Charities Act 2006 has made big changes to the detail of those two tests, but it has not changed the tests themselves. An organisation does not become a charity by being registered with the Charity Commission: the Commission's role in registering charities is simply to assess these tests and rule on whether or not an organisation meets them.⁴¹
- 3.21. I would also stress that charitable status does not mean a certain structure. People wanting to set up charities often think there is a standard package for this purpose, but in fact, many different types of organisations can be charities – trusts, associations, non-profit companies, and others, if they meet the twin tests of charitable objects and public benefit. Nevertheless, later this year we should see the implementation of a new legal structure under the Charities Act 2006 – the “Charitable Incorporated Organisation”. I believe the CIO form will bring many benefits⁴² – and the fact that Parliament has agreed to establish a complete new legal structure for charities is another sign that the *spirit of charity* is moving forward. But a new structure does not mean a change in the nature of charity itself: everything I say about charities includes organisations with a wide range of legal forms.

³⁶ At the one end, many MPs felt that the legislation was far too lax in not clamping down on organisations with charitable status where only a small part of the public would ever be able to benefit from the work due to the high fees charged: the targets here were charitable independent schools and fee-charging private hospitals. At the other end, many other groups, especially religious charities, seemed to think that changes in the law were out to get them – partly fuelled in my view by ill-informed religious journalism.

³⁷ Charity Commission (2008b).

³⁸ See Morgan (2007a and 2007b).

³⁹ To take the religious charities, for example, it is all too easy to focus on the maintenance of a church building when the formal object of the charity might be “the advancement of the Christian faith”. In such cases, the provision of a building for public worship is an important *means* by which public benefit is provided, but a building can never be a *beneficiary* – the beneficiaries are the public at large who have the opportunity to experience Christian worship, or to benefit from Christian service in the community. Even in the case of a heritage charity established to conserve a particular building, the public benefit requirement means trustees will need to consider how the that conservation work will benefit the public at large, rather than focusing purely on the building itself. Likewise, those professional bodies with charitable status will need to focus more on the wider public whose interests they seek to support, and will need to remember that the work they do with their own members is only a means to that wider aim.

⁴⁰ Some charities will need to work harder to ensure that people on a wide range of incomes can benefit from their work, but I do not think that is a bad thing. I think that in practice, the charities most likely to fail the public benefit test are not the independent schools, but those charities which have become completely inward looking, who offer no benefits except to their own members, and who have erected all sorts of barriers to newcomers who may wish to become members.

⁴¹ When a new charity is added to the register it does not mean that it has suddenly become a charity: just as passing an exam does not make students more knowledgeable – it is simply evidence that they meet a certain standard! Moreover, there are quite a few organisations which – at present – are recognised as charities without needing to be registered with the Commission: for example most universities and places of worship. (Some of these are *excepted charities* and some are *exempt charities*.) However, it should be noted that the Charities Act 2006, when fully in force, will substantially reduce both of these categories.) So, whilst being a registered charity is a very convenient of proving to the outside world that an organisation is indeed charitable, it is by no means the only evidence.

⁴² CIOs will be incorporated bodies with limited liability but they are *not* subject to company law – the regulatory framework is entirely within charity law. (In this respect they are completely different from CICs – see note 6 – which *are* a form of company and in any case CICs are *not* permitted to be charities.)

4. The Significance of Charitable Status

- 4.1. So I hope I have now managed to persuade you that charitable status is not a fuzzy concept. Any organisation either is or is not a charity: there is no half-way house.
- 4.2. This is extremely important as we seek to understand the different organisations which make up the third sector. The latest statistics published by NCVO estimate that there are in total around 865,000 third sector (or civil society) organisations in the UK⁴³. Within this the number of *registered charities* is known quite accurately – excluding charities which are subsidiaries of others, there were 169,299 main charities on the Charity Commission register at 31 December 2007⁴⁴. But as I mentioned, there are also many charities which are currently excepted or exempted from registration – no one knows the exact figure, but this could well account for a further 50,000 charities. So adding charities in Scotland and Northern Ireland, there are perhaps 240,000 charities in total, amounting to just over a quarter of organisations which make up the third sector.⁴⁵
- 4.3. So, how important is this? Charitable status receives a great deal of attention from lawyers, and a fair bit from accountants, and of course from studies of charitable giving – but many voluntary sector studies from fields such as social policy or even from my own discipline of management studies mention the charitable status of organisations at best as a footnote, and frequently not at all. It is almost as though people see charitable status as no more than an irrelevant fiscal or regulatory issue, with little bearing on the actual work of a voluntary organisation.
- 4.4. Now it is true that some charitable organisations place a big emphasis on their charitable status and some less so, but I want to argue that in every case it make some very fundamental differences.
- 4.5. The most obvious difference is, of course, that charities get various *benefits under the tax system*. It's a myth that charities don't pay tax – taxes like employer's national insurance and VAT on the majority of purchases are paid by charities in the same way as anyone else. In fact, whereas most businesses are VAT registered and can therefore reclaim VAT on their purchases, a charity funded by grants and donations is not a trading organisation, so it cannot register for VAT⁴⁶. But there are important tax concessions for charities: no income tax or capital gains tax to pay on investments, no VAT on press advertising, no inheritance tax when people leave legacies to charities, and the right to reclaim tax paid on individual donations under gift aid. Charities occupying premises for their charitable work pay no more than 20% of the normal level of business rates, and where charities charge for their services, no tax is paid on the profits provided they are reinvested in the long term work of the organisation⁴⁷. These factors make a very big difference for charities as compared to non-charitable social enterprises.
- 4.6. Then there is the *reputational benefit* of being a charity. Many people will *give* to charity in a way that they would be very reluctant to do with a non-charitable organisation. When we are asked to support an organisation which has a registered charity number (or some other evidence of charitable status) we have a sense of confidence that our contributions will go to a worthwhile cause and not (we expect) into the hands of the people running the organisation. This doesn't just apply to individuals – businesses wanting to work with third

⁴³ Reichardt et al (2008). It must be stressed that this figure is subject to a wide measure of uncertainty as there is no overall register of third sector organisations in the UK.

⁴⁴ Charity Commission (2008a).

⁴⁵ Author's estimates from a range of sources – including Scottish figures from the Office of the Scottish Charity Regulator (www.oscr.org.uk) discounted to allow for charities on the Scottish register which are also registered in England & Wales.

⁴⁶ Charities charging fees (i.e. those involved in trading) can often register for VAT, but are usually then subject to complex VAT partial exemption calculations, and in most cases only a small proportion of input VAT can be reclaimed (i.e. they still have high levels of irrecoverable VAT) – this is partly because many services provided by charities are classed as VAT exempt. See Morgan (2008b, chapter 11) for further discussion.

⁴⁷ This applies to "primary purpose trading" – i.e. trading where goods or services are supplied directly as part of the charity's objects (as opposed to trading for fundraising purposes). See Morgan (2008b, chapters 4 & 11).

sector organisations feel much safer in working with a charity – it is more likely to impress their customers – and there are tax reliefs for business gifts to charity.

- 4.7. Thirdly, and this has been the focus on my own research in recent years, there is nowadays a huge *regulatory benefit* from being a charity. The framework of charity law and the oversight of the Charity Commission rightly gives people a confidence that charities can be trusted. I will say more about this in a moment.
- 4.8. Until recently, charitable status in all these senses has been very much unique to this country, particularly with its emphasis on voluntary trusteeship, and therefore the term “charity” is less widely used in international third sector research⁴⁸. But times are changing, and the English system of charity regulation is starting to be copied elsewhere – not just in the rest of the UK but also overseas.⁴⁹

5. The Funding of Charitable Work

- 5.1. But I now want to look briefly at the funding of charities. Let’s start with the issue of direct gifts by individuals which – as I mentioned earlier – lies at the heart of charity.
- 5.2. In the last 15 years or so, charitable giving has become a very important area of research.⁵⁰ As a result of the work of researchers CAF and NCVO⁵¹, we know that, in an average month, 54% of adults will give something to charity – women are more likely to give than men. Of those who give, the mean monthly amount given is £29 (this comes from combining the figures for many different methods of giving). But this mean is somewhat skewed – nearly half of all charitable giving comes from around 7% of very generous donors, who represent under 4% of the total adult population.
- 5.3. My own work has touched on giving in a couple of small studies – in the late 1990s I did a survey of the top 500 fundraising charities and was surprised to find that only 15% of those with individual donors said they asked their donors to make any kind of sacrifices in other expenditure in order to support the charity – and those that did were mainly religious organisations⁵². Given that most charities are addressing really important issues, I find it surprising that many still ask for little more than people’s spare change⁵³.
- 5.4. I have also been involved in some technical work around tax-effective giving, especially regarding “new gift aid” when it came into effect in 2000⁵⁴ as means by which any charity can reclaim tax on donations from UK taxpayers.⁵⁵ But I find it surprising how many charities are

⁴⁸ Most countries have some kind of legal framework for non-profits, but until recently few have systems similar to ours with protection of charitable gifts by an independent charity commission. Many countries with common law legal systems recognise the concept of “charity” but sometimes its only significance is in terms of eligibility to tax concessions – see Cain (2007).

⁴⁹ Scotland now has its own charity regulator - the Office of the Scottish Charity Regulator (“OSCR”) established by the Charities and Trustee Investment (Scotland) Act 2005. Northern Ireland is soon to have its own Charity Commission under the Charities Bill (introduced 2007) currently under consideration in the Northern Ireland Assembly. In the Republic of Ireland, a Charities Bill 2007 is under consideration in the Dáil (Irish Parliament) which will establish a Charities Regulation Authority. However, such moves are not limited to Britain and Ireland: the Charity Commission has an international programme, it has been asked by a number of countries, including developing countries, to advise on setting up system of non-profit regulation drawing on the English charity model.

⁵⁰ I am delighted that the ESRC has recently launched a Centre for Charitable Giving and Philanthropy, led by colleagues I much respect – Professors Jenny Harrow and Cathy Pharoah at City University, London.

⁵¹ NCVO/CAF (2007).

⁵² Morgan (1996).

⁵³ Of course there are exceptions, such as major donor campaigns. But often these are focused on small numbers of individuals. It is rare for normal campaigns to ask donors to give to charity at costly levels.

⁵⁴ Gift aid began in 1990 as a means by which charities could reclaim a donor’s income tax on lump sum gifts, but initially this was limited to donations of at least £600. This limit was gradually reduced, and a “Millennium Gift Aid” scheme allowed small gifts to be accumulated for gift aid in relation to projects in the poorest countries – but it was only from 2000 that the gift aid regime allowed charities to reclaim tax on any relevant donation, with no lower limit, thus enabling the phasing out the former system of “deeds of covenant”. Donors must be UK taxpayers and must complete a “gift aid declaration” identifying themselves and confirming that they wish the relevant donation(s) to be treated a gift aid.

⁵⁵ Morgan (2000).

still reluctant to ask for direct gifts from individuals⁵⁶. However, I was expecting to have to use this lecture to comment on a reduction in the value of gift aid from next week as a result of the reduction in the basic rate of income tax. So I was very encouraged that in last month's Budget⁵⁷, the Chancellor agreed a transitional relief which, for three years, will continue to give gift aid tax refunds based on 22%, even though the basic rate of tax will have gone down to 20%. This is a very positive sign of recognition from the Government for the work of *charities as a whole* – rather than just those who have a direct role in delivering Government policies – another positive recognition for the *spirit of charity* at this time.

- 5.5. But individual giving is only one source of charity income – there are many others sources. It has long been the case that charities can charge fees in appropriate circumstances – for example an almshouse charity can charge rents to residents, and (long before state schools) there were charitable schools charging fees for education. But the level of such fees, and who can afford them is now central to the debate on whether or not such organisations meet the public benefit test⁵⁸. Charities are increasingly providing services on behalf of local authorities or the NHS, and some are thus receiving considerable levels of contract income – in fact the charitable income from public sector sources is now almost the same as the income from individuals⁵⁹. Then there are many charities – particularly grant-making foundations, whose income comes almost entirely from investments. For some charities, fundraising events bring in substantial income. A few charities are supported mainly by income from businesses. Nowadays on our MSc in Charity Resource Management, the fundraising modules explore many different forms of income generation for charities.
- 5.6. So today, a charitable appeal can take many forms:
- mailings and inserts seeking individual gifts
 - bids for public sector funding
 - the sale of goods through charity shops
 - even academic bids for research funds!
- 5.7. So, with all this diversity, it may be helpful to try to give a picture of the funding of an “average” charity – in the way that TV programmes love to do for things like an average bottle of wine. So – based on the figures for registered charities – I can tell you that an “average” charity⁶⁰ in 2007 would have an income of £263,000. And if this average charity has a totally average split of income from difference sources⁶¹ it would look something like this.

⁵⁶ The Institute of Fundraising runs a major government-supported tax-effective giving project to promote the use of gift aid, and the Treasury is keen to do more to help smaller charities make use of gift aid (HM Treasury 2008).

⁵⁷ Darling, Alistair *Budget Statement* (House of Common 12 March 2008).

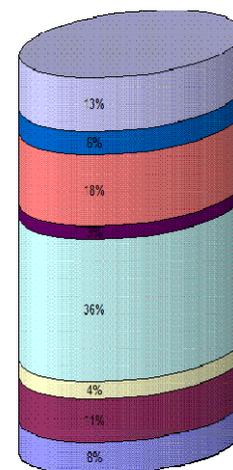
⁵⁸ Draft guidance has been published by the Charity Commission on this issue, in the context of the Charities Act 2006 (Charity Commission 2008b).

⁵⁹ Reichardt et al (2008).

⁶⁰ This is based on the *mean* across all registered charities in England & Wales, using Charity Commission (2008a) figures. The *median* income would be under £10,000 due to the large number of very small charities on the register.

⁶¹ Based on income data as reported by NCVO (Reichardt et al 2008).

INCOME OF AN "AVERAGE CHARITY" IN 2007		
Individual Donors	£35,000	13%
Legacies	£15,000	6%
Individual Fees	£47,000	18%
Trading Subsidiaries	£9,000	3%
Public Sector (incl Lottery Distributors)	£94,000	36%
Private Sector	£12,000	4%
Other Charities	£29,000	11%
Investment Income	£22,000	8%
Total	£263,000	100%



- 5.8. However, these figures are growing substantially from year to year, as more and more work is being done by charities: moreover, charities here in the Yorkshire and Humber region are now growing faster than any other UK region⁶². To me, the fact that charities are receiving substantial support from such a wide range of sources, and that much of this support is growing faster than inflation is another very positive sign for the *spirit of charity* today.

6. Critique of Charities

- 6.1. Now I accept that so far almost everything I have said about “charity” and “charities” has been positive. But I am certainly not suggesting charities should be immune from criticism. Research needs to include a proper debate on the effectiveness of charities and their contribution to society.
- 6.2. There has certainly been much critique of the concept of charity as a means of redressing wrongs in society – in particular, the Victorian notion of “charity” was often extremely patronising, with attempts to distinguish between the deserving and undeserving poor in deciding whom should receive charitable support. The founders of the welfare state successfully argued that those who are disadvantaged – for whatever reason – should receive support as a *matter of right*: not simply as an act of charity, at the discretion of individual philanthropist. In fact, at one time there was a belief that the need for charity would die out once the state was properly able to meet the needs of all its citizens.
- 6.3. Now I stress that the social construction of charity is well outside my specialisation, but I am happy to accept the criticism of “charity” in that patronising sense. In fact, many charities nowadays will refuse to accept funding which requires them to distinguish between beneficiaries on criteria which they feel are unjust. However, there are clearly many areas of activity, ranging from the preservation of historic railways to the advancement of religious belief, which the state may recognise as sufficiently worthwhile to justify according charitable status, but which the state would never wish to fund directly. So, whilst I accept that the place of charity in modern society is a really important debate, I have yet to hear anyone argue that there are *no organisations at all* which deserve charitable status.
- 6.4. The other big criticism is where things go wrong with individual charities. Because of the nature of charity, and the esteem which society accords to charitable organisations, we are shocked more than we would be in other sectors when we hear of a charity treasurer who stole money from the organisation he had offered to serve, or a fundraiser who has diverted

⁶² Reichardt et al (2008, p25).

gifts meant for her charity to her own personal benefit, or simply when we hear of charity trustees who run their organisations inefficiently.

- 6.5. The good news is that such scandals are – mercifully – very rare in the charity sector. But the key to ensuring that charities can be trusted with funds and trusted to put their beneficiaries first is, I believe, effective regulation. The regulation of charities – especially on accounting issues – is where the majority of my own work has been focussed in recent years, and that is the final area I want to speak about tonight.

7. The Regulation of Charities

- 7.1. Charity Commissioners have existed in various forms since the 1601 Act, and they first became a permanent body in 1853⁶³. But since 1960 when the registration of charities began⁶⁴, and especially since 1992⁶⁵ when the current accounting framework began, a quite sophisticated system of charity regulation has emerged.
- 7.2. Particularly for registered charities, the process of achieving registration in the first place, and then producing accounts in certain formats and making returns is actually, I believe, very helpful. Anyone can now go to the Charity Commission web site, look up any registered charity to check its objects and whether or not it is up to date with its returns, and for charities over £25,000 income you can directly print off their latest Annual Report and Accounts. Moreover, when the Charity Commission receives evidence of charitable funds being abused, it now has huge powers of intervention – which is another immense difference between charitable and non-charitable organisations.
- 7.3. I realise that some charities find this to be a regulatory *burden* rather than a benefit, but overall I believe the regulatory framework is one of the major benefits of charitable status. It requires trustees of charities to think and plan their work with a focus on their beneficiaries, and accountability for funds received, in a way which does not generally apply to non-charitable organisations in the third sector.
- 7.4. All charities, whatever their size⁶⁶, are required to produce Annual Accounts and, in most cases, an Annual Report – and these are *public documents*. Charitable status has many privileges, but it also brings responsibilities, including this requirement to publish an account of how funds have been used in the last year, and what the charity has done to advance its objects – including, from next year, a clear statement on what it has done for public benefit.
- 7.5. Fortunately, however, when the framework for charity accounting was being considered⁶⁷ prior to the Charities Act 1993, it was accepted that the law could not require a local playgroup run entirely by volunteers to produce the same sort of accounts as a national charity like Oxfam, so various thresholds were set based on the charity's income. The thresholds have been amended a couple of times: the key requirements are now as follows.

⁶³ Under the Charitable Trusts Act 1853 (Luxton 2001 p9).

⁶⁴ Charities Act 1960.

⁶⁵ Most of the regulatory requirements of the Charities Act 1992, including the charity accounting regime, were consolidated into the Charities Act 1993. The accounting requirements came into effect for years beginning 1 March 1996 onwards. The 1993 Act remains the central framework on charity reporting and accounting, though it has been amended several times, including by the Charities Act 2006.

⁶⁶ This requirement even extends to excepted charities (not registered with the Charity Commission), although compliance amongst excepted charities is variable (Morgan 1999).

⁶⁷ In the Woodfield Commission (Woodfield 1987) and subsequent Government proposals (Home Secretary 1989).

<i>Income of Charity</i> ⁶⁸	<i>Minimum Accounting Requirements</i> ⁶⁹
> £0	Must publish annual accounts (but they can be on a receipts and payments – R&P – basis)
> £5,000	Must apply to become a <i>registered charity</i> (unless excepted/exempted ⁷⁰)
> £10,000	Accounts must be independently scrutinised (by a <i>lay independent examiner</i>)
> £100,000	R&P accounts no longer permitted – accounts must be on accruals basis, and presentation must comply with the Statement of Recommended Practice on Accounting and Reporting by Charities (<i>Charities SORP</i>)⁷¹
> £250,000	Accounts must be independently examined by a professionally-qualified <i>independent examiner</i>
> £500,000	Accounts must be audited (by a firm of registered auditors)

- 7.6. When this regime first started to take effect, in 1996, there were howls of protest from some parts of the voluntary sector, with many claiming that charity treasurers would never be able to cope. But my own research⁷² has found that whilst the new regime certainly created new demands, it has for the most part been beneficial. In many cases, charity trustees were forced to think properly about the different funds of a charity, about the accountability to funders and donors, about proportions of expenditure spend on different functions, and about the charity's long term commitments and need for reserves. Subsequently it has led to charities becoming much more aware of the true costs of different parts of their work⁷³. In my view, this regime has thus led to a real improvement in the effectiveness of smaller charities in particular. Their willingness to take this on is, I believe, a further positive demonstration of the *spirit of charity*.
- 7.7. The Charity Commission and Office of the Third Sector have recently undertake a consultation about raising the various financial thresholds in this table⁷⁴, but my own submission has argued that, for the most part, the thresholds are working well. In fact, I have argued, based on research with users of charity accounts, that relaxing the rules could well have a detrimental effect on smaller charities seeking funding⁷⁵.
- 7.8. However, the aspect of the regime which I feel is most significant for the *spirit of charity*, is the scheme for *independent examination* of charity accounts – and much of my own work over the last decade – both in research and in professional practice – has been concerned with this⁷⁶. Before 1992 there was no general law requiring charities to have their accounts audited – it was entirely at the discretion of the charity trustees. Given the public expectation of charities, this was quite a serious position, and there had been some scandals. But in remedying this, it was accepted that it would be impossible to burden even the smallest

⁶⁸ Where a charity has more than £2.8M of assets, in some cases the requirements go further than those indicated by the table.

⁶⁹ The option of receipts and payments accounts does not apply to charities which are formed as companies. For more on these requirements, see Morgan (2008b).

⁷⁰ Currently this includes most places of worship, armed forces charities and a number of other special categories. However, most categories of excepted charity are being phased out under the Charities Act 2006, and exempt charities will only continue where another body can act as "main regulator" similar to the Charity Commission.

⁷¹ Charity Commission (2005).

⁷² Morgan (1999).

⁷³ Generally referred to in the sector as the principle of "Full Cost Recovery", following work, in particular, by ACEVO (2004).

⁷⁴ Charity Commission & Office of the Third Sector (2007).

⁷⁵ Morgan (2008a).

⁷⁶ Morgan (2002, 2003, 2004, 2005a, 2005b, 2005c & 2006) – plus various articles in professional periodicals.

charities with a full professional audit – the costs would be prohibitive⁷⁷. On the other hand, informal arrangements whereby the treasurer just got a friend to look over the books were clearly inadequate in most cases. So, in 1996⁷⁸ a three⁷⁹ level regime took effect:

- for charities up to £10,000 income no external scrutiny was needed
- from £10,000 to £250,000 income, the charity must at least have its accounts scrutinised by *independent examiner*
- above £250,000 income a professional audit was needed.

- 7.9. So a new kind of “charity person” was created – an *independent examiner* – who is defined in law as: *an independent person who is reasonably believed by the charity trustees to have the requisite ability and practical experience to carry out a competent examination of the accounts*.⁸⁰
- 7.10. An independent examiner does not have to be a qualified accountant, but must be someone genuinely independent of the charity who has sufficient understanding of charity accounting (in relation to the size of charity concerned) to make a proper report on the accounts. It could be an experienced treasurer of one charity acting for another charity – so long as they are serious about the responsibilities. Also, a number of independent examiners are people employed in the sector by *community accountancy services* – that is, charities which support other voluntary organisations on finance and accountancy⁸¹.
- 7.11. But independent examination is quite a thorough system. The duties are laid down in law: in a 12-stage programme of Directions from the Charity Commission⁸², and in Regulations⁸³ which specify seven separate opinions needed for an independent examiner’s report.
- 7.12. When I first saw the independent examination arrangements in the legislation (this was back in 1995, when consultations were taking place on the implementation of the 1993 Act) I thought this was a brilliant concept, but how will it work in practice? In particular, if people outside the ranks of professional accountants were to be encouraged to come forward to act as independent examiners, they would need support and training. Outside the University I ran some one-day courses on the subject, but longer term support was wanted. In particular, it seemed that some sort of professional qualification would be needed – accessible to independent examiners who didn’t have accountancy qualifications – so that charities could have some confidence in their skills. I circulated a discussion paper on the idea of an *Association of Charity Independent Examiners* which gained a good deal of support, and ACIE was formally launched in 1999. Nine years later, ACIE has around 600 members, a highly committed secretariat, and operates from offices here in South Yorkshire.⁸⁴
- 7.13. Moreover, when the Charities Bill proposed to increase the threshold for independent examination to £500,000 there was acceptance that a professional qualification was essential for those acting as independent examiners for these larger charities. Following debates in the House of Lords⁸⁵, which drew on some of my work, Fellowship of ACIE was accepted for this and was written into the Act⁸⁶. And, from this week, independent

⁷⁷ For the origins of independent examination, see Woodfield (1987), Home Secretary (1989) and Jones (2002).

⁷⁸ Charities Act 1993 s43 – as amended by the Deregulation and Contracting Out Act 1994, and by The Charities Act (Substitution of Sums) Order 1995 (SI 1995/2966).

⁷⁹ The £250,000 to £500,000 professionally-qualified independent examination band shown in the table was only created by the Charities Act 2006 and implemented for accounting years beginning from February 2007 – prior to this, audit was required for all charities over £250,000 income.

⁸⁰ Charities Act 1993 s43(3).

⁸¹ See Morgan et al (2007) for a study of Community Accountancy Services in England, including their needs for strategic support and development.

⁸² Charity Commission (2001). This was slightly updated in 2005 in publication CC63a (but without changing the essential Directions) – however updated Directions are expected later in 2008 to reflect changes as a result of the Charities Act 2006 and Companies Act 2006.

⁸³ The latest requirements are in the Charities (Accounts and Reports) Regulations 2008 (SI 2008/629).

⁸⁴ See www.acie.org.uk.

⁸⁵ See especially House of Lords Hansard 14 March 2005 col GC451.

⁸⁶ The provisions are now incorporated into s43(3A) of the Charities Act 1993 (as amended by the Charities Act 2006).

examination further extended to include charitable companies – again, research from here helped to provide the evidence.

- 7.14. The independent examination regime brings together a great deal of what I passionately believe is so important about charities. It allows people who are rooted in the voluntary sector – with experience of other charities – to share in the role of oversight of charity accounts (in fact, the former Chief Charity Commissioner described independent examiners as “invaluable allies” in the Commission's task of improving the transparency and accountability of charities⁸⁷). With small charities, the independent examiner often acts on a voluntary basis. Voluntary activity is, of course, at the heart of the voluntary sector – volunteers support the sector in all kinds of ways, especially as charity trustees. But when people voluntarily take on what amounts to a regulatory role, by acting as independent examiners to *other* charities, it is a sign that people care not just about the work of charities *but about the regulatory framework* – a framework which I have argued is fundamental to the nature of charity.

8. Conclusion: Is the *Spirit of Charity* still relevant today?

- 8.1. In the course of this lecture, I have tried to make a strong case for the importance of the concept of charity in understanding the third sector. Charitable status is *not* just a matter for lawyers or regulators. Charity accounting is not just a matter for accountants and treasurers: the way charities present accounts, and the way those accounts are scrutinised (often by volunteers) is fundamental to essence of charity. Charitable giving is not just an issue for those who study spending: the extent to which we do or don't give to charity says a great deal about our understanding of society – our willingness to accept the obligation to “love our neighbour” and accept some measure of self-sacrifice in doing so. Public sector support for charities is *not* just a matter of whether charities are best placed to deliver public services: the frameworks of regulation and of tax reliefs (which apply to charities much more than other third sector organisations) are about the state saying charities *as a whole* have a special place in society which needs protection and support.
- 8.2. So I hope I have persuaded you that this is an important area for academic research. And I make a plea to other third sector researchers – whatever discipline you come from – please don't overlook these *fundamental differences* between charitable and non-charitable organisations in the third sector: this distinction must, I believe, be imbedded in all our research.
- 8.3. Provided this is taken on board, I believe the *spirit of charity* is alive and well in the UK in the first decade of the 21st century. We have, just this week, seen the implementation of the biggest upheaval in the nature of charity for over 400 years. Almost all the recent changes in charity law and regulation – not just in the definition of charity, but also the accounting changes, the new standards in fundraising, the new CIO legal form, the bringing of excepted charities into registration with the Commission – all these changes and much else indicate that charities are valued and important. I think we will see a significant net increase in the numbers of charities in the coming years. Provided the Charity Commission is given the necessary resources to support charities through these changes, it is a good time, I believe to be involved with the charity sector, and a good time for researchers to look afresh at the *spirit of charity*.

⁸⁷ Stoker, John. *Address to the Annual Conference of the Association of Charity Independent Examiners* (London 18 May 2004, as quoted in *Independent Examiner* 6(2), pp1 & 5).

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