Charities and the Bribery Act
What do you need to know?

FEATURE
The billion-pound charity on the Isle of Man
The Albert Gubay Charitable Foundation

A lot of opportunities
Diversifying Investments

Karen Thompson joins as a partner from FARM-Africa
Welcome to the winter edition of Charity Matters newsletter

Welcome to the new-look Charity Matters! As you can see we have had a makeover – I hope you find it an even more engaging read as a result. We are now well into the new year, and the sector continues to show resilience and ingenuity in the face of a difficult time. One philanthropist with particular cause to be proud is Albert Gubay, who has at last seen the creation of the Albert Gubay Charitable Foundation on the Isle of Man. It will be interesting to see what other charities take advantage of the Island’s favourable climate.

Charities may believe they have little to fear from the introduction of the Bribery Act, but complacency is unwise, as our guest article from law firm Farrer & Co makes clear. In particular, overseas aid charities may need to review their policies and controls – but further guidance from the government is expected, so action should not be taken in haste.

I am delighted to introduce a new member of PKF’s Charities team. Karen Thompson joins us in our London office as an Assurance and Advisory partner. Karen has impressive charity credentials, having recently been the Chief Operating Officer & Director of Resources at FARM-Africa.

Finally, this is my final letter for Charity Matters, but I am delighted to hand over the next issue to Ian Mathieson, who will be assuming the role of Head of Charities. However, I will still very much remain part of the Charities team here at PKF.

To discuss any of this issue’s topics in more detail, please contact your usual PKF representative. If you have any comments or suggestions for future articles or any feedback on our new look, please get in touch.

Charles Cox
Partner, PKF (UK) LLP
RECENT PUBLICATIONS

Technical Edge
January 2011

Technical Edge is PKF’s bi-monthly newsletter aimed at keeping finance directors and company accountants up to date with financial reporting, tax and other technical developments. It takes a fresh look at how technical developments and proposals may affect your company, while maintaining our usual high quality technical coverage.

www.pkf.co.uk/technicaledge

Risk Survey
September 2010

The Risk Survey is produced annually in association with the Charity Finance Directors’ Group (CFDG) and is designed to help you overcome the obstacles to achieving your charity’s vision. The report highlights the areas of strength, common difficulties and issues that are emerging and looks forward at how the sector needs to develop.

www.pkf.co.uk/risksurvey

If you would like to receive a copy of either of these publications, or to be added to our mailing list, please contact:

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Charities and the Bribery Act – what do you need to know?

There has been much discussion, and already much controversy, surrounding the Bribery Act 2010, which was due to come into force in April of this year. The Act revises anti-bribery legislation in the UK for the first time since 1916, and brings UK law into line with the OECD Bribery Convention.

In response to some of the criticism of the Act, a government review has recently been announced, which (as a minimum) may lead to some delay in its implementation. Charities may wish to wait for the outcome of this review before considering what steps to take, if any. Nevertheless, every organisation with a UK presence needs to be aware of what is proposed.

Offences under the Act

The Act replaces the existing law with four offences. Under the Act it is an offence to bribe (“active bribery”) or to be bribed (“passive bribery”). A third offence is the bribing of a foreign public official. Bribery is widely defined and includes trying to get a person in a position of trust to do something they should not do.

The fourth offence applies only to commercial organisations (the definition of this term is not completely clear but may catch corporate charities that carry on a business). If a commercial organisation fails to prevent bribery by employees, agents and any subsidiaries (or anyone else performing a service on the organisation’s behalf) it is an offence unless the organisation can show it has in place “adequate measures” to prevent bribery.

Guidance is expected shortly on what may constitute “adequate measures”, which will focus on broad principles rather than serving as a manual describing the steps an organisation should take. The guidance is likely to centre on the principles in the draft guidance, which include carrying out risk assessments, due diligence and having in place accessible and monitored anti-bribery policies.

Areas of concern for charities

Concerns for charities have centred on the potential compliance burden and, more specifically, on the application of the Act to international aid charities and whether the Act will impact on corporate hospitality within the sector (limited as this may be).

Overseas aid charities may be left in the position where it may prove difficult to avoid committing what is technically an offence under the Act in certain situations, but where it is unlikely that any prosecution would ever be brought.

Questions have also been asked about whether corporate hospitality either offered or received by a charity and its employees would be covered by the Act. The draft guidance clarifies that there is no intention for reasonable corporate hospitality to constitute an offence under the Act (although this is not obvious from a literal reading of the Act), and the typical types of corporate hospitality in the sector – such as an occasional dinner with a key supplier or partner – are likely to fall into this ‘reasonable’ category. The draft guidance notes that the mischief the Act is designed to catch is lavish corporate hospitality, where the hospitality offered is seeking to improperly influence a person in a position of trust.

The Act applies to the worldwide activities of UK organisations. This has caused understandable concerns for aid charities working in jurisdictions where making “facilitation payments” can at times be hard to avoid. It is hoped the final guidance will make the position clearer and provide reassurance to overseas charities.

Unfortunately, overseas aid charities may be left in the position where it may prove difficult to avoid committing what is technically an offence under the Act in certain situations, but where it is unlikely that any prosecution would ever be brought.
Once the guidance is available, charities should review it carefully against any existing anti-bribery policies.

What should charities do?

There may be little benefit in taking action ahead of the outcome of the government review of the Act and the publication of the final guidance. However, once the guidance is available, charities should review it carefully against any existing anti-bribery policies they may have in place (including guidelines on receiving or offering corporate hospitality). At this point it may also be advisable to undertake a review of standard form employment contracts and commercial contracts, to ensure that these include anti-bribery provisions.

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The philanthropist Albert Gubay has publicly thanked the government of the Isle of Man, where he lives, for its help in creating The Albert Gubay Charitable Foundation. Already well known for his commitments to charity, Gubay now looks set to realise a long-held dream, in part thanks to the Island’s distinctive regime.
Albert Gubay has long made it clear that he intended to use a large proportion of his fortune for charitable purposes. Having made provision for his family, Gubay has spent recent years organisations his affairs so that, on his death, the companies he has built up can be left intact to the charity he has set up with the help of John Nugent, Director at PKF (IOM) LLC. The companies in question could already be worth over £800 million, but he is determined that the end result will be a £1 billion charity. His aim is to create an organisation capable of generating an annual income for good causes of at least £20 million.

Gubay has already placed the bulk of his wealth into trust, thus commencing the process that he hopes will lead to the fulfilment of his charitable ambitions. In the meantime, he continues to work tirelessly on behalf of the trustees to grow the fund that will end up in the charity.

The private charity regime

Gubay maintains that it is the Isle of Man’s new private charity regime that has allowed him the freedom to base the Foundation in the Isle of Man. Even before this regime was put in place, the Island was already an attractive location for the establishment of charities, being well regulated and also retaining a traditional definition of charitable causes. It also has straightforward and wide ranging tax exemptions (including underlying companies), good professional and financial infrastructure, and licensed organisations that are used to managing large complex financial arrangements. However, as in other jurisdictions, the degree of regulation attached to charitable status can be a perceived disadvantage for privately funded philanthropic arrangements.

Alongside his decision to establish his charity in the Isle of Man, Gubay was determined to protect potential beneficiaries, and so wanted the charity properly regulated. However, certain aspects of existing charity regulation did not seem appropriate for such a privately funded arrangement.

The situation improved when the Isle of Man government introduced the Charities (Exemption) Regulations 2008. This new regime requires the approval of the charity and ensures that the legitimate concerns of regulators and potential beneficiaries are met, but without, for example, the public filing of accounts or potentially onerous investigations into investments.

The new Isle of Man regime is specifically designed for charitable arrangements funded by wealthy individuals

1. The initial funds must originate from named persons who must be clearly identified to the Isle of Man Attorney General.
2. The name of the institution must be approved by the Attorney General.
3. The governing instrument must be approved by the Attorney General and in broad terms must incorporate the following elements:
   a) No further funds can be solicited or received from any person other than the original donor, and certain persons connected with the donor.
   b) The majority of the trustees or directors must be resident in the Isle of Man, and all meetings of the trustees or directors must take place in the Isle of Man.
   c) A trustee or director who is regulated under the Corporate and Trust Service Provider licensing regime must be appointed to accept service of notices and other documents.
   d) The Attorney General must be notified of certain trustee appointments.
   e) Each year audited accounts must be sent to the Attorney General, together with a certificate confirming compliance with the provisions of the governing instrument.
   f) Certain amendments require the prior approval of the Attorney General.

The new Isle of Man regime is specifically designed for charitable arrangements funded by wealthy individuals, which will not collect further funds from the public. It will be particularly attractive to individuals who do not need relief from estate taxation in respect of the funds passing to the charity. This may be where the estate of the individual, or the trust that will fund the charity, are in any case outside the scope of estate taxation.

Albert Gubay’s charity was the first to be approved under the new regulations, but it seems likely that others will be keen to follow in its footsteps, and that the regime will attract other privately funded charities to the Isle of Man.

For further information contact

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Diversifying investments is generally a good strategy, but smaller charities may not be in a position to take advantage of it on their own. Collective investment is one possible solution getting together with other charities through managed schemes. Charity Matters looks at the opportunities and consider the risks.
CIFs were first permitted under schemes established in the Charities Act 1960, operating as investment vehicles with charitable tax status. They give smaller charities the opportunity to invest collectively to benefit from diversification, and to access a wider range of investment opportunities. Currently there are 47 CIFs managed by 22 fund managers, managing in excess of £8 billion worth of charity assets.

Tax efficient investments

In the UK, organisations classed by HMRC as recognised charities can reclaim tax relief on income tax or corporation tax and capital gains tax where proceeds are used for charitable purposes only. Recognised charities can reclaim income tax deducted at source and may be entitled to certain VAT reliefs, although charities still need to complete tax returns for non-exempt income or gains. Since April 1999, 10% dividend tax credits cannot be reclaimed.

Furthermore, charities do not pay stamp duty when buying shares or convertible securities (currently 0.5%), nor do they pay stamp duty land tax (SDLT) when purchasing a property or a lease (SDLT is currently 4% over £500,000 and will be 5% over £1 m from April 2011).

Charities are also exempt from tax on income received from renting out land or property held for charitable purposes, as long as income is used for charitable purposes, but there is no exemption from tax on profits made from development of land or property.

CIFs thus clearly have tax-efficient benefits. They are not subject to stamp duty or SDLT, and because they distribute dividends gross, they avoid the administration of reclaiming UK tax. However, CIFs investing in overseas investments or equities will be subject to overseas withholding taxes.

In addition CIFs have other noteworthy benefits:

- CIFs have reduced monitoring obligations under Charity SORP requirements and are generally considered to offer cheaper administration for segregated portfolios.
- Broadly, annual management charges can be lower than for unit trusts although investors should confirm that these charges reflect all associated costs, as they can exclude trustee fees.

The current regulatory regime for CIFs allows for smoothing of income across financial years.

Risks and returns

CIFs undoubtedly offer a level of convenience, allowing for much greater diversification of investments, a wider range of opportunities, tax efficiencies and other notable benefits. However, it is important always for charities to review investment returns from a wider perspective.

The key for any charity is for its trustees to understand clearly the level of risk that the charity tolerates

CIFs are designed with charities in mind, but they are not always unbeatable in practice. Indeed, it may be possible to find higher growth investment funds which, even after allowance for tax leakage and possibly higher fees, can offer more attractive returns than some CIFs. That said, finding such a superior investment will also depend on the charity’s attitudes to risk and its income requirements, and rigorous qualitative diligence should always be undertaken before such investments are taken on.

The key for any charity is for its trustees to understand clearly the level of risk that the charity tolerates – its ‘risk appetite’. Many charities need income to meet fixed liabilities, and thus may seek investment in products with downside risk protection. Charities should carefully consider asset allocation to determine how best to meet their income and growth targets within their acceptable risk parameters. Only once a charity’s risk appetite is clearly understood can it consider the full range of appropriate collective investment opportunities. It may well be that non-CIF ranges offer higher net return opportunities than those available from the traditional established CIFs. Nevertheless, CIFs will undoubtedly continue to be favoured by many smaller charities looking for greater diversification in their investments.

Your company auditors, who may also act as your reporting accountants, should have a track record of auditing and advising listed companies, and understand the flotation process and the requirements thereafter. The company will also need a legal advisory firm that is very familiar with the listing legislation and is able to advise the company on all the legal aspects concerning its operations. Public relations advisers are also necessary in most cases. These can help build the profile of the business to attract potential investors. They can also assist in the general management of company news and announcements.

The future

The future of CIFs remains unclear. Respondents to a Treasury consultation in 2009 recognised that the Charity Commission may not have the appropriate expertise to regulate increasingly complex financial products. However, the consultation also raised concerns that the transfer of regulation to the FSA could produce an increase in fees.

It may also be that the possible emergence of new ‘Charity Authorised Investment Funds’, coupled with the proposed regulatory changes, will lead to a broader range of investment options. But this remains to be seen. Given the huge variety of charities and their different risk profiles and investment requirements, any increase in choice and diversity is to be welcomed. But whether a charity invests in CIFs or in another form of fund, is ultimately a matter for the trustees to resolve. Trustees are responsible for the investment decisions they make on behalf of their charity, and so should always first seek advice from their own professional advisers.

With thanks to

DELYTH RICHARDS
Head of Research – Funds, Kleinwort Benson
The Charity Commission has recently updated its investment guidance (last revised in 2003) to reflect current practices and investment policies. The draft guidance acknowledges that in today’s world, charities are investing to deliver not only a financial return but also to create a direct social benefit. This type of ‘social investment’ may allow a charity to consider ethical issues, and may well shape decisions about how an investment can help to further the direct aims of the charity.

The draft guidance makes clear that the trustees of a charity are ultimately responsible for determining the most appropriate investment strategy, but sets out their respective duties and responsibilities when making these decisions.

The Charity Commission has announced that it expects the required legislation allowing for the establishment of a charitable incorporated organisation (CIO) to be introduced in late spring 2011. In readiness for this, detailed guidance for trustees is to be developed which will explain how to set up a new CIO and how existing charities (either charitable companies or unincorporated charities) can convert to become a CIO.

The idea of a CIO is to allow a body to have the advantages of a company structure, but without the need to have the governance of two different kinds of legislation. Other advantages of a CIO include being regulated by (and registered with) only the Charity Commission and not Companies House, freedom from EC company law directives, a simpler constitution, and no penalties for a CIO based on the conduct of its directors.

Until the legislation has been passed it is not known whether there will be a phased implementation which may see the CIO provisions initially restricted to new CIO formations with the conversion aspects being introduced at a later stage.

If your charity may be interested in exploring the CIO model in greater detail, you can find more information about the advantages and other attributes of CIOs on the Charity Commission website.

It acknowledges that, for some trustees, seeking the best financial return will be their fundamental objective, whereas other trustees will be focused on trying to achieve a balance between obtaining a financial return and furthering the charity’s direct aims.

Before the guidance is finalised, the Charity Commission wishes to consult with the sector to ensure that the revised guidance provides trustees with sufficient information. The aim of such information is to assist trustees as they try to evaluate different investment approaches, and to provide answers to commonly asked questions relating to investing charitable funds.

The consultation document can be found on the Charity Commission’s website and is open until 28th February.
The year to make a difference

Helping you be more resilient, responsive and resourceful in 2011

In these increasingly challenging times, we consider it even more vital that we continue to add value in our services to the sector, and address the key concerns of our clients and contacts as effectively as we can.

With this in mind, we will be launching our seminar programme for 2011 over the next few weeks. In these we are looking to address the issues that are of most interest and relevance to your organisation now and hopefully the areas where you feel most in need of support and advice.

The seminars and round-table discussions will be hosted by our London office to begin with however we shall look at how these can be rolled out nationally as well.

More information on this will follow in the coming weeks.

Karen Thompson joins PKF from FARM-Africa

Karen trained and qualified with Deloitte in their London office, where she worked for 12 years in various roles in their corporate finance and audit departments. Her audit experience included managing the audits of FTSE 100 and 350 clients, SMEs, charities and arts clients. She has significant experience advising in owner managed buyouts, including AIM flotations and due diligence, and on financial modelling and business planning.

Having Karen on the team will be a great asset to PKF’s charity services, and we have no doubt that her experience will be of huge benefit to our clients too.

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PKF is delighted to welcome Karen Thompson to the London office as a specialist audit partner in the firm’s national charity team. Karen joins from the international development charity FARM-Africa where she held the posts of Chief Operating Officer and Director of Resources for 5 years.

As Chief Operating Officer, Karen headed up the Senior Management Team to ensure the strategic alignment of the charity’s global activities, and as Director of Resources she had global responsibility for all aspects of FARM Africa’s Finance, IT and HR functions.

Prior to joining FARM-Africa, Karen was Director of Finance and IT at the charity War on Want.

Please note that from this year, our Charity Risk Survey will be moving to an electronic-only format to help reduce our carbon footprint.

If you wish to continue receiving and taking part in the survey, please make sure we have your email address by either emailing risksurvey@uk.pkf.com or contacting your local PKF office.