

Restricted funds: Rationalisation and Registration

1. Purpose of this guidance¹

- 1.1 Cathedrals have been looking at aspects of their governance and considering what they can do before the draft Cathedrals Measure comes into force to improve their governance in anticipation of their application to register with the Charity Commission. One aspect of cathedral governance that cathedrals can review now is the restricted funds held by many cathedrals. This guidance seeks to help those cathedrals with restricted funds identify those which may be able to be rationalised and amalgamated and those which may need to be registered with the Charity Commission.
- 1.2 Many cathedrals have various funds of different sizes for specific purposes, of which the Chapter members are the trustees, often as a result of an historic gift or legacy. Some of these funds are already registered as separate charities with the Charity Commission. However, some of these funds are not registered and may be too small to be registered as they do not meet the £5,000 annual income threshold. Other funds may be special trusts and so only need to be registered where they are a distinct ongoing separate charity meeting the test in s.30(2) Charities Act 2011. Where a fund is a special trust and needs to be registered, it can be registered as a linked charity to the Chapter charity, rather than as a separate charity with its own registration number². As part of the process to register cathedral Chapters with the Charity Commission, any unregistered special trusts which do need to be registered can be registered and linked to the Chapter charity. The linking will reduce the administrative burden involved in the registration process and, as linked charities³, they will continue to be able to be accounted for within the Chapter's accounts.
- 1.3 Another reason why cathedrals may find it beneficial to review their restricted funds at this point is that some historic funds may have restrictions which mean that the money is not able to be used to best effect. This could be because the purposes for which the money can be used are out of date or because there is a restriction on the use of the capital and the income generated by the capital is too small to enable the stated purposes to be carried out. Therefore, this guidance seeks to inform Chapters about the statutory powers which may be available to them in the Charities Act 2011 to alter the objects, remove the restriction on the use of capital and/or amalgamate any of their small historic funds in advance of the registration process, so the Chapter consider whether they can use any of these powers to amalgamate or rationalise their funds. As a result, the Chapter will be clear which restricted funds may need to be registered with the Charity Commission when they embark on the registration process.

¹ This guidance does not refer to a cathedral's endowment.

² See para 2.3 below. Chapters will need to consider whether a fund is a special trust which requires to be registered, so that it can ask the Charity Commission whether a special trust needs to be registered and can be linked to the Chapter charity or not, which is a matter for the Charity Commission to decide pursuant to s.12(1) Charities Act 2011.

³For more information on linking charities please see the Charity Commission's Operational Guidance [g555a001 Linking Charities \(charitycommission.gov.uk\)](https://www.gov.uk/guidance/how-to-merge-charities) and its general guidance <https://www.gov.uk/guidance/how-to-merge-charities>

2. Restricted funds and cathedrals

- 2.1 Many cathedral Chapters hold restricted funds that are subject to a legal restriction on how the fund can be used. The legal restriction will usually be set out in the trust deed, Will or letter making the gift to the cathedral. Where the funds were gifted for purposes that are no longer relevant, or the sums involved are too small to be useful and so the fund has become an administrative burden, Chapters should seek legal advice on whether and how these restrictions can be removed or altered to enable the funds to be used to support their cathedral's work.
- 2.2 It is important to note that the term "restricted fund" is often used in a broad sense to encompass various types of funds. In this guidance the term "restricted funds" is used only to describe the types of funds in paragraph 2.2.3 below.

2.2.1 Designated funds

Designated funds are unrestricted funds that the trustees have decided to ringfence and designate for a certain purpose, such as a building project. Just as the trustees can resolve to designate such funds for a purpose they can also resolve to undesignate them by a resolution of the Chapter. No specific statutory powers or Charity Commission involvement is required in order to pass a resolution to undesignate funds, but the Chapter should inform their accountants/auditors.

2.2.2 Grant funds

Grants funds received by the Chapter are held on the trusts for which the grant was made and may be used only in accordance with any restrictions imposed by the grantor. Examples include s.21 or s.23 grant funding from the Church Commissioners, or Heritage Lottery funding for a building project. Whilst these funds are treated as "restricted" in terms of how they can be used, they are not the subject of this guidance.

2.2.3 Restricted funds

Restricted funds are restricted because of a legally binding restriction imposed by the donor. There are two common types of restriction:

- (a) Restriction on the fund's purposes: Property or money given to the cathedral to hold on trust for a specific charitable purpose which is narrower than the cathedral's purposes, for example a restricted fund that may only be used for cathedral music.
- (b) Restriction on the expenditure of the fund's capital: This is where the cathedral has a fund where only the income generated by the fund's capital can be expended but not the underlying capital. This may be a permanent restriction (where the fund is 'permanent endowment') or it may be a temporary restriction so that the capital can only be accessed after a specified event takes place ('expendable endowment'). An example of permanent endowment would be a legacy given to a cathedral with the requirement that it must be invested and only the income can be spent on the cathedral's purposes.

It is fairly common for a restricted fund to be subject to both types of restriction, for example where a legacy is left to a cathedral on trust for the gifted property

to be invested to produce an income and only the income can be spent, but that income must only be used for fabric maintenance.

- 2.3 Some restricted funds held by Chapters are “special trusts”. Special trusts are trusts held and administered by or on behalf of a charity for any special purposes of the charity, on separate trusts relating only to that property. The fund is administered in accordance with specific directions (in effect creating a separate or distinct fund), rather than simply being intended to be added to an existing fund of a charity. If a special trust is an ongoing separate distinct charity and has an income over the £5,000 per annum threshold then it would be liable to registration. Chapters need to consider whether or not a special trust needs to be separately registered with the Charity Commission so a request can be made to the Charity Commission to decide, pursuant to s.12 Charities Act 2011. The Charity Commission will also need to decide whether a special trust which does need to be registered can be linked to the Chapter charity⁴. It is anticipated that any decisions on the need to register special trusts and whether they can be linked to the Chapter charity will be taken by the Charity Commission as part of the pre-registration due diligence process before the Chapter applies for registration with the Charity Commission.
- 2.4 Restricted funds are held on legally distinct charitable trusts and so they do not normally form part of the cathedral’s corporate property and so will already be subject to the jurisdiction of the Charity Commission. If the capital of a restricted fund generates a gross annual income in excess of £5,000, that fund will normally need to be registered with the Charity Commission. If a fund’s income is less than £5,000 per annum, so it does not need to be registered, you may want to consider whether it would be advisable to merge it into another fund or to wind it up.
- 2.5 As restricted funds are unincorporated charities and subject to the Charity Commission’s jurisdiction, the trustees of a restricted fund can normally use the statutory powers in the Charities Act 2011 which are available to the trustees of unincorporated charities to alter or remove the legal restrictions on those funds, or to amalgamate funds, in certain circumstances. These statutory powers are outlined in sections 3, 4 and 5 below. As they can take time to exercise, Chapters are encouraged to consider whether they are able to exercise them in relation to any restricted funds held at an early stage.
- 2.6 Chapters should take professional advice before seeking to exercise these powers to ensure that they do so correctly.

3. Altering the purposes for which restricted funds are held⁵

- 3.1 The first step is to establish whether the restriction on the fund is legally binding. Often, on closer examination, there is no legal restriction on how the funds are used. For example, where there was a non-binding ‘request’ from a donor that the funds be spent in a particular way, it would not be legally binding on the trustees (although there may be a moral obligation that needs to be considered). In addition, funds may on occasion have

⁴ For more information on linking charities please see the Charity Commission’s Operational Guidance [g555a001 Linking Charities \(charitycommission.gov.uk\)](https://www.gov.uk/guidance/how-to-merge-charities) and its general guidance <https://www.gov.uk/guidance/how-to-merge-charities>

⁵ [g519a001 Alteration to Governing Documents and Transfer of Property: Unincorporated Charities \(charitycommission.gov.uk\)](https://www.gov.uk/guidance/how-to-merge-charities)

been incorrectly described as permanent endowment in a cathedral's accounts but, when the terms of the gift are reviewed, there may be no legal restriction on the expenditure of the capital of the fund. It is recommended that you seek legal advice on the circumstances of any fund if you consider that it has incorrectly been classed as a restricted fund and want to re-classify it correctly.

3.2 Where the restriction affecting the purposes for which the fund can be spent causes difficulties, for example, the purposes become out-of-date, you may want to change them to something more relevant to enable it to be used. It is not possible to change the purposes of a restricted fund by seeking the agreement of the donors for the change. However, there are powers in the Charities Act 2011 that enable the trustees of small unincorporated charities to alter their purposes⁶.

3.3 Smaller restricted funds⁷

Where the fund does not hold designated land and the gross income of the fund did not exceed £10,000 in the previous financial year, provided certain criteria are fulfilled (for example, the trustees are satisfied that it is expedient in the interests of the fund for the purposes to be replaced), the trustees can resolve to change the purposes of the fund, provided the Charity Commission agrees. The trustees must send the Charity Commission a copy of the resolution passed by at least two-thirds of the trustees present at a quorate trustees' meeting setting out the current and altered purposes, together with a statement of the trustees' reasons for passing it. The statement of reasons must explain how the new charitable purposes are as similar in character to those being replaced as is reasonably practical. The Charity Commission then has a period to object and it may ask for more information and insist that public notice is given.

3.4 Larger restricted funds

If the fund is too large for the above power to be exercised, trustees will need to apply to the Charity Commission to request that it alters the purposes of the fund using its powers to make a cy-près scheme. However, the reasons for applying for a cy-près scheme must meet the statutory criteria which may not be simple to demonstrate. For example, the Charity Commission may agree to make a scheme where the original purposes of the fund cannot be fulfilled, or where they no longer provide a suitable and effective method of using the fund, taking the spirit of the original gift and the current and social economic circumstances into account. When deciding on the new purposes, the Charity Commission must take various factors into account, including the desirability of securing that the fund is applied for purposes close to its original purposes, and the need for it to have purposes that are suitable and effective in the light of current social and economic circumstances. The procedure for making a scheme is set out in detail on the Charity Commission's website⁸.

⁶ Chapters may find the Charity Commission's guidance useful: [How to make changes to your charity's governing document - GOV.UK \(www.gov.uk\)](https://www.gov.uk/government/publications/how-we-approve-changes-to-charities)

⁷ s.275 Charities Act 2011

⁸ <https://www.gov.uk/topic/running-charity/managing-charity>
<https://www.gov.uk/government/publications/how-we-approve-changes-to-charities>
<https://www.gov.uk/guidance/change-a-charity-governing-document-by-scheme>

4. Removing the restriction on the expenditure of a fund's capital⁹

4.1 There are powers in the Charities Act 2011 which enable the trustees of certain permanent endowment funds to resolve to release the capital or part of the capital from the restriction so that the capital can be spent as well as the income. Whether or not Charity Commission consent is needed depends on the size of the fund and its income.

4.2 Smaller restricted funds¹⁰

Where the gross income of the fund did not exceed £1,000 in the previous financial year, or the market value of the whole permanent endowment is £10,000 or less, provided certain criteria are fulfilled the trustees can pass a formal resolution that the permanent endowment restrictions should be removed from all or part of the fund concerned. The trustees must be satisfied that the purposes of the fund could be carried out more effectively if they use some or all of the fund's permanent endowment as well as its income, rather than income on its own. Once passed, the Charity Commission's consent is not needed.

4.3 Larger restricted funds¹¹

Where the gross income of the fund exceeded £1,000 in the previous financial year and the market value of the whole permanent endowment exceeds £10,000, provided certain criteria are fulfilled the trustees can pass a formal resolution at a quorate trustees' meeting that the permanent endowment restrictions should be removed from all or part of the fund concerned. The trustees must be satisfied that the purposes of the fund could be carried out more effectively if they use some or all of the fund's permanent endowment as well as its income, rather than income on its own.

The trustees must send the Charity Commission a copy of the resolution passed by at a quorate trustees' meeting together with a statement of the trustees' reasons for passing it. The statement of reasons must explain the decision made by trustees is reasonable considering:

- (a) the purposes of the trusts for which the permanent endowment was given;
- (b) that what is proposed remains within the spirit of the original gift; and
- (c) that those purposes could be carried out more effectively by expending the permanent endowment rather than simply relying on its income.

In looking at the fund's purposes and the spirit of the original gift the Charity Commission will take account of the wishes of the donor for use of the endowment and any changes in the charity's circumstances. The Commission then has a period to object and it may ask for more information and insist that public notice is given.

⁹<https://www.gov.uk/guidance/permanent-endowment-rules-for-charities-g545a001-identifying-and-spending-permanent-endowment> (charitycommission.gov.uk)

¹⁰ S.281 Charities Act 2011 (where the fund has been identified by the Charity Commission as a special trust, s.288 of the Charities Act 2011)

¹¹ S.282 Charities Act 2011 (where the fund has been identified by the Charity Commission as a special trust, s.289 of the Charities Act 2011)

5. Amalgamating small restricted funds with substantially similar purposes¹²¹³

- 5.1 Where the gross income of the fund did not exceed £10,000 in the previous financial year, and no designated land is held in the fund, provided that the trustees are satisfied that the objects of the transferee fund are substantially similar to those of the transferor fund, the trustees may be able to resolve to transfer the property and/or funds held in one charitable fund to another charitable fund to amalgamate small funds. The trustees of the funds must be satisfied that to do so is expedient in the interests of furthering the purposes for which the property is held by the transferor fund. Care must be taken to use the appropriate power where property that is subject to a restriction on the expenditure of the capital is being transferred.
- 5.2 The trustees of the transferor fund must send the Charity Commission a copy of the resolution passed by at least two-thirds of the trustees present at a quorate trustees' meeting, together with a statement of the trustees' reasons for passing it. The Charity Commission then has a period to object and it may ask for more information.

¹² S.268, s.273 and s.274 Charities Act 2011

¹³ [g519a001 Alteration to Governing Documents and Transfer of Property: Unincorporated Charities \(charitycommission.gov.uk\)](#)