



## BRIEFING PAPER

# Charities & Insolvency

**A TRUSTEE RECENTLY ASKED:  
"AM I PERSONALLY LIABLE IF MY  
CHARITY BECOMES INSOLVENT"?**

**INDEPENDENT EXAMINERS LIMITED**

Sovereign Centre · Yapton Lane · Walberton · West Sussex · BN18 0AS

Tel: 01243 555611 · Email: [support@iel.org.uk](mailto:support@iel.org.uk)

Web: [www.iel.org.uk](http://www.iel.org.uk)

**The following advice can be summarised by saying, if you are in financial difficulties, don't put your head in the sand and hope someone else (God even?) will sort it out. If you do, you could get into trouble. On the other hand if you seek appropriate help and advice, you are going a long way to staying out of the personal liability area.**

**If your charity is unincorporated:**

Any liabilities will pass to the trustees and bankruptcy rules will apply if the debts cannot be paid, and the trustees can't meet them personally.

**If your charity is incorporated:**

The Insolvency Act 1986, as amended by the Insolvency Act 2000 and the Enterprise Act 2002 will apply.

**1. The Tests for insolvency:**

- a. Going Concern or Cash Flow:** Can the charity pay its debts as they fall due? Does it have sufficient cash, short term debtors, investments etc to meet its immediate liabilities and continue to do so in the short term?
- b. Balance Sheet test:** The charity could be insolvent if its liabilities exceed its assets.

**2. Liability of trustees:**

- a. Duty to act prudently.** They must ensure that there is sound management in place including financial procedures and they must comply with the law.
- b. Loss of limited liability protection:** This could happen if the charity has been carrying on fraudulently, or if it has been incurring debts that the directors knew the charity could not meet (wrongful trading).
- c. Onus of proof:** On the liquidator. Intent to defraud must be proven, and there must be evidence of dishonesty. Wrongful trading: the liquidator will need to show that the directors failed to exercise appropriate diligence in monitoring the company's affairs, and failed to take timely corrective action. (Note, this can apply to shadow directors)

**3. What should I do if insolvency beckons?**

- a. Unincorporated charity:** The trustees must take immediate action to reduce outgoings and raise cash. In view of their personal risk trustees might need to review whether the charity should be closed. However this in itself will often add to the liabilities.
- b. Incorporated charity:** They must make sure that their protection of limited liability is not put at risk. They must be able to show that they did all they reasonably could to protect the charity's assets.

**4. IMPORTANT STEPS WHICH MUST BE TAKEN:** If the directors/trustees know, or ought to have known that the charity cannot survive they must:

- a. Understand** that their primary duty now is to the creditors not the charity and its work.

- b. Ensure** that they take appropriate advice and be able to show they have acted responsibly.
- c. Meet** regularly to show they are taking the issues seriously and acting in the best interests of creditors.
- d. Make** sure there is a proper paper trail of meetings, advice and decisions.
- e. Don't** ignore the problems, hoping they will go away. They probably won't, and it's down to the Trustees to sort things out.
- f. Always** remember that trustees and directors are 'jointly and severally' liable. This means that trustees and directors cannot plead ignorance or the fact that they were leaving it all to someone else. Also liabilities cannot be avoided by resignation.

Finally: If you are in difficulties contact us as soon as possible. We are charity specialists with extensive experience of working with charities in difficulties. We are not insolvency specialists but we can guide you into that step if it's needed.

### Notes prepared by Daryl Martin

With thanks to the Directory of Social Change for some of this material.

Also [www.bateswells.co.uk](http://www.bateswells.co.uk).

**COPYRIGHT:**

This publication is the copyright of Independent Examiners Ltd. and may not be reproduced without permission. If you would like to reproduce or publish this material, permission should be sought in advance by emailing [support@iel.org.uk](mailto:support@iel.org.uk) or telephoning 01243 555611

**DISCLAIMER:**

This guide is intended only to give very general advice in relation to the topics covered. These guidelines should not be relied upon as a substitute for obtaining specific and more detailed advice in relation to a particular matter. This material may be drawn from a variety of sources and we give credit where we can. If we have failed to do this on any occasion please let us know so we can put it right.

**INDEPENDENT EXAMINERS LIMITED**

Sovereign Centre · Yapton Lane · Walberton · West Sussex · BN18 0AS

Tel: 01243 555611 · Email: [support@iel.org.uk](mailto:support@iel.org.uk)

Web: [www.iel.org.uk](http://www.iel.org.uk)