

# Pembrokeshire Association of Voluntary Services

Your local county voluntary council



## 5. Trustees and governance

### 5.7 Liability of trustees and governing body members

#### **Liability generally**

##### **What does liability mean?**

Liability means being held legally responsible for actions taken and for defaults (actions not taken which should have been).

##### **Who can be liable?**

Depending upon the legal status of an organisation, and the circumstances in which liability comes about, liability may rest with:

- a corporate body (company; Community Interest Company etc)
- the members of a governing body
- employees of an organisation
- the members of an organisation (rarely happens)
- people authorised to act on behalf of an organisation (agent)
- people claiming to act on behalf of an organisation (even if not authorised to do so)
- volunteers (rarely happens)

##### **How does liability come about?**

Liabilities arise where individuals or organisations:

- are in breach of criminal law
- are in breach of statutory duty
- are in breach of trust
- are in breach of contract
- are in breach of covenants or other property rights
- are in breach of duties under an insolvency
- cause a tort to be committed

##### **Personal liability**

Personal liability arises where a member of the governing body, organisation member, employee, volunteer or other person associated with an organisation has to use their own money to meet the organisation's obligations, make repayment to it for losses it incurs, unauthorised personal benefits or penalties imposed upon the organisation for breaches of the law.

## **Liability of companies and other legal forms**

- Liability of members is limited to the amount of guarantee they have made or unpaid shares they hold
- All other liabilities generally rest with the company, but in some situations can rest with the directors, company secretary and senior employees
- Other legal forms that enjoy limited liability are Industrial and Provident Societies, Limited Liability Partnerships, Community Interest Companies and the soon to be introduced Charitable Incorporated Organisations.

## **Liability of unincorporated associations and trusts**

- Liability is joint and several, and generally rests with the members of the governing body
- No limited liability protection is available
- **NB.** Incorporation of a charitable governing body under section 50, Charities Act 1993 – creates a single legal entity for title and succession purposes but does not provide limited liability

## **How is it decided who is liable?**

Who is liable will depend upon:

- whether or not the organisation is incorporated
- who authorised an action and whether they were authorised to do so
- who carried out an action and whether they were authorised to do so
- who omitted to do something they had a duty to do

## **Apportionment of liability**

Where members of an organisation or the governing body are held liable for the organisation's financial obligations the liability is **joint and several**. This means that each member could be held liable for all or any part of the obligation. But, a distinction should be drawn between:

- those people who are adjudged to be held liable
- those people who are sued to recover a loss or as compensation for damage

Where 2 or more members are held liable for the same tortious (e.g. negligence) or contractual loss/damage, but only selected individuals are sued, they can seek to recover a contribution from the other liable individuals under the **Civil Liability (Contribution) Act 1978**.

## **Can individuals be held liable for acts of others?**

In general the answer to this question is no; people are only liable for their own actions or failures to act. But there are many exceptions in both criminal and civil law. For example where:

- An employer has **vicarious liability** for acts of negligence and other torts committed by its employees during the course of their employment.

- Trustees may be liable for losses caused to the charity by people acting on their behalf who were not properly supervised etc (see delegation powers and duty of care under Trustee Act 2000).
- A person (the **agent**) enters into a contract on behalf and with the authority of another (the **principal**), the principal remains liable for the contract.
- Statute law can impose civil and criminal liability, particularly in the areas of employment and health & safety (e.g. discrimination; unsafe working premises).
- A person may be liable if they authorise, instruct or allow another person to commit a criminal act.

### **Who are charity trustees?**

Anyone who controls and organisation should be thought of as a 'governing body member', regardless of what their title might be. Governing body members in charities are known as 'trustees', and charity law places additional responsibilities on them.

**Section 97(1) of the Charities Act 1993** defines charity trustees as '... the persons having the general control and management of the administration of a charity'. Those who fit this description are trustees regardless of what they are actually called. In general terms trustees are responsible for the proper administration of the charity in accordance with the law, and its trusts as set out in the governing document. Their overriding duty is to pursue the objects of the charity and they must apply the income and property of the charity exclusively for these objects.

### **Some specific trustee liability points**

- Trustees remain liable - even after retirement - for the actions taken during their period of office.
- New trustees are not generally liable for acts taken before their period of office, but must seek to put irregularities right on discovery otherwise they could become liable for them.
- Generally governing body members are not liable for the unauthorised/ultra vires actions of 'rogue' trustees, but they must ensure all steps are taken to avoid such an occurrence.
- Do not forget trustees have specific responsibilities under charity law and regulation (e.g. SORP; personal benefit; etc).

### **Specific areas of liability**

#### **Breach of criminal law and statutory duties**

- Criminal law is breached when someone commits an offence against other persons, property or the public interest. Prosecution is normally brought by the state rather than by individuals (although private prosecutions are made).
- Penalties for failing to comply with statutory duties are technically criminal because they are enforced by the State (e.g. health & safety).

- Normally a person who commits a criminal act is liable for their own actions but a corporate body can be liable for its criminal actions (e.g. corporate manslaughter) and employers can be vicariously liable for the criminal acts of employees.
- Governing body members are personally liable for their own criminal acts as individuals or as a body.
- Individuals are always liable for their own criminal acts regardless of whether committed as an individual, employee, volunteer, governing body member, etc.

Incorporated organisations normally attract criminal liability directly but in certain situations the governing body members can be personally liable, including failure to operate PAYE or comply with statutory duties.

### **Breach of contract**

A contract is a legal agreement enforceable by the courts. Usually an organisation's liability under contract arises if:

- the organisation cannot pay sums due under a contract
- it is unable or fails to supply goods or services it has committed itself to provide
- it has supplied goods or services which do not meet the standards specified by the contract or required by law
- it breaches other conditions of a contract (E.g. failing to comply with reporting obligations)

Questions of liability under contract depend on whether an organisation is incorporated or not.

**Corporate bodies** are **legal persons** and can be parties to legally enforceable agreements in their own right. The members of the company and its governing body act as agents of the company and are not direct parties to the contract. They are protected from personal liability for breach of contract provided that:

- the contract is within the objects and powers of the organisation
- those who agreed to the contract had authority to do so
- those who agreed to the contract were not disqualified from acting as directors of a company
- they do not allow the company to contract fraudulently or whilst insolvent

**Unincorporated organisations** are not legal persons and cannot enter into contracts. Individuals must act on behalf of the organisation and the contractor's liability is **unlimited**. Primary liability rests with the **principals** – those who authorised a contract or action. Those who merely enter into a contract with authority are **agents**. The principals are typically the trustees either directly, or if they authorise delegation of authority, but individual trustees can be liable if they act independently of the trustee body or outside their authority. It is important to note:

- NB principals (including trustees) remain liable for contracts after leaving office and it passes to the estate on death unless passed over by a novation agreement.
- **Contracts (Rights of Third Parties) Act 1999** – gives third parties a right to enforce terms that benefit them in contracts to which they are not a direct party - usually excluded.

### **Breach of trust and fiduciary duty**

- Breach of trust, or fiduciary duty (to act in good faith), occurs when someone in a position of trust breaks that trust.
- Trustees are those people who hold assets in trust for defined beneficiaries to be administered in accordance with specified objects – they have a duty of trust (e.g. charity).
- Trustees and governing body members of non-charitable organisations also have a fiduciary duty to their organisation. Fiduciary duty is similar to the duty of trust but is of a lower standard in non-charitable companies and other incorporated organisations than charitable ones.
- Fiduciary duties of company directors are set out in the **Companies Acts**.

Breaches of trust and fiduciary duty by an individual generally result in personal liability of the individual to the organisation. These may arise where all or some of the governing body members:

- Carry out, or use charity money/property for, activities which are outside the scope of the organisation's objects, area of benefit, or are not charitable (e.g. political campaigning; trading).
- Exercise powers or carry out activities which are not permitted in the organisation's governing document, or fail to obtain consent of the Charity Commission/Court where consent is required.
- Cause loss to the organisation through mismanagement, a failure to exercise a proper duty of care or take professional advice.
- Steal from the organisation or make an unauthorised personal gain/benefit.
- Misuse information obtained through their position as a trustee or governing body member.

Trustees are liable for their own acts and defaults, and are jointly and severally for decisions made by the governing body in which they have participated. But they are not liable for breaches by former trustees, although they are expected to take remedial action to recover losses once discovered. Where trustees believe that a breach is likely to be committed by a fellow trustee(s), they must take positive action to raise their concerns, and if they retire before the breach should seek relief of liability in writing. Trustees who retire, and the estate of trustees who die, remain liable for breaches committed by them whilst in office. **NB.** Limited liability does not protect directors/trustees against breach of trust or fiduciary duty.

## **Tort**

A **tort** is a civil wrong which results in injury, loss or damage to a person. Generally a tort requires intention to commit the act, or negligence; however, committing some torts attracts **Strict Liability** where no intent or negligence is required. Common torts include negligence; defamation; nuisance, and trespass.

Those liable for torts:

- Torts can be committed by individuals or corporate bodies.
- Individuals are liable for their own tortious acts and for those they authorise. But employers also have vicarious liability for the torts of their employees when carried out in the course of their employment. This is the case even if the employer did not authorise or know about the act.
- Organisations can be vicariously liable for the acts of volunteers where they are treating them as employees, or directly liable if they have failed to properly train and supervise them.
- Members of a governing body are liable for their own torts, those of the governing body, those of the organisation or others they authorised or allowed to happen.
- Governing body members will not generally be liable for torts of the governing body or organisation where he/she did not know of the decision or action at the time it was taken, or knew about but did not participate in it.
- Ordinary members of an unincorporated organisation may all be liable in tort where: they all authorised or carried it out; are in overall control of the activity; are deemed to be the de facto occupiers of premises, or are deemed to be the de facto employer.

## **Protecting against liability**

Charities and voluntary organisations can guard against, or minimise, personal and organisational liability in a number of ways:

### **Incorporation**

Incorporating an organisation as one of the company forms creates a separate legal entity with limited liability which can contract, hold land etc, and thus be legally liable in its own right distinct from its members:

- Liability of members is limited to the amount of guarantee they have made or unpaid shares they hold.
- Unincorporated associations and trusts are not corporate bodies and thus do not enjoy limited liability – the governing body members are personally liable for the actions of the organisation.

Incorporation does not protect the members of the governing body against:

- fines or penalties for their own or the organisation's criminal acts, or breaches of statutory duty

- liability to the organisation for their own breaches of trust or fiduciary duty
- liability on contracts which are beyond the objects or powers of the organisation i.e. acting **ultra vires** (unless subsequently ratified by the company members in a non-charitable company only)
- liability for debts incurred whilst the company is insolvent, or is heading for insolvency - **wrongful and fraudulent trading**

### **Charity Commission**

Charity trustees may seek **advice in writing** from the Charity Commission under **section 29 of the Charities Act 1993** before carrying out an act about which they are uncertain, or about the proper administration of the charity generally. Trustees cannot subsequently be held liable for any breach of trust that arises provided:

- they revealed all material facts to the Commission at the time of seeking advice
- they act strictly in keeping with the advice they are given

**NB. section 73D of the Charities Act 1993** (as inserted by Charities Act 2006, s.38) has introduced a power for the Charity Commission to grant relief for a breach of trust or duty where it is considered the trustee has acted honestly and reasonably.

### **Limiting liability in the governing document**

It is possible to include a clause in the constitution of an unincorporated organisation saying that ordinary members are not liable for the organisation's debts or actions. This does not protect them if they:

- are members of the organisations governing body
- are principals to a contract
- commit a criminal or tortious act

Similarly, the governing document of a trust may seek to limit the liability of trustees for losses caused to the trust/charity where proper advice has been taken (e.g. poor performance of investments).

### **Contractual clauses limiting liability**

Unincorporated organisations and trusts should consider including in contracts a clause limiting the liability of members and governing body members to the extent of the assets of the organisation (but such clauses are often resisted).

To avoid the contract being subject to other agreements/correspondence etc, you may have forgotten about or are unaware of, it is always sensible to include an 'entire agreement' clause specifying the present document is the only binding contract.

## Exclusion of liability

In some instances liability may be limited by an **exclusion of liability** or **disclaimer clause** in a contract, lease etc, or a notice, but legal advice should be sought before trying to limit or exclude liability in this manner. Liability cannot be excluded in cases where a clear duty of care can be proven, or where there is legal requirement or statutory duty to protect. Reasonable steps have to be taken to meet these obligations and liability for death or personal injury can never be excluded (**Unfair Contract Terms Act 1977, s.2**)

## Indemnity

**To indemnify someone means to compensate them for a loss suffered**; however, this right is worthless if the assets or insurance cover of the organisation do not meet the total liability. There is no right to be indemnified for fines or penalties or where the individual is liable to the organisation itself (e.g. breach of trust).

Individuals in voluntary organisations and charities may have a right to indemnity under:

- **Statute:**
  - Trustees of a trust or charity are entitled to be reimbursed out of trust funds for expenses properly incurred on behalf of the trust if acting with authority and due care (Trustee Act 2000, s.31).
  - A company can provide loans and pay the legal fees of a director, company secretary, senior employee or auditor for the successful defence of an action relating to offences against the company (but cannot indemnify for penalties in a successful action).
- **Common law:** if a member of the governing body of a non-charitable association, or an ordinary member of any association, is successfully sued by a third party they are entitled to be indemnified for damages and costs if they were sued as a representative of all the members, or they were carrying out activities for and with the approval of the association and its members. The right to indemnity is limited to the assets of the organisation and indemnity cannot be sought from the other members unless permitted by the governing document.
- **Governing document:** can give additional rights of indemnity to ordinary and governing body members out of organisational funds for liabilities properly incurred in managing the organisation's affairs. However, such a clause typically set out a number of exclusions such as acting ultra vires. **NB.** If the organisation has holding trustees provision should be made to indemnify them for losses incurred in the discharge of their duties.

## Contribution

- Where two or more governing body members are jointly and severally liable for a tort or contractual claim, but only some are sued, they can seek a contribution from the others to be assessed by the court against their relative responsibility under the **Civil Liability (Contribution) Act 1978**.

- In common law, if some or all of the members of a governing body are liable for a contract and one or more pay a disproportionate share, they are entitled to a contribution from the others.

## Further information

Charity Commission for England & Wales

Tel: 0870 333 0123

[www.charity-commission.gov.uk](http://www.charity-commission.gov.uk)

*Reducing the Risks - A Guide to Trustee Liabilities,*

[www.ncvo-vol.org.uk](http://www.ncvo-vol.org.uk)

## Disclaimer

The information provided in this sheet is intended for guidance only. It is not a substitute for professional advice and we cannot accept any responsibility for loss occasioned as a result of any person acting or refraining from acting upon it.

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