



31 October 2011

Our ref: ICAEW Rep 103/11

Your ref:

The Secretary
Law Reform Commission
20/F Harcourt House
39, Gloucester Road
Hong Kong

Dear Sir

Consultation paper on Charities

ICAEW is pleased to respond to your request for comments on your consultation paper on Charities. The attached response is subject only to a final review by ICAEW in London and a final version, which I do not anticipate will differ in substance to the attached, will be submitted to you over the next few days

Please contact me should you wish to discuss any of the points raised in the attached response.

Yours faithfully

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ICAEW REPRESENTATION

Charities

Memorandum of comment submitted in October by ICAEW, in response to the Law Reform Commission consultation paper Charities published in June 2011.

Contents	Paragraph
Introduction	1
Who we are	2
Major points	5
Responses to specific questions	9

INTRODUCTION

1. ICAEW Foundation in Hong Kong welcomes the opportunity to comment on the consultation paper on *Charities* published by the Law Reform Commission of Hong Kong Charities Sub Committee in June 2011.

WHO WE ARE

2. ICAEW Foundation in Hong Kong was set up and launched in 2011 as a registered charity in Hong Kong, sharing the same trustees as the ICAEW Foundation in the UK. The charity aims to provide meaningful annual bursaries to talented aspiring undergraduates and post-graduate students in Hong Kong universities; these will include opportunities for overseas exchanges.
3. ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter which obliges us to work in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 136,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.
4. ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.

MAJOR POINTS

Support for the initiative

5. We welcome most of the recommendations set out in the consultation paper, as set out in more detail below.
6. The paper does not include any evidence that the current structure has been the cause of, or has concealed, the misuse of charitable funds. Indeed there are no statistics relating to the number or type of governance failures in the consultation paper. If there are compelling reasons for the establishment of a Charities Commission, these should be explained to the public to justify the administrative costs of such a statutory body.
7. If there are good reasons for the proposed Commission and the transfer of responsibility and powers to it, then we suggest that such transfers of responsibility should be made only where absolutely necessary. If specific powers and responsibilities can effectively remain where they are at present, they should so remain to avoid unnecessary delay in the implementation of better governance and unnecessary additional costs.
8. As examples, the Commission should be set up to supervise all aspects of the authorization and regulation of Charities but the actual operations could remain within the existing Government Departments:
 - (a) Setting up a publicly available register of charities – the Inland Revenue Department already holds a list of charities that have been granted tax exempt status, and the Companies Registry has a record of all those charities that are limited companies (more than 70% of the total number of charities in 2007 according to the consultation paper). These existing lists could form the basis of a publicly accessible register. The IRD's records are currently not accessible to the public for obvious reasons, so the Companies Registry could require all charities seeking approval from the IRD to become registered alongside the existing corporate charities.

This would mean that the Companies Registry would administer the register of charities, reporting to the proposed Commission. This would save the cost and time delay that would be involved in setting up new systems and staffing a separate charities register.

- (b) Filing of financial and other information – Assuming the Companies Registry holds the register of charities, it could require the filing of the annual return and financial information. The Companies Registry requires filing by limited companies so it would be a minor expansion of its current role to cover charities that are not limited companies. Any defaults by charities in the filing requirements would then be reported to the Commission for investigation and/or regulatory action.
- (c) Other functions and powers – all those listed in Recommendation 19 could be carried out by the Companies Registry in the first instance, referring exceptions to the Charities Commission only when necessary. Disciplinary powers and investigations would rest with the Commission.

RESPONSES TO SPECIFIC QUESTIONS

Q1: Do you think that there should be a clear statutory definition of what constitutes a charitable purpose?

- 9. Yes, there should be a statutory definition of what constitutes a charitable purpose.

Q2: If you have answered "yes" to Question 1, please also answer the following questions:

- (a) Do you think that the statutory definition of what constitutes a charitable purpose that is exclusively charitable should include all of the heads of charitable purpose set out in Recommendation 2?
- (b) If not, which head or heads do you think should be deleted from the list? Which should be amended, and how? Are there any other heads which you think should be added to the list of heads of charitable purpose?
- (c) Do you think that charities falling under any of the heads of charitable purpose must be also for the public benefit?
- (d) Do you think that "*The advancement of human rights, conflict resolution or reconciliation*" should be included in the statutory list of heads of charitable purpose?

- 10. We agree with the heads of charitable purpose in Recommendation 1 and consider that they should be for the public benefit. We do not consider that the advancement of human rights should be included.

Q3: Do you think that the various existing legal forms for charities should be reformed?

Q4: If you have answered "yes" to Question 3, please also answer the following questions:

- (a) Do you think that the current system of allowing a variety of legal forms of charitable organisations to exist should continue, and if so, what modifications, if any, should be made to it? (See Recommendation 3.)
- (b) Alternatively, do you think that a unitary approach of imposing one uniform model of charitable organisation structure should be adopted, and if so, what form should that model take? (See Recommendation 3.)

- 11. We do not think it is necessary for the legal forms for charities should be changed – to do so would cause major disruptions and cost for those charities that do not fall within the required

legal form and could cause some to have to cease their work. All the governance rules and reporting can apply to any of the currently permitted legal forms.

Q5: Do you agree that all charitable organisations which:

- (a) make any charitable appeal to the public; and/or
 - (b) seek tax exemption
- should be required to register?

- 12.** Yes – all charities should be required to register. We suggest that the registration process should be kept simple to minimise costs to smaller charities. If the registration process is complex and involves excessive costs (such as legal or other professional fees), then consideration should be given to exempting smaller charities or having a small charity register with simplified registration processes.

Q6: If you agree that charitable organisations should be registered, but do not agree with the pre-conditions for registration set out in Question 5(a) and (b), please answer the following questions:

- (a) which pre-condition(s) do you think should not be required, and why? Are there other pre-conditions which you think should be included, and why?
- (b) Do you agree that the list of registered charitable organisations should be established and maintained by the future charity commission?
- (c) Do you agree that this list should be available for public inspection?
- (d) Do you agree that the application process for registration should not be subject to public notification?

- 13.** The preconditions are acceptable. The register can be maintained by either the IRD or the Companies Registry as set out in the opening paragraphs of this submission. As the IRD's records are not normally accessible to the public, the Companies Registry is probably the more logical department for maintaining the register that should be open to the public. The Companies Registry can also determine the use of particular names of charities. We see no reason for the application process for registration to be subject to public notification.

Q7: Do you think that registered charitable organisations should be required to file an annual activity report to the future charity commission, and if so, should the report be provided in a standard form and should it cover the list of matters set out in Recommendation 5? Are there any matters which you think should be deleted from the list? Are there any matters which should be added?

Q8: Do you think that charity trustees or directors of a registered charity should be under a duty to declare any conflicts of interest and personal interests?

- 14.** Registered charities should be required to file the activity report as set out in Recommendation 5, and it should incorporate the declaration of conflicts of interest.

Q9: Recommendation 7 proposes that:

"(1) Registered charitable organisations with an annual income exceeding \$500,000 should be required to file an auditors' report and financial statements with the future charity commission.

(2) Without prejudice to the statutory requirements under the Companies Ordinance (Cap 32), registered charitable organisations with an annual income not exceeding \$500,000 should be required to file financial statements certified by the Board of these charitable organisations with the future charity commission.

(3) *The auditor's report and financial statements submitted by charitable organisations to the future charity commission should be accessible to the public.*

Do you agree with the requirements set out in Recommendation 7? If not, which requirements do you think should be deleted? Are there other requirements which you think should be added?

- 15.** We agree with the recommended requirements for the preparation, audit and filing of financial information. To minimize the administrative burden on charities, there should only be one filing required each year that incorporates all the required information or requires it to be attached to the return form. To ease the burden on very small charities, we suggest that those with less than a prescribed level of income should be exempted from the financial information filing requirement, or at least only a minimum of such information should be required.

Q10: Do you think that for every charity registered with the future charity commission, an activities report and financial statements should be filed with the future charity commission on an annual basis, and if so, what should be the contents included in the annual report of activities?

- 16.** As stated in the opening paragraphs of this submission, the annual filing should be with the Companies Registry, which already has procedures for receiving such filings for companies, and not with the Charities Commission. The activities report, which, as suggested in paragraph 15 above, should be filed as part of the annual return, should include the information proposed in the consultation paper, but changes in directors and registered office address should probably be filed as such changes occur (as is currently required for companies).

Our suggestion that the Companies Registry should maintain the register of charities and therefore be the recipient of annual and other filings is made in the interests of efficiency (as it already has the systems in place for dealing with this activity) and to minimise disruption to the majority of charities that are already registered with the Companies Registry. It must be apparent that this suggestion will require proper communication and a good working relationship between the staff of the Charities Commission and that of the Companies registry.

Q11: Do you think that charity trustees or directors of a registered charity should be under a statutory duty to keep proper accounting records of the charity which are sufficient to show and explain all transactions of the charity, and if so, should such records be retained for at least seven years?

- 17.** Yes, the trustees or directors should have a statutory duty to maintain and retain proper accounting records.

Q12: Do you agree that the future charity commission should be vested with the power to investigate any alleged mismanagement and misconduct of charitable organisations with regard to its charitable objects?

Q16: Do you agree that the future charity commission should be vested with powers relating to enforcement and remedies in cases of non-compliance by charities with their

Q18: Do you think that the future charity commission should be vested with the power to protect charities' property in cases of misconduct or mismanagement in their administration

Q19. If you have answered "yes" to Question 18, do you agree that this power should include, but not be limited to, the powers to:

- "(1) appoint additional trustees or directors of the charity;
(2) suspend or remove trustees, directors or officers of the charity;***

**(3) vest property of charities in an official custodian; and
(4) require persons holding property on behalf of the charity not to part with the property without the approval of the future charity commission"**

as listed in Recommendation 12? If not, which powers should not be included? Which additional powers to protect property of charities, if any, should be given to the future charity commission?

18. We agree with that the Charities Commission should have the powers etc. set out in Recommendations 9 -12. Care will be needed to ensure that the responsibilities of the Charities Commission and other investigatory bodies are clearly defined. There will presumably be situations where the Charities Commission discover criminal activities and may need to pass the investigatory process and subsequent prosecutions to the HK Police or the ICAC

Q20: Do you think that there should be a sole regulatory body (a "one-stop shop") to process and grant all permits and licences necessary for charitable fundraising, and to monitor the use of funds raised by such activities?

Q21: If you have answered "yes" to Question 20, please also answer the following questions:

(a) Do you think that this "one-stop shop" service should be provided by the future charity commission, and that the commission should be vested with the powers and duties currently exercised by the Social Welfare Department, the Food and Environmental Hygiene Department and the Television and Entertainment Licencing Authority in relation to authorising charity fundraising activities in public places and those involving lotteries?

(b) Do you think that the future charity commission should be responsible for enabling public access to information on fundraising activities and for providing an enquiry response service to the public?

19. We do not consider it necessary to transfer the issue of permits and licences from the existing departments as to do so would cause unnecessary delay in establishing the governance and reporting processes envisaged elsewhere in the proposals. Existing charities are well aware of the current requirements, and newly registered charities can be provided with the relevant rules and guidelines so that they know how to apply for the relevant licences etc from the relevant departments. To have one government department dealing with the issue of a licence to a charity, and a different department dealing with the issue of the same licence for a non-charity can only cause confusion and could result in inconsistent application of the same rules.

Q22: How, and to what extent, do you think solicitation of donations via the internet should be regulated in order to minimise the risk of abuse, while at the same time not unduly inhibiting the work of *bona fide* charities?

20. We do not believe that there is any practical means of regulating the solicitation of donations through the internet, particularly where such fundraising is conducted by non-Hong Kong charities. We agree that the most practical steps to minimize any abuse is through raising public awareness of the issue and requiring the prominent display of the charity's status in Hong Kong and its registration number in the web-site concerned.

Q23: Do you agree that for all forms of charitable fundraising activities, the registration number of any charitable organisation involved in those activities should be prominently displayed on any related documents, or displayed on any means through which appeals for charitable donations are made (such as solicitation leaflets)?

21. We agree that the registration number should be displayed on all fundraising documents.

Q24: Do you agree that the future charity commission should carry out the initiatives listed in Recommendation 15 to promote good practice by professional fundraisers and, if not, which initiatives should not be included? Are there other initiatives which you think should be added to the list?

22. The initiatives set out in Recommendation 15 should be implemented by the Charities Commission. We can foresee some practical issues with enforcement of the initiatives in respect of professional fund raisers. Are the professional fund raisers, or the professional bodies to which they belong going to be registered with the Charities Commission to achieve this?

Q25: Do you think that there should be an express power given to the future charity commission to sanction organisations for non-compliance with the terms laid down in codes of conduct issued by the commission?

23. We agree that this power should be granted to the Charities Commission, but there will be the practical issues identified in paragraph 22 above.

Q26: Do you agree that existing powers of tax exemption and functions of periodic review of charities for taxation purposes should remain with the Inland Revenue Department?

Q27. Do you agree that tax exemption should be granted to a charity by the Inland Revenue Department only when the charity has been registered with the future charity commission and, subject to this, there should be no change to the existing law on the taxation of charities in Hong Kong

Q28. Do you think that the future charity commission should collaborate with the Inland Revenue Department as far as possible, particularly by the provision of relevant charities' accounts information, to facilitate the Inland Revenue Department's functions in assessing charities for tax where appropriate

Q29. Do you agree that the Administration should ensure that sufficient resources are allocated to the Inland Revenue Department to carry out the function of reviewing annual accounts submitted by charities to the future charity commission?

24. We agree that the IRD should continue to grant tax exemptions etc. and that this should only be granted once the charity has been registered. To save administrative time for the charities, the application for registration should also include the application for tax exemption so that the Companies Registry would pass the relevant part of the application to the IRD and maintain the information about the tax status in the register of charities.
If any small charities are granted exemption from registration (see our response to Q5 above), there should still be a process for them to obtain the same tax status as a registered charity.

Q30: Do you think that legislation should be introduced in Hong Kong along the lines of the English statutory model of the *cy-près* doctrine (comprised in provisions of the English Charities Act 1993, as amended in 2006), so as to provide a statutory basis for the *cy-près* doctrine in Hong Kong and to broaden the scope of its application?

Q31. If you have answered "yes" to Question 30, do you agree that in line with the English model, the *cy-près* doctrine should be broadened in Hong Kong so that it may apply in the situations listed in Recommendation 17, even where it is not impossible or impractical to carry out the charitable purpose of the charitable trust?

Q32. Do you agree that the future charity commission should be empowered by statute to administer the application of the *cy-près* doctrine in particular cases?

25. We concur with Hong Kong applying the *cy-près* doctrine.

Q33: Do you think that a charity commission should be set up as a sole regulatory body for charities in Hong Kong?

Q34. If you have answered "yes" to Question 33, do you agree to the objectives of the future charity commission set out in Recommendation 18? If not, what objectives do you think should not be included in the list? Are there other objectives which you think should be added to the list?

Q35. Do you agree that the future charity commission should have the functions and powers set out at Recommendation 19? If not, which functions and powers should not be included in the list? Which additional functions and powers, if any, should be given to the future charity commission?

Q36. Do you agree that a charitable organisation or person aggrieved by a decision of the future charity commission, either:

- "(1) in its refusal to register an organisation as a charitable organisation;*
 - (2) in the exercise of its powers relating to enforcement and remedies due to non-compliance of charities with their legal obligations; or*
 - (3) in the application of the cy-près doctrine"*
- should have the right to appeal to the Court of First Instance?

26. As discussed in paragraphs 5 – 8 of this submission, if it is necessary to establish a new Charities Commission, it should be done in a cost effective and timely manner by granting it the powers and responsibilities that are not currently conducted by other departments. Thus most of the registration and compliance monitoring would be carried out by the Companies Registry, which already has those functions in respect of other companies, with the Commission dealing with investigations and disciplinary matters. The Commission would therefore be the appropriate body to handle the grievances in the first instance in respect of any refusal to register a Charity by the Companies Registry, with the right of further appeal to the Court of First Instance thereafter and in respect of the exercise of the Commission's powers.

Q37: Do you think that appeals relating to applications for fundraising permits and licences should be handled by the Administrative Appeals Board or by a new administrative appeal system set up for the purpose?

27. In the interests of saving administrative costs and avoiding confusion, we suggest that the appeals should be handled by the Administrative Appeals Board.

Signed on behalf of ICAEW

Robin Fieth

Executive Director, Finance and Operations

October 2011

Robert Hodgkinson

Executive Director, Technical Strategy

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