

## Large Legacies & Donations

### Some notes on wider issues (eg: grant applications)

**These notes are NOT intended to be part of the formal policy document but are provided for guidance only.**

This model policy is dedicated to Dr Seuss's "The Lorax" and is a caution to charities – and funders – who inadvertently (or, worse, knowingly) squander gratuitous resources, such as large legacies, by prioritising short-term policies without appropriate consideration of the potentially detrimental consequences for long-term sustainability.



Unlike large charities for which legacies are a significant regular part of their income and are sufficient to justify having a "legacy management team", for small charities which receive occasional "out of the blue" large legacies, they can be very much a mixed blessing.

One can, of course, understand the position of funders - themselves now under severe pressure of demand for their grants - charities which have been "blessed" with a large legacy are an "easy option" for them to decline, however much they might otherwise be supportive of what the charity is asking funds for.

The solution is, therefore, not easy and small charities should (for their own well-being and long-term peace of mind) try to "look on the positive side" not become unduly disappointed when their applications are rejected in favour of other small charities who have not been "blessed" with a large legacy.

However, there are two things which can be tried to side-step the risk of being rejected on the basis of "you've already got loads of money, so why should we give you any more!".

It is well established in the commercial world that one of the biggest risks of a small business failing is over-rapid expansion (usually unplanned and therefore poorly controlled) due to an unexpected "favourable wind" creating a surge in demand for its services/products. The business takes on more staff and invests in more accommodation/equipment/resources to cope with the surge in demand, and profits boom for a bit. Then equally suddenly and unexpectedly, fashions change, demand falls dramatically and the business finds itself lumbered with staff and resources that it can't sustain. Any profits quickly get consumed by debt and, in the worst scenario, the business goes bankrupt leaving its staff unemployed and its creditors unpaid.

The effect of unexpected "one-off" legacies on small charities can have a similar effect. Buoyed up by the windfall, the charity takes on ambitious projects way beyond its usual resources - perhaps in the hope/expectation that the projects will succeed and so will attract additional funding. But in a fickle world such hopes/expectations are not always realised. So, when the legacy money runs out and the charity is unable to find other resources to sustain it, the project crumbles to a halt - staff/volunteers may have to be put off, and if the charity has run up unsustainable commitments it may have to close completely. And, in the



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worst case, the trustees could even be held liable for some of the charity's debts if they were found to have acted "recklessly or negligently". And, of course, whatever the ultimate outcome, it's the charity's beneficiaries who are at the front of the queue to be disappointed and let down if the charity's services on which they had come to expect/rely are suddenly withdrawn.

Such a "boom and bust" approach is not helped by the Charity Commission general guidance that "charitable donations should be spent on the charity's charitable purposes" - *ie*: should not just be left "gathering dust" (not much interest around these days !) on the grounds that "it might come in useful one day". However, the Commission has, at least, recognised that prudent planning for future expenditure IS a good thing, hence the facility to designate - *ie*: put aside - money for specifically identified future purposes. However, such designated funds MUST be identified in the charity's Financial Review in its Annual Report and Financial Statements. Designated funds should have: (a) a specific identified purpose; (b) the amount of funds required to deliver that purpose (*ie*: the amount being designated - which can be build up over several years if necessary); (c) the date by which the designated funds are expected to be spent.

The Pathhead and District Community Association's "Large Legacies & Donations Policy" is designed to address this issue. It specifically addresses the need to avoid "boom and bust" scenarios by the charity having a policy of putting unexpected large legacies/donations aside into a designated fund specifically intended to allow the "windfall" to be trickled back into the charity's general fund in a way which promotes, rather than undermines, sustainability. Note here that designated funds are NOT restricted funds and so may still reject applications on the grounds that funds identified as "designated" can be converted back into general funds for running costs at any time by the trustees. But what is important about having the policy is that it demonstrates to potential funders that the trustees have recognised and understand the risks, as well as the benefits, associated with large windfall amounts and have a properly considered strategic plan for dealing with them. The charity simply having "put to the money to one side while it decides what to do with it" - rather than it being presented as prudent financial management within a clear overall financial strategy - will NOT be sufficient to satisfy funders.

Which takes us on to the second thing that charities can do to try to avoid grant applications being rejected because of existing "windfall" funds.

Another common reason for grant applications being rejected is because the charity is unable to demonstrate how the project for which the grant is being sought can be continued sustainably once the initial grant has come to an end. *ie*: grant-givers are unwilling to pour money into a project (particularly if a significant part of the grant will be covering start-up costs) if that money will only be wasted by the project closing down again once the grant comes to an end. Windfall funds provide a splendid way of demonstrating long-term sustainability when applying for fixed term project grants. It's the old trick of re-presenting a "vice" (in this case, money sitting unused) into a "virtue" (money to take over sustainability of a project when the initial grant comes to an end). Specifically: the charity designates some (or, perhaps, all) of its windfall legacy money as a designated fund specifically (a) to maintain the project for a further x years once the initial grant comes to an end; (b) the amount thus designated is £y - the estimated costs of continuing to run the project for x years; (c) the use of the designated funds to come into effect when the initial grant expires in 20zz. Of course, that doesn't (and can't) make the designated fund a restricted fund (though the grant donor may make its grant restricted by the condition that the charity does all in its reasonable power to keep its designated fund for the mutually agreed purpose). But, once again, the important explicit message to the funder is that the charity is worth



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giving grants to because it has a carefully considered and robust financial management strategy which protects both the funder's interests (getting the best return for its grant), the charity's interests and MOST IMPORTANTLY OF ALL, the charity's beneficiaries' interests by making the best possible provisions for long-term sustainability.

That approach does, of course, need to be backed up by a credible Business Plan - for which Small Charity Support's guidance on business planning (<http://www.smallcharity.support/BusPlan.html>) may also be useful.

## Large Legacies & Donations

### Preamble

Like many small charities, the Pathhead and District Community Association (the PDCA) occasionally receives large legacies and donations unexpectedly.

Where such legacies/donations are large (eg: greater than 20%) in relation to the charity's typical or budgeted annual income they can have a very distorting influence on the charity's financial situation. In particular, if such legacies/donations significantly increase the charity's reserves and are therefore to be disbursed as soon as is reasonably practical thereafter, they can create "feast and famine" situations. This can distort the charity's priorities for meeting its charitable objects and might lead to The Charity taking on commitments which are not sustainable once the legacy funds have been exhausted.

In order to avoid such distortions The Charity has adopted a Large Legacies & Donations Policy which is intended to ensure a more controlled and evenly distributed disbursement of the legacies that it receives.

### Definitions

Within this policy the use of the terms Designated Funds, Restricted Funds and Reserves have the following meanings as defined in the Charity Commission's Glossary of Terms <http://ogs.charitycommission.gov.uk/glossary.aspx>

#### Designated funds

"Unrestricted funds are expendable at the discretion of the trustees in furtherance of the charity's objects. If part of an unrestricted fund is earmarked for a particular project it may be designated as a separate fund, but the designation has an administrative purpose only, and does not legally restrict the trustees' discretion to apply the fund."

#### Restricted funds

"Restricted funds are funds subject to specific trusts which may be declared by the donor(s), or with their authority (eg, in a public appeal), but still within the objects of the charity. Restricted funds may be restricted income funds, which are expendable at the discretion of the trustees in furtherance of some particular aspect(s) of the objects of the charity, or they may be capital funds, where the assets are required to be invested, or retained for actual use, rather than expended."

#### Reserves

"The term '**reserves**' has a variety of technical and ordinary meanings, depending on the context in which it is used. In our guidance we use the definition established by the charities (Accounts and Reports) Regulations 2008 and we use the term 'reserves'



(unless otherwise indicated) to describe that part of a charity's income funds that is freely available for its general purposes. 'Reserves' are therefore the resources the charity has, or can make, available to spend, for all or any of the charity's purposes, once it has met its commitments and covered its planned expenditure. See [OG 43 B1](#).

More specifically this defines reserves as income which becomes available to the charity and is to be spent at the trustees' discretion in furtherance of any of the charity's objects (sometimes referred to as 'general purpose' income); but which is not yet spent, committed or designated (ie: is 'free').

Attention is also drawn to the Charity Commission's publication CC19, Charities and Reserves

<https://www.gov.uk/government/publications/charities-and-reserves-cc19>

### Restricted Legacies/Donations

Restricted legacies/donations are restricted funds and are received and disbursed in accordance with the terms of the trust under which they were donated.

As with any restricted legacy/donation offered to The Charity, the Trustees will decline to accept large restricted legacies/donations which, in their view:

- Are inconsistent with the charitable objects of The Charity;
- Would inappropriately distort The Charity's charitable priorities and/or its operational ethos;
- Would require the allocation of additional resources (eg: human, physical, financial) which The Charity does not have, or would be to the detriment of its other charitable activities, either immediately or once the legacy has been exhausted.

### Unrestricted Legacies/Donations

Unrestricted legacies/donations are funds donated to The Charity for general use at the discretion of the Trustees to further its charitable objects.

The Trustees of The Charity have resolved to create a specific Legacies Designated Fund the purpose of which is to enable the Trustees to manage large legacies/donations to The Charity in an efficient and effective manner to best promote The Charity's objects and the Public Benefit. This policy provides for the steady and controlled release of such funds into the charity's reserves in order to avoid the financial distortions and instabilities which can be created by the irregular and unexpected receipt of significant legacies/donations to the charity .

As with any designated fund, having due regard for the needs and best interests of The Charity the Trustees may, at any time, resolve to manage the Legacy Designated Fund on an interim basis in a manner other than as described in this policy. This might include, for example, the need to manage a short-term cash-flow problem or to fund a specific project or acquisition that would not be affordable under The Charity's regular income.

**Note:** As the charity's Legacies Designated Funds are committed/designated for release back into the general fund at a specific time in the future for the specific purpose of stabilising the charity's cash-flow they are not considered to be part of the charity's reserves.

The Charity's Threshold for the transfer of funds between its General and Legacies Designated Fund shall be £5000 or as agreed by the Trustees. Options for how this is done will be agreed by the trustees on a case by case basis.



### **Options Transfers to the Legacies Designated Fund**

There are two options for transferring large legacies/donations to the Legacies Designated Fund:

**Option 1: Individual Threshold** – whether legacies/donations are transferred to the Legacies Designated Fund is determined by whether or not each individual legacy/donation exceeds the Threshold;

Individual Legacies/Donations which are below the Threshold are added to the General Fund at the time that they are received.

Where the amount of an individual legacy/donation exceeds the Threshold the Threshold portion is added to the General Fund at the time that the Legacy/donation is received and the excess over the Threshold is transferred to charity's Legacies Designated Fund.

**Option 2: Aggregate Threshold** – the amount transferred to the Legacies Designated Fund is the amount by which the aggregate of ALL legacies & donations received within the year exceed the Threshold.

Legacies/Donations up to the Threshold in aggregate received in any financial year are added to the General Fund at the time that they are received.

Any excess over the Threshold of the aggregate of legacies/donations received in any financial year is transferred to charity's Legacies Designated Fund at the time that the excess legacies are received.

### **Transfers From the Legacies Designated Fund**

There are two options for transferring monies from the Legacies Designated Fund back into the General Fund:

**Option 1: Fixed rate transfer** – a fixed amount, based on the value of each legacy, is transferred each year back to the General Fund until all of the original legacies have been thus transferred;

On the first day of each of the {4} financial years following a financial year in which an excess over The Threshold of legacies is received {1/4} of the excess of legacies received in that Financial Year will be transferred from the Legacies Designated Fund back into the General Fund of The Charity.

For the avoidance of doubt, the amount transferred each year is cumulative.

**For example:** If the Threshold is £5,000; in year-1 the excess of legacies is £4,000; in year-2 it is £20,000, and no further legacies are received thereafter:

- In year-1 the General Fund will receive just the £5,000 Threshold from the legacies received in that year;
- In year-2 the General Fund will receive the £5,000 Threshold from the legacies received in that year PLUS the amount transferred from the Legacies Designated Fund of  $\frac{£4,000}{4} = £1,000$
- In year-3 The Charity receives no additional legacies, so the General Fund receives just the  $\frac{£4,000}{4} + \frac{£20,000}{4} = £6,000$  transferred from the Legacies Designated Fund



- .....etc.

**Option 2: Proportional transfer** – the amount transferred is a percentage of the amount remaining in the Legacies Discretionary Fund, or the transfer threshold (as above), whichever is greater, is transferred back to the General Fund until the Legacy Discretionary Fund is empty.

On the first day of each financial year  $\{1/4\}$  of the amount held in the Legacies Designated Fund, or the Threshold, if greater, will be transferred from the Legacies Designated Fund back into the General Fund of The Charity until the Legacies Designated Fund is empty.

**For example:** If the Threshold is £5,000; in year-1 the excess of legacies is £4,000; in year-2 it is £20,000, and no further legacies are received thereafter:

- In year-1 the General Fund will receive just the £5,000 Threshold from the legacies received in that year;
- in year-2 the General fund will receive the £5,000 Threshold from the legacies received in that year PLUS the amount transferred from the Legacies Designated Fund of  $\frac{£4,000}{4} = £1,000$ , leaving a residue of £3,000 to which is added the £20,000 in excess legacies for that year;
- In year-3 The Charity receives no additional legacies, so the General Fund receives just the  $\frac{£23,000}{4} = £5,750$  transferred from the Legacies Designated Fund leaving a residue of £17,250;
- In year-4  $\frac{£17,250}{4}$  is less than the Threshold and so £5,000 will be transferred from the Legacies Designated Fund instead, leaving a residue of £12,250.
- Similarly, in years 5 & 6 £5,000 will be transferred from the Legacies Designated Fund leaving a final residue of £2,250
- In year-7 the remaining £2,250 is transferred leaving the Legacies Designated Fund empty.

## Change Record

Date	Change / Approved by	Comments
16/12/20	NHD	Formatting & clarification that options to transfer funds between accounts will be agreed on a case by case basis by the Trustees.
10/12/20	Committee	Policy approved by the Trustees
30/11/20	Trustees, BC	Policy approved by the Treasurer and The Trustees
27.11.19	MJ sec	Final version
18.11.19	MJ,NHD	Draft written and discussed