



Briefing

Housing Associations - August 2010

Cuts in the Social Housing Grant – impact on charitable activities of RSLs

The recent announcement by the UK Coalition Government in relation to cuts in public spending is likely to have an impact on the award of Social Housing Grants by the Welsh Assembly Government (“WAG”). This may leave many charitable RSLs wondering how it will be able to fund future development work in accordance with its objects.

Many RSLs are considering different means of funding development work.

One option may be to develop schemes where a proportion (if not all) of dwellings are allocated to be sold on the open market. With the aim of making a profit, this profit would be used to further the RSL’s charitable objects.

RSLs and Model Rules

Many RSLs in Wales are charitable and governed by the Model Rules. The Model Rules (version 2005) permit RSLs to:

carry on for the benefit of the community:

- the business of providing housing, accommodation, and assistance to help house people and associated facilities and amenities for poor people or for the relief of aged, disabled, handicapped (whether physically or mentally) or chronically sick people.
- any other charitable object that can be carried out by an Industrial and Provident Society registered as a social landlord.

Being a charity, all activities undertaken by the RSL must be exclusively charitable. There are limited exemptions to this.

An RSL may undertake activities which are not charitable if they are either:

- insignificant (falling under the *de minimus* principle); or
- reasonably incidental to the charitable objects. For example, a small amount of non-charitable activity might be permissible on the grounds that it would hamper the RSL’s charitable activity if there was not a margin of tolerance.

The difficulty with relying on the narrow exemptions is that each activity will have to be considered on its own merits either by assessing whether the activity is charitable (by relying on the extended scope of ‘charitable purpose’ pursuant to the Charities Act 2006) or whether the activity is ‘reasonably incidental’. This therefore is potentially a time intensive exercise for the management and the board and one which may also be expensive if the board needs to seek legal advice each time.

Since an RSL will not be able to seek ‘clearance’ from WAG, board members will need to be confident in their assessment (or the assessment of their lawyers!) or run the risk of acting in breach of the rules.

Is the RSL ‘Trading’

One of the key features of RSLs is that they are not permitted to trade for profit. The Model Rules specifically state in Rule A 3 that an Association “shall not trade for profit”. This rule further limits the ‘reasonably incidental’ exemption if the sole purpose of the non-charitable activity is to make a profit.

What amounts to ‘trading’ depends on a number of factors including the nature of the ‘goods’ being sold and the presence or absence of a profit motive.

The sale of a significant number of dwellings on the open market for the sole purpose of raising funds is likely to amount to 'trading for a profit' and therefore not permitted.

What risks are involved?

Even where only a small element of a scheme is non-charitable and the profit of the sale of such dwellings is intended to be ploughed back to further the RSL's objects the activity could involve a significant risk.

For example, if the turnover is insufficient to meet the cost of carrying on the trade and the difference has to be met by the assets of the RSL. In these circumstances board members will be at risk of acting ultra vires and being personally liable to meet any shortfall.

Given the current economic climate the risk involved is arguably even greater.

Is there a solution?

Clearly there is a need for RSLs to consider how they will raise funds for future developments.

To ensure that RSLs can lawfully undertake this type of profit making activity, one option may be to set up a trading subsidiary company. This company must be set up in such a way so as to:

- protect the parent RSL and its assets from the risk involved in the trading.
- be consistent with the Welsh Assembly Government's publication RSL 05/08 Group Structures which states, amongst other things, that:
 - financial and contractual arrangements between an RSL and an unregistered subsidiary must be at arm's length; and
 - any loans or investments made must be on a commercial, secured basis.
- ensure that the subsidiary is able to covenant any trading profits to the parent RSL.

There are tax implications on setting up a trading subsidiary company and RSLs should ensure that they seek professional advice at the outset in respect of this. We also recommend that RSLs discuss this with the Welsh Assembly Government.

More information

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