George Osborne MP
Chancellor of the Exchequer
HM Treasury
1 Horse Guards Road
London SW1A 2HQ

12 July 2012

Dear Chancellor,

We welcome Government reforms to enhance financial stability and integrity in the UK banking system. However, we are concerned with the proposed changes to creditor hierarchy as outlined in the banking reform white paper, and the impact these will have on the charity sector.

A significant number of charities will be put at financial disadvantage under the new depositor preference arrangements. We are asking you to grant UK registered charities *preferred creditor* status so that they rank 'pari passu' with the Financial Services Compensation Scheme (FSCS) in the event of bank or building society failing.

Under the new proposals, in which FSCS liabilities are given priority, the chances of a charity losing a substantial proportion or all of its deposits in the event of a bank or building society failing is greatly increased. As charities tend to hold large deposits for longer periods than other sectors (to allow for the time lapse between fundraising and project commencement or to ensure commitments can be met regardless of income fluctuations, amongst other reasons), this means in the exceptional event of a bank failing, charities would lose substantial sums of donor money relative to their size.

However, the real and long-term impact of this policy change goes well beyond the exceptional event of bank failure. In order to mitigate this increased level of risk, as is only prudent for a charity, they will need to adopt more conservative banking arrangements and deposit in those banks deemed 'lower risk', which typically pay a much lower deposit rate. Charities sensibly adapting in response to the changes will therefore face immediate financial loss. Charity Commission returns show that the sector holds £18bn in cash deposits. If charities adjust their banking arrangements to accommodate the additional risk then in theory the sector could lose millions per year from lower returns.

Data from NCVO's Almanac, which provides information and statistics on the UK charity sector using evidence from a range of government and industry sources, suggests a substantial number of charities will be affected: These include the 2900+ charities ineligible for FSCS compensation, as well as many eligible charities holding more than £85,000 (the compensation limit) in cash deposits.

The proposed hierarchy positions charities alongside big businesses, something we firmly disagree with in this circumstance. Charities would need to invest in additional expertise or upskill in order to manage these greatly increased exposures and it would be almost impossible to maintain the same level of knowledge as big business and the financial sector. Consequently it is likely that charities would be the last to hear of problems and therefore the worst affected as other depositors exit a risky bank.

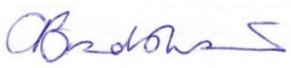
Granting charities preferred creditor status will help Government in achieving its wider policy objective of allowing banks to fail in a way which minimises both cost to and impact on the taxpayer. Charity deposits are funds that have been donated by the public or other funders, which are effectively in trust or transit for the ultimate benefit of beneficiaries. It is the beneficiaries – often the most vulnerable in society– that will be negatively affected, undermining the Government's objective of minimising taxpayer impact.

Many charities lost money as a result of the Icelandic banking crisis and so it is extremely promising that progress is being made in this area. It is important, however, that measures intended to protect individuals do not unfairly and ineffectively work to the detriment of charities and their beneficiaries. If a consequence of these actions is to crystallise a loss for highly valued charities then the proposals undermine the white paper's stated aim of ensuring that the cost of bank failures are borne by those able to understand the risk and who can absorb loss best.

We believe that conferring charities with *preferred creditor* status is a simple and positive change that the Government can make - without additional risk or expense to the Exchequer, but one that would make a tangible financial difference to many charities.

We are working with the sector to develop a more detailed submission and estimate of losses, however are keen to flag our concerns at this juncture. We would welcome the opportunity to meet with you to discuss the issue further. To arrange a meeting or discuss further, please contact Melora Jezierska, CFG policy and public affairs officer, at melora.jezierska@cfg.org.uk or 020 7250 8348.

Yours sincerely,



Caron Bradshaw
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cc. Nick Hurd MP, Minister for Civil Society
Mark Hoban MP, Financial Secretary to the Treasury
Rt Hon Dr Vince Cable MP, Secretary of State for Business, Innovation and Skills