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Charity regulation in the British Isles

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Sustaining public confidence in Charity

The British approach since the 1990s: a graduated regulatory regime slowly evolving from State-regulated to self-regulated public accountability, *in the public interest*, for the ‘proper administration’ of charitable resources derived from public or private funds granted/donated for the public benefit

Development of the UK charity sector

- *'Care in the Community'* - from State to private action
- Consumer-demands: *Quality Standards; Kitemarking*
- Social expectations: *equality; inclusion; transparency*
- Regulated *charity accountability* to the general public
- *Summary Information Returns* for the public domain
- Free public-access website database: ***Guidestar***
- Government focus on 'charity effectiveness' – ***CC10***
- ***Self-regulation*** – the Fundraising Standards Board
- *'Public Benefit' testing* under the Charities Act 2006
- *Where next: pan-European / global accountability?*



Dimensions of the UK charity sector

England & Wales (for Scotland, add 20%, say):-

- 168,350 registered 'reporting' charities at 31 Dec. 2008
- £Bn48 gross annual income (in aggregate)*
- £Bn43 (90%) audited in 9,000 charities > £k500 income
- + ca. 100,000 'exempt'/'excepted' charities
- a million trustees; half-million paid charity employees
- Many millions of volunteer charity workers/supporters
- Government - Voluntary Sector 'partnership'
- **Public Confidence** is the 'driver' for regulation

(*said to be approx. 4% of UK GDP)

Profile of the *Register of Charities* (E&W)

Website: 31 Dec. 2008

Income band:	Gross Income		Total Nos		Companies (estd.)	
	£Bns	%/tot.	000's	%/tot.	No.	%
Over £5m	31.6	65.3%	1.6	0.9%	1k	70%
£500k+ -> £5m	11.2	23.2%	7.5	4.5%	5k	70%
Charities over £500k	£Bn43	89%	9k	5%		
£100k+ -> £500k	3.6	7.5%	16.1	9.6%	8k	50%
Charities over £100k	£Bn46	96%	25k	15%		
£10k+ -> £100k	1.7	3.5%	48.8	29.0%	5k	10%
£0 -> £10k	0.3	0.5%	79.8	47.4%	4k	5%
Unknown income*			14.5	8.6%		
Totals	48.4	100%	168.3	100%	23k	13%

*non-responders, assumed no income or no trustees

The Sector's 'rival' database (*Guidestar*)

- Launched December 2005 as a free public facility
- Receives basic data-feed from the Charity Regulator
- Charities can use “*Update My Charity*” to upload their own data, making their own* free website there
- Was funded by HM Treasury (£3m) as a regd. charity
- Grant-funding secure but slow take-up by ‘major users’
- Offers subscription-based services for due diligence
- Huge potential for inter-charity ratio-comparisons, etc.

*(*10,000 small registered E&W charities already use this free facility)*

Charity size-bands for State regulation

Charities > £5k gross income: **registration** (unless exempted/excepted)

- All charities must meet the '**Public Benefit test**' from April 2008
- Registered charities > £25k gross income: **Annual Return, Annual Report and Accounts** must be filed with the Regulator within 10 months
- Accounts must be '**true and fair**' in compliance with standards/SORP, but non-company charities < £250k gross income can opt for 'cash-basis'
- **Audit** threshold: £500k gross income (or £250k if gross assets > £3.26m)
- Smaller charities: **Independent Examination** option if > £25k gross income (Charitable companies > £6.5m turnover &c: Companies Act audit)
- Charity groups > £500k gross income: **consolidated accounts** obligatory
- Charities > £1m gross income: simplified **Summary Information Return**

External Scrutiny reporting (E&W)

Whistle-blowing to the Regulator if charity or beneficiaries put ‘at risk’:-

Reporting by auditors (larger charities)

- Top 11,000 charities = 90% of aggregate gross income on the Register
- Regulatory implications if report contains a “qualified” audit opinion

Reporting by independent examiners (smaller charities)

- the statutory alternative to a professional audit if < £500k gross income
- only for charities > £25k gross income (total exemption below that)
- Examiner must be an eligible[#] individual not ‘connected’ with trustees
- “negative assurance” provided by the Independent Examiner’s Report

[#]someone the trustees consider has the required knowledge and experience –
BUT: Examiner must also be suitably qualified, if charity’s gross income > £250k

Charity Auditors &c - **‘whistle-blowing’**

“Whistle-blowing” duty to the Regulator by charity auditors and independent examiners:

- Applies to all (non-exempt) charities > £25,000 gross income
- Loss of the audit: any “circumstances” must be notified
- PN11*: Trustees’ *own* notifications to Regulator do not relieve the charity auditor’s duty to report in writing any:
 - wilful misleading of the Regulator (includes Annual Returns)
 - breach of the Charity Fundraising Regulations
 - breach of any Regulatory Order or Consent requirements
 - failure to register the reporting charity (a rarity)

*“The Audit of Charities” – issued Dec.2008 by the Auditing Practices Board (a government agency under the Financial Reporting Council)

Annual Returns to the Regulator (E&W)

- Part A: **Register-updating** data for all charities
- Part B: **(confidential)** charities with gross income:
 - > £25k: the “Serious Incident Reporting” regime
 - > £500k: box-numbered summary of SoFA/BS
- Part C: **Public Domain data** – if income > £1m:
“Summary Information Return” (certified)

Possible 'high-risk' situations: the Regulator's 'Serious Incident Reporting' regime (E&W)

Annual Return, Part B: charities > £25k gross income:-

1. Fraud/theft/loss of funds > £25k (or 20% of total funds, if less)
2. Major gifts where source unknown/verified (cf: AMLR2007)
3. Known/alleged links between charity/trustees/staff and proscribed organisations
4. A 'disqualified trustee' on Board (now or previously)
5. No policy in place (cf: CRB checks) for safeguarding any 'vulnerable groups' among beneficiaries
6. No vetting procedure in place (self-certification?) for trustee/staff eligibility when appointed
7. Beneficiary-abuse/mistreatment (actual or suspected)
8. Criminal (police) investigation or Regulator/Agency investigation; or the latter's imposition of sanctions or raising of concerns

Checklist for **‘Serious Incident Reporting’**

- Is this an actual or alleged/suspected ‘incident’?
- Name and post of any charity personnel involved?
- Is that person still with the charity – or what?
- Impact of this incident on the charity/beneficiaries?
- Action taken since the incident occurred?
- Any publicity generated by the incident – or likely?
- Outcome of any internal inquiry held by the charity?
- Action/stance taken by any other relevant authorities?
- Awareness of any relevant statutory obligations (eg, CRB)

*Annual Returns to the Regulator, Part C: the **Summary Information Return** ('SIR')*

Cabinet Office Strategy Unit (2002 Report):

“... the largest charities (those over the £1 million threshold) should complete an annual Standard Information Return (“SIR”). This should highlight key qualitative and quantitative information about the charity, focusing on how it sets objectives and measures its outcomes against these.”

The SIR's governance-related questions

Q.2: How can beneficiaries influence the charity's development?

- Immediate vs Ultimate beneficiaries? And how accessible are they?
- What opportunities do the trustees provide? How do they "listen out"?

Q.6: What is the charity's "financial health" at the year-end? - eg:

- Are all Funds deployed in the right assets to do the job?
- Are next year's planned activities covered by reliable funding?
- How do existing reserves compare with any future funding needs?

Q.8: Effectiveness of governance – eg, your policy/procedures for:

- *Trustee-selection*, -competence, *-training*;
- *Delegation* of management tasks (authority limits; feedback-reporting);
- Internal control systems and risk-management;
- Conflicts of loyalties or of personal interests, etc.

Disclosure required in the Annual Report & Accounts

The SIR's 'performance' questions

Q.1: **The charity's 'aims'** (Strategic Plan; Mission Statement)

Q.3: **The strategy** (medium/long-term) and its **"success-indicators"**

Q.4: **The year's objectives and achievements**

Q.7: **Next year's main objectives**; **How the medium- to long-term strategy will be affected by last year's results**

Disclosure required in the Annual Report & Accounts

- Which 'key performance indicators' (KPI's) are safe to publish year-on-year?
- Does the internal management reporting system monitor those KPI's in-year?
- When to reset the published objectives for next year - halfway-through?

The SIR's 'league-tabling' Question 5

- **Income analysis by type;**
- **Expenditure on 'the most significant' activities;**
- **Fundraising Costs & Income**

(in each case: 3 main categories + all other)

These are also, in the main, Annual Report & Accounts disclosures

- **Issues arising:** Relationship/Consistency of all this with Q.4?
- Is use of resources proportionate to reported achievements?
- Early warning from the internal management reporting system?
- Peer-group comparisons – to pre-empt the league-tablers?

The Regulator's Code of Practice for charities: Charity Commission website leaflet **CC10**

‘Hallmarks’ of an effective charity :

- I. Clarity of purpose and of how to provide public benefit**
- II. A competent, caring, informed, *non-conflicted* Board**
- III. Structure, policies, procedures all ‘fit for purpose’**
- IV. Learning and improving through the processes of performance-assessment/planning & quality control**
- V. Financially sound and prudent management of its resources for optimal use to achieve its purpose**
- VI. Open-handed in accounting to the public/stakeholders**

Impact of the EU's 'NPO Code of Conduct'

'Framework recommendation', issued Nov. 2005:-

- **“Member States should ensure they have oversight of their non-profit sector. The oversight role could either be dedicated to a single public body or entrusted to existing authorities or to self-regulatory bodies” ...**
- **“Member States should encourage NPOs to apply enhanced transparency and accountability measures in their daily management in order to reduce the scope of their [possible] misuse for criminal purposes.”**

NPO Code of Conduct: *key requirements*

- ‘Simplified financial reporting’ by smaller NPOs
- **Lists of [all] bank account numbers for each registered NPO and any detailed personal data to be kept confidentially on the Register and at the NPO’s office**
- **Compliance ... to be promoted through certification or a “seal of approval” from a public or private body ... (cf CC; FSA; HEFCE; IoF/FrSB; NCVO; ACEVO? &c)**
- **Privileged tax status, the award of public grants and the right to public fundraising *could be dependent on registration and continued compliance with the Code***
- **Q: What where is the Code of Public Accountability?**

Updating/fine-tuning the British regime – the Charities Act 2006, Part 2: regulation

Ch.1 & Sch.1/2 The Charity Commission's status, aims, functions, &c

Ch.2 & Sch.3/4 The Charity Tribunal (as Court of First Appeal)

Ch.3 Registration of charities & **Sch.5:** regulation of exempt charities

Ch.4 Charity Variation Schemes (widening of the *cy prè*s doctrine)

Ch.5 The Commission's enforcement & advisory powers

Ch.6/7 & Sch.6 Audit/IE; Group Accounts; "Whistle-blowing" to the CC

Ch.8 & Sch.7 The CIO (Charitable Incorporated Organisation)

Ch.9 Trustee-remuneration; Relief from liability for breach of trust

Ch.10 Trustees' statutory powers of *cy prè*s trust-variation

Ch.11 Expending of permanent endowment; Charity Mergers Register

The Charitable Incorporated Organisation (CIO) ***– a new legal vehicle to ‘Europeanise’ the UK Sector?***

- **Corporate form of charitable ‘trust’ with limited liability**
- **Trustees & Members (min=1) can be identical or different**
- **Quick and easy conversion from other legal forms of charity**
- **Optional alternative to charitable company status - BUT**
 - **Company option under threat? (cf: CIC as ‘next best thing’)**
- **Trustees’ ‘duty of care’ to be explicit in the CIO Regulations**
- **Charity Commission = registrar and sole regulator of a CIO**
- **Will use model constitutions to suit different needs of Sector**
- **Good for EC harmonisation but less latitude than a company**

Scope/Status of the **‘Charities SORP’**

- A *‘highway code’* of generally accepted best practice as the “default” SORP for charities throughout the UK (but: SORP 2005 excludes Eire)
- Applies to all charities not covered by a more specialised SORP (e.g., Universities and Higher/Further Education Colleges, Social Housing)
- In Scotland, charitable companies must comply with the SORP for a “true and fair view”; in E&W they only need to comply with the SORP
- Compliance is statutory in Britain under Charities Act regulations for *non-company charities’ accruals-based Accounts*
- Effective enforcement of the SORP by the Regulator largely hangs on the FRC’s independent regulatory regime for all professional audits

Charities' *Annual Reports* under SORP 2005

- **Reference and Administrative data for the charity**
- **Structure, Governance and Management**
- **Public Benefit purpose/aims, Objectives and Activities**
- **Achievements/Performance against any targets set**
- **Financial Review and Results for the Year**
- **Future Plans**

Seen as the context for a proper understanding of the accounts!

The **Statement of Financial Activities (SoFA)** to demonstrate charity law compliance

- Charity law requires a full account of all resources:
 - Incoming resources for the year (income *and capital*)
 - Expenditure for the year (i.e., resources consumed)
 - All other funds-movements (transfers; gains/losses)
- Segregation of movements on all 'restricted' funds:
 - Endowment capital (permanent and expendable)
 - restricted income funds
- Reconciliation of opening and closing Funds balances between the two year-ends = complete accountability!

Charity *Balance Sheets* under the SORP

Assets & Liabilities: as for commercial organisations

Funds summarised under charity law categories*

- Provision for Liabilities versus Designated Funds
- Endowed and other 'Restricted' Funds and their assets/liabilities
- Movements on major individual Funds
- Explanation of Funds (nature/purpose)

*Charities have no 'owners' – only administrators, for public benefit

What makes the SORP “statutory”?

E&W: The Charities (Accounts & Reports) Regulations

- S.I.2005/572 - until replaced by S.I.2008/629 for all financial years starting after March 2008 (or upon earlier voluntary adoption)
- **Entity/Group accounts (*non-company* charities) & consolidated accounts for small company groups:** must comply with the SORP 2005 “methods & principles” (plus specified Accounts Notes)
- **Companies otherwise:** Regs cover the Trustees’ Report only

Scotland: the Charities Accounts (Scotland) Regulations 2006

- Under S.S.I.2006/218 all annual accounts and reports for years from 1 April 2006 must comply with SORP 2005 (or HEI/FEI / RSL SORP per Reg.14), but for non-company charities < £100k gross income: if opting for Receipts & Payments accounting:
 - the R&P Account & Statement of Balances must comply with Sch.1;
 - the Annual Report must provide the information required by Sch.2
- Charitable companies must have a Scottish audit even if already audited; all charities: either an audit or an independent examination



Charity Fundraising – still an unsolved problem for the Charities SORP...

- Inter-departmental liaison/reconciliation:
 - Donor-promises vs SoFA-recognition
- Transparency in performance-reporting:
 - Current fundraising performance vs Investing in the future (e.g., legacy-marketing)
- Sector research: average cost/proceeds ratios
 - Regulator's 'concerns' where ratio > 40%
- Life-cycle reporting for major projects?

The big issue for Charity Accountability?

IAS/IFRS v. IPSAS as the pace of 'globalisation' quickens

- No IAS/IFRS option for **charitable companies**: UK standards must apply, as national SORPs have “no standing” with IASB
- Yet “IPSAS” / IPSFRS offer an *unrecognised* solution here:
- IFAC, the global umbrella body for standard-setters, derived its IPSAS/IPSFRS as *IAS adaptations* suitable for adoption by all ‘public sector bodies’ but has ‘no funding’ to deal with issues that are special to the ‘*private*’ not-for-profit sector
- Yet the Charities SORP and IPSAS do fit ‘hand-in-glove’ ...
- Meanwhile the ASB’s grand design “*Proposed Interpretation of the ‘Statement of Principles’ for Public Sector Bodies*” aims to converge and unify profit-accounting with gift-accounting, while the IASB/FASB aim to tack the latter onto the former! -

