

# Charities Back on Track

Themes and lessons from the Charity Commission's investigations and regulatory casework

2011-12



## The Charity Commission

The Charity Commission is the independent regulator of charities in England and Wales. Its aim is to provide the best possible regulation of charities in England and Wales in order to increase charities' effectiveness and public confidence and trust. Most charities must register with the Commission, although some special types of charity do not have to register. There are over 160,000 registered charities in England and Wales. In Scotland the framework is different, and the Commission does not regulate Scottish charities.

The Commission provides a wide range of advice and guidance to charities and their trustees, and can often help with problems. Registered charities with an annual income over £10,000 must provide annual information to the Commission. The Commission has wide powers to intervene in the affairs of a charity where things have gone wrong.

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## A. Introduction

The charities on our online Register are incredibly diverse. But they all have one important thing in common. They are all managed, ultimately, by their trustees. Most of the 945,000 trustees in England and Wales are volunteers, who take their roles seriously and dedicate time and effort to ensuring their charities are well-governed and make the biggest possible difference to their cause. From time to time, trustees make mistakes but, on the whole, they know how to prevent small problems becoming serious concerns, whether by consulting our online guidance or seeking support from their umbrella bodies or from professional advisers.

But occasionally, charities experience problems serious enough to require our involvement. This often happens when trustees do not fully understand their legal duties and responsibilities, or when they renege on those duties. Our casework also shows that many trustees are not aware of the steps they can take to prevent a small mistake or problem escalating and putting the charity's money, property, its beneficiaries, or its reputation at risk.

This report provides an overview of the types of concerns that have prompted our involvement in charities over the past year and explains how we have helped resolve the problems.

The reason we publish this report is not to 'name and shame' charities that have experienced difficulties. Our aim is to provide a resource for trustees that allows them to learn from the mistakes others have made, and to avoid leading their own charities into similar difficulties. As in previous years, we have focused on real examples from our case work. We expect that, for trustees, the case studies included in this report will prove the most interesting and useful reading. Those interested in general information and statistics relating to our casework and investigations may find the section on *Our role and approach to casework*, as well as the Annexes, more helpful.

For the first time, we have also included themes and lessons from the work of one of the principal regulators of *charities that are exempt* from registration with the Commission. This report highlights the work of the Higher Education Funding Council for England (HEFCE), the principal regulator of 110 charities.

We hope that trustees make use of this report and find it helpful.

## B. Our role and approach to casework

The Charity Commission is the independent registrar and regulator of charities in England and Wales. We regulate charities in the public's interest and it is our mission to ensure charities know what they have to do, the public know what charities do and charities are held to account.

Our role covers a range of activities from registering charities to providing online guidance to help trustees understand charity law; from maintaining the online register to investigating serious concerns about mismanagement and abuse in individual charities. We also provide charities with legal schemes and permissions where this is necessary to allow them to adapt to change. All of these activities aim at improving charities' compliance with the law.

We are a risk-based and proportionate regulator. This means we work to prevent problems by identifying and managing risks facing charities - whether they be to charity funds and property, charity beneficiaries or wider public trust and confidence in the charity sector.

We use our statutory powers proportionately according to the nature and level of the risk and our potential impact. Often, when we have concerns about a charity, we can make the biggest impact and ensure the best use of our resources by providing corrective regulatory advice that makes clear what steps trustees need to take to put the charity back on a secure footing. But in some cases the risk to the charity is so high that we may need to intervene to protect the charity using our legal powers.

We are not a criminal or prosecuting authority and the investigation of alleged criminal offences is the responsibility of the police and other law enforcement agencies. We work with other agencies, regulators, and Government departments to help us pursue our objectives, or to complement their work and to avoid duplicated regulation.

### New risk framework

In January 2012 we published a new *risk framework*, which explains how we assess concerns raised about individual charities. The assessment is based around three questions: do we need to be involved; what is the nature of the risk; and what is the most effective response. Factors that will help us answer those questions include whether the concerns fall within our remit; whether they call for the use of powers only we have; what impact the concerns might have on the charity's beneficiaries and assets; whether there might be wider implications for other charities; and what guidance and advice already exist to support a resolution. The new framework has not radically changed our approach to assessing concerns in individual charities. But we do now place greater emphasis on ensuring we only get involved and only use our regulatory powers where that is really the best way of resolving a problem. This reflects our statutory duty to use resources in the most efficient, effective and economic way and to be mindful of best regulatory practice.

## New approach to case handling

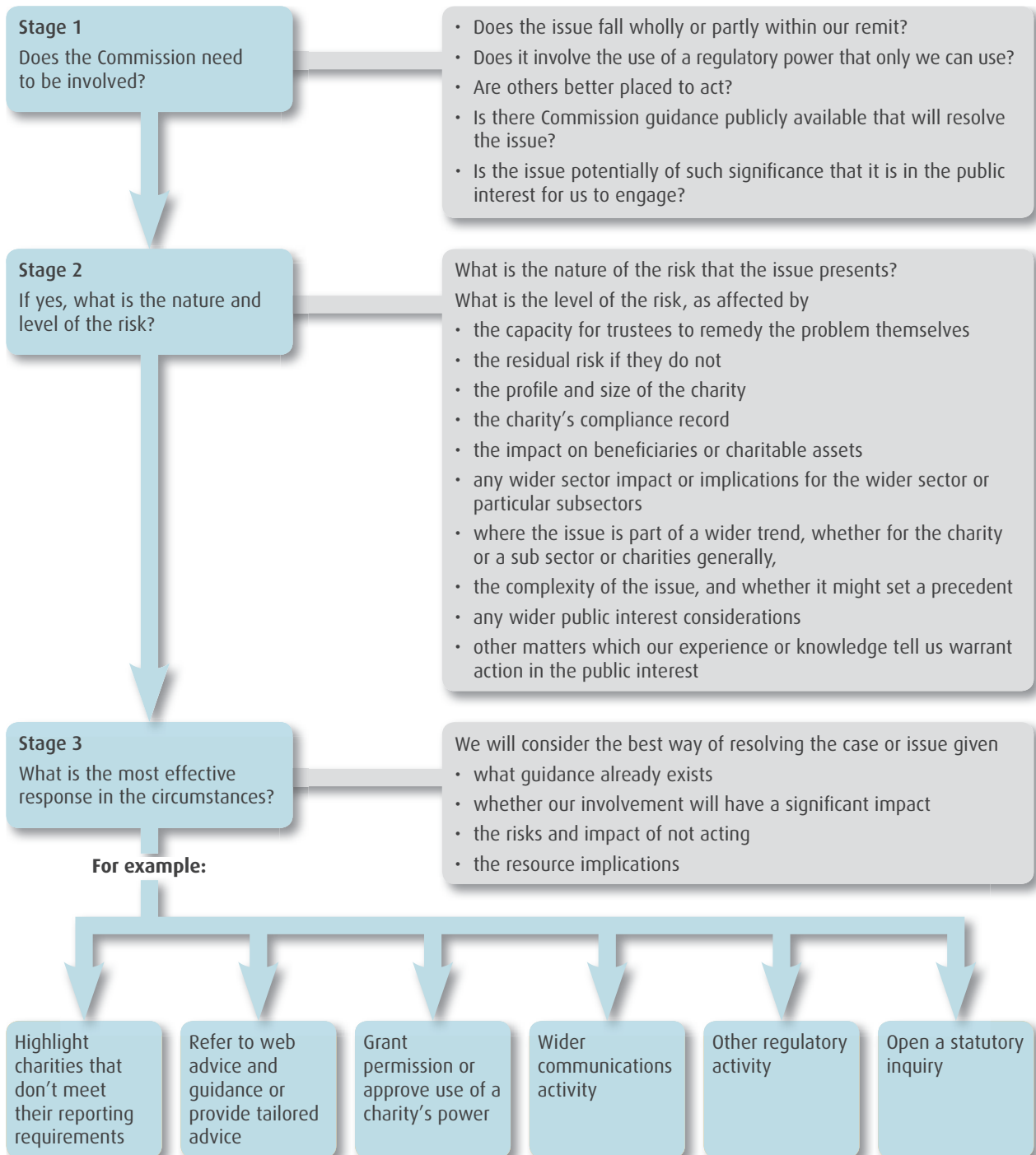
In December 2011, we adopted a new internal structure. Our restructure changed the way we handle cases involving serious concerns about charities.

Most concerns are now initially assessed by a new First Contact team. The First Contact team applies the *risk framework* to consider the seriousness and extent of the risk involved and to assess how well the charity itself is dealing with it. While the First Contact team resolves the majority of issues raised, it refers some cases to one of four new multidisciplinary Operations teams, which can look in more detail at problems and concerns and provide corrective regulatory advice and guidance to ensure trustees resolve their charity's problems. In the most serious cases, the First Contact team and the Operations teams refer matters to our new Investigations and Enforcement team, which carries out a pre-investigation assessment to determine whether it is appropriate to open a statutory inquiry (see diagram).

## This year's report

Because of changes to our structure, not all figures included in this report are directly comparable to last year's *Charities Back on Track*. Next year's *Charities Back on Track* report will look back at the first full year during which we dealt with compliance work under the new structure.

## Our approach to protecting the public's interest in charity – how we assess risks and manage resources



## Deciding whether to open a statutory inquiry

As explained, most problems in charities can be resolved by trustees themselves. Others will be resolved by our First Contact or Operations teams without the need to open a formal investigation. However, in the most serious cases we may need to open a statutory inquiry. This allows us to make use of the full range of powers at our disposal, including to obtain documents, protect charity assets, freeze charities' bank accounts<sup>1</sup> and remove trustees (for a list of all the powers used during statutory inquiries this year, please see Annexes 2.2 and 6). The cases we consider most serious are those in which there is evidence or serious suspicion of misconduct or mismanagement on the part of a charity's trustees and cases in which risks to the charity or to public confidence in charity more generally are high. This will include cases in which charity assets, services or beneficiaries are at immediate and/or high risk of abuse or harm. All statutory inquiries are carried out in our Investigations and Enforcement function. Our priority is always to ensure trustees meet their legal duties and requirements, stop the abuse or non-compliance and to take robust action where it is appropriate and proportionate to do so.

## Three strategic risks

Flowing from our approach to risk as set out in our risk framework, which explains how we address concerns about individual charities, we identified three areas of high regulatory risk needing a public strategic response from the Commission. These are tackling fraud and financial crime, safeguarding vulnerable beneficiaries and counter-terrorism. We have developed [three separate strategies](#) that explain how we respond to these high risks to the charity sector.

### Our strategy for dealing with fraud, financial crime and financial abuse in charities

Trustees are legally responsible for ensuring that their charity's funds are properly used and that they manage the risk of financial abuse, including fraud and other financial crime. Sound financial controls, good management and oversight are key to ensuring this.

The National Fraud Authority's Annual Fraud Indicator showed that charities estimated they lost 1.7% of their annual income to fraud, equal to £1.1bn of the sector's income for 2010/11. The most common types of fraud were cited as payment fraud, fraud by employees or volunteers and cyber fraud.

To help charities address the threat of fraud and financial abuse, we published our strategy for [Dealing with fraud, financial crime and financial abuse](#). The aim of our strategy is to prevent problems from occurring in the first place by alerting trustees to the risks of fraud and financial crime and by providing online guidance to help them to manage these risks.

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<sup>1</sup> Freezing a charity's bank account does not prevent it from operating; trustees or interim managers can ask for our permission to access their funds



It is for the police to investigate or prosecute fraud; our role is to establish how criminal matters arose and whether the trustees have responded appropriately. Where there is evidence that there has been mismanagement or misconduct in a charity and the risks justify it, we will intervene to ensure charity funds are protected and to put the charity back on a secure footing.

A key part of our strategy is cooperation with the sector and other government agencies to detect, deter and disrupt fraud in charities. We are currently leading a voluntary sector fraud project, which brings together charity regulators, members of the sector and other parts of government to reduce the risk of fraud to charities. This project supports *Fighting Fraud Together*, the government's UK strategy for tackling fraud. As part of our partnership work, we have supported the publication of guidance produced by the Fraud Advisory Panel - *Giving Safely* and the Charity Finance Group - *Charity Fraud: a guide for trustees and managers of charities*.

See section C of this report for examples of our case work involving concerns about fraud and financial crime.

It is important that people who abuse charities are brought to justice and in our investigative and compliance cases we work with the police, Her Majesty's Revenue and Customs (HMRC) and other law enforcement agencies to help ensure that happens. We help them to secure successful prosecutions of charity trustees or staff members who have abused their position for personal gain. Over the past three years, we have made over 30 referrals about suspected serious criminal activity connected to charities to the police and law enforcement agencies and our staff have provided over 100 police witness statements. Our staff members have also appeared in court to give oral evidence at criminal trials.

Often, criminal cases take a long time to conclude. It is vital that those involved have a fair trial and nothing we do as regulator prejudices that. For this reason, we may not be able to discuss our own cases publicly, meaning that it can sometimes be difficult for the public and charities to see what we are or have been doing - namely working very closely with the police and the Crown Prosecution Service to help secure a conviction.

### **Our strategy for dealing with safeguarding children and vulnerable adults issues in charities**

The Commission's aim is to ensure that charities working with or providing services to vulnerable beneficiaries protect them as best they can and minimise the risk of abuse. We may consider any failure to do so as misconduct and/or mismanagement in the administration of the charity. We are not the agency primarily responsible for safeguarding issues. Our focus is on charity law and on ensuring trustees fulfill their duties. Concerns about the safety of vulnerable people or allegations of criminal abuse in charities are for other agencies, including the police and local authorities to deal with. In the past, there was some confusion in about our role as regulator, and concern about possible duplication with the work of other agencies.

Our strategy - *Dealing with safeguarding children and vulnerable adults issues in charities* helps clarify our role and approach in dealing with safeguarding issues in relation to charities. It has a four-strand approach which emphasises prevention and makes clear when we might intervene, why and how. It explains what trustees' duties mean in practice and sets out what is expected of trustees when dealing with allegations or actual incidents of abuse. It also explains how we work with the sector and other agencies to help charities prevent safeguarding issues from arising in the first place and how we respond when such concerns do arise. See section C of this report for an example of a case involving concerns about the safeguarding of vulnerable beneficiaries.

### **Our counter-terrorism strategy**

Charities, like other types of organisation, can be vulnerable to criminal and terrorist abuse. Our experience indicates that the number of cases in which there is evidence to prove charities have been involved in supporting terrorist activity whether directly, indirectly, deliberately or unwittingly is small in comparison to the size of the sector. However, such abuse is completely unacceptable and corrodes public confidence in charities. Trustees therefore need to ensure that their charity is not at undue risk. They must handle concerns and allegations about links between the charity and known or suspected terrorist groups or individuals responsibly and appropriately. Charities working in regions where terrorist groups are known to operate must take adequate steps to manage the risk and ensure proper due diligence checks and monitoring is carried out so that the donating public can have confidence that their money is reaching the intended beneficiaries.

Our *Counter-terrorism strategy* explains our role and approach for dealing with concerns about the abuse of charities for terrorist purposes and tackling the risk of terrorist abuse in the charitable sector. It explains how we make trustees aware of the ways in which they can safeguard their charities against this risk. It also sets out what help there is for trustees to ensure they protect their charity from terrorist and other abuse.

### **Assessing risks and monitoring charities**

As well as looking into concerns that come to us, the public expects us to be proactive about identifying serious problems in the sector. Some of this work is carried out by our Monitoring unit (part of the Investigations and Enforcement team) and focuses on our three strategic risk areas. The unit monitors charities about which there are serious concerns relating to non-compliance. Regulatory supervision and monitoring is an important tool in identifying and detecting harm and abuse within charities, and in disrupting the activities of those seeking to abuse them. We work closely with other government regulators and law enforcement agencies. Sometimes, we monitor a charity when we are not able to take immediate action, or are restricted in the action we can take because a law enforcement agency is undertaking an investigation and there is a risk our work might prejudice or frustrate this.

## Assessing risk in our Operations teams

Pro-active work forms a key component of our four new Operations teams to ensure regulatory compliance and accountability across the Sector. This includes monitoring charities identified as being potentially at risk and ensuring, in appropriate cases, that charities have implemented agreed action plans to remedy identified problems. Increasingly, we will follow up cases following our initial intervention to ensure that these charities are no longer at risk.

We particularly aim to increase our knowledge of the various sub-sectors to identify risks and trends and increase our own internal knowledge and expertise, helping us become more responsive to issues. We have, for instance, started to look at think tanks to identify whether any specialist guidance is needed to prevent trustees breaching charity law. We will also undertake wider projects where risks have been identified, such as the [work that we are currently undertaking with charities in Wales](#), in conjunction with other bodies, to promote good governance. This will supplement the Operations teams' work in providing regulatory permissions in higher risk cases and examining non-compliance in cases where investigations have not been opened.

## Accounts scrutiny

We also review information that charities supply to us in their accounts. For example, this year, we have reviewed samples of charities' accounts to establish how well trustees are complying with their duty to include information regarding their reserves policies in their accounts. A [report of that research](#), which showed improvements in charities' compliance since 2006, is available on our website. Over two thirds of the Trustees' Annual Reports we looked at as part of this research included a reserves policy. Similarly, we have conducted research into the profile of charities that failed to file their annual accounts on time. We sampled the accounts of 400 charities that filed their accounts more than 30 days late, and found that a quarter of those with incomes of over £250,000 had filed late for all of the previous five years, indicating that non compliance in this area is a habitual problem for many charities. You can read an [article about this research](#) on our website.

## Working with the sector

We also work with the sector and charity advisers to help identify areas of general risk to charities. For example, we have developed pilot charity review projects with the Institute of Chartered Accountants in England and Wales (ICAEW) and the Institute of Chartered Secretaries and Administrators (ICSA). The two projects, the first of which is now complete, aim at helping us and the wider sector understand areas of strength and good practice as well as potential areas of weakness in charities.

## Reporting Serious Incidents

Trust in the sector is so important. Abuse of a charity or serious incidents in a charity can give rise to regulatory problems and can undermine public confidence in charities. This is why trustees should let us know when their charity experiences an incident that is particularly serious. We regard an incident as serious if it has resulted or could result in a significant loss of funds or a significant risk to a charity's property, work, beneficiaries or reputation. Serious incidents might therefore include theft or fraud within a charity, or vulnerable beneficiaries having been put at risk. As a matter of good practice, trustees should inform us as soon as the incident has occurred. *Reporting serious incidents* lets us know that trustees have properly identified a risk to the charity and are taking appropriate steps to manage this. When it is clear that the trustees are managing an incident appropriately, there may be no role for us. However, we may need to get involved following a serious incident if we have concerns about the way in which the trustees have responded. We also check to make sure that the incident is not likely to have an impact on other charities, for instance because someone involved has links to another charity. Where we identify a pattern, for instance a certain type of scam affecting charities, we issue alerts to warn the wider sector.

## C. Common areas of serious concern

### Poor governance and failures of trusteeship

Trustees are in charge of their charities and have wide discretion to make decisions on their charities' behalf - including decisions that are controversial or difficult for some people connected to the charity to accept. But with that freedom come important responsibilities for trustees, including a fundamental duty to make proper decisions in good faith, taking into account only the charity's best interests - not private interests or the interests of any other organisation. This involves ensuring that decisions are in line with the charity's governing document, that any conflicts of interest are managed appropriately and that trustees account transparently for their decisions. These principles are the cornerstone of good charity governance. Most trustees understand this instinctively and know how to separate their decisions as trustees from any other interests or roles they might have in their lives and how to ensure they act within their powers.

But our casework this year has, yet again, found that too many charities experience problems because trustees have failed to understand their duties or have acted outside their powers.

Concerns about poor governance or poor trusteeship featured in:

- **597** of the 1,374 assessment cases
- **73** investigations closed this year (out of a total of 85) - this includes concerns about breaches of the charity's governing document, unmanaged conflicts of interest, fundraising governance and unauthorised trustee benefits.

### Concerns about breaches of governing document

One of the most important characteristics that mark out a good charity is that it is clear about its purpose, mission and values.

Charities gain that clarity from their governing document. A charity's governing document is a formal document which sets up a charity and which should contain information about:

- *what* the charity does (the charity's objects)
- *how* the charity will do things (its powers)
- *who* will run the charity (who the trustees are)
- *what* happens if the charity needs to make changes to the governing document or needs to wind up.

Many governing documents also include information about how the trustees will run the charity and the arrangements for meetings, voting and minute taking.

Making sure the charity operates within the provisions of its governing document is one of trustees' most important duties. This does not mean that the charity's objects or powers cannot change with the times. In fact, most charities that have been in existence over a long period of time will need to make changes at some point to ensure the charity is still able to provide an important service. Often, charities will need our consent to make the changes.

But a charity cannot simply act outside the provisions of its governing document. After all, those supporting a charity - whether through donations or by volunteering - will be doing so in the expectation that the charity has certain aims and goals and a certain way of doing things. Trustees cannot simply ignore or overrule these.

Most trustees understand this, but problems resulting from breaches of governing documents are among the most common reasons we have to get involved in charities and are often linked to wider governance problems. Breaches of governing documents or concerns about charities acting outside their objects featured in **17** investigations concluded this year (out of a total of 85).

### **Case study - Regulatory compliance case into Knotty Ash Special School Trust<sup>1</sup> (charity number 526085)**

The charity, which owned land and buildings, was established to provide services and facilities to schools in Liverpool for children with special educational needs. Liverpool City Council ('the Council') was the corporate trustee of the charity, a school for children with special needs was sited on part of the charity's land.

Concerns were raised in the local media about a Council employee who had been allowed to live rent-free for over twenty years in a property owned by the charity and also about the lack of charitable use of much of the land.

The tenant had been an employee of the Council and had occupied the property under a service tenancy as a caretaker of the land. When the service tenancy had ceased many years ago, the Council had been unable to remove the tenant from the property due to issues relating to local authority tenants' rights. In allowing a Council employee to live rent-free, the Council had breached its trustee duty to act in the best interest of the charity. Charity property should either be used to further its objects or be invested to generate income. Although the Council maintains that it had made a prior commitment to repay the charity the market rent lost as a result of this breach of trust, it was only after we intervened that £89,000 of charitable funds were repaid to the charity.

With the exception of the land upon which the special school is sited, the investigation found that the charity's property had not been used for any significant charitable purpose for many years. As a result of our intervention the charity's land was split in two. The land on which the special school is sited was transferred to a new charity of which Liverpool City Council is the sole trustee. The remaining land stayed in the original charity and a scheme was sealed that transferred the trusteeship from the Council to Liverpool Lighthouse Ltd which intends to use the land as an eco garden. The name of the charity was changed to Bright Park.

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2 The charity is now known as Bright Park

## Lessons from this case

Trustees must use charity assets to further the charity's objects. Any decisions to lease charitable property should be in the charity's best interests and lease agreements should seek the best financial return possible.

Trustees need to be aware of the potential negative impact that a lack of charitable activity and the ineffective use of charity resources can have on the reputation and public trust and confidence in a charity.

Many charities have a local authority as a sole trustee. When a local authority is the sole trustee of a charity it must take care to be clear when it is acting in its capacity as a trustee. When doing so, its actions must be in the best interests of the charity and it must not allow its interests as a local authority to interfere with its decisions as a charity trustee.

## Unmanaged conflicts of interest

Conflicts of interest are situations in which trustees' personal interests, or their relationship with another organisation affect - or may appear to affect - their decision making. It is inevitable that conflicts of interest occasionally occur in charities. This does not necessarily cast doubt on the integrity of the trustee in question or mean they have done anything wrong. However, even the appearance of a conflict or interest can damage a charity's reputation. So trustees need to ensure they are aware of these and that any conflicts or potential conflicts are managed carefully.

Sadly, our case work shows that trustees often fail to manage conflicts of interest appropriately. Charities can therefore lose out to the interests of other organisations, or individuals. Unmanaged conflicts of interest featured in **16** investigations concluded this year (out of a total of 85).

### **Case study - Regulatory compliance case into Plymouth Argyle Supporters Training and Development Trust (charity number 1056117)**

The charity was set up to provide leisure and recreation facilities (and in particular football), for young people in the West Country. In practice, the charity had historically provided football training sessions for young people, in connection with Plymouth Argyle Football Club ('PAFC') across the South West of England. From inception, its trustee body was drawn from various PAFC supporters' clubs across the UK. Over time, two trustees also became directors of PAFC.

We opened an investigation after becoming aware that the charity had made a £330,000 loan to PAFC. The investigation looked into whether the loan was a lawful exercise of the trustees' powers and a proper discharge of their duties. It also examined aspects of the charity's financial controls and its management by the trustees.

After the loan had been made, PAFC went into administration, putting the charity's remaining funds at risk. Although the loan had been secured against PAFC's stadium, this was worth less than the loans secured against it.

We concluded that the trustees' decision to lend £330,000 of charitable funds to PAFC did not appear, in the circumstances, to be one which a reasonable body of trustees could have made. In addition, the trustees did not take adequate security to safeguard the charitable funds lent. By not seeking professional financial investment advice before the decision to make the loan, the trustees had failed to follow the terms of the charity's governing document, and making the loan was therefore not a proper exercise of the trustees' investment powers and was a misapplication of funds.

We also concluded that the trustees, all of whom had links to, or an interest in PAFC, had not properly managed their conflicts of interest. This affected whether they could demonstrate that the decision to lend to PAFC was in the best interests of the charity rather than those of the football club. We were critical of the trustees for allowing the situation to arise, but found they had since done everything expected of them to rectify it.

Our intervention ensured the trustees took steps to try to secure the future repayment of the funds so that these could be used in accordance with the charity's objects. The charity has now entered a new agreement with the new owners of PAFC for the repayment of the loan, plus interest, over a five year period. We also provided regulatory advice and guidance to the trustees to enable them to regularise the position of the charity and in particular on governance, decision-making processes and financial controls. We are monitoring the trustees' adherence to their new policies and the supervision of the recovery of the charity's funds.



## Issues for other charities

Charities are independent entities that exist to assist their beneficiaries. Where charities may be linked to other groups, such as professional sports clubs, the trustees must remember that the interests of the charity must be placed at the forefront of their decision making. Trustees must actively manage any conflicts of interest. It is vital that trustees avoid becoming involved in situations in which their personal interests may be seen to conflict with their duties as trustees. The trustees should put in place policies and procedures to identify and manage such conflict. Further information can be found in [A guide to conflicts of interest for charity trustees](#).

Charitable funds must only be used to further the charity's purposes. If charitable funds have been misused then charity trustees are expected to take reasonable steps to identify what has happened to the funds and consider what course of action is reasonable, seeking professional advice as appropriate.

It is essential that trustees are familiar with and follow the requirements of their charity's governing document. All decisions concerning the charity must be taken by the trustees in accordance with its governing document and must be made collectively as a trustee body. Trustees are not carrying out their duty to the charity if they place the interests of other bodies ahead of those of the charity and the Commission considers this an example of poor governance which may be used as evidence of mismanagement.

Advice about good governance can be found in the Commission's publications [The Essential Trustee: What you need to know \(CC3\)](#) and in respect of charity finances - [Internal Financial Controls for Charities \(CC8\)](#).

Trustees have overall responsibility for the investment of a charity's funds. If trustees can demonstrate that they have considered the relevant issues, taken advice where appropriate and reached a reasonable decision, they are unlikely to be criticised for their decisions. The Commission has produced guidance on [Charities and Investment matters: A Guide for trustees \(CC14\)](#).

## Concerns about fundraising governance

Trustees must ensure their charity complies with the law relating to fundraising and should follow best practice. This includes all aspects of fundraising including the methods used, the costs involved, the financial risk and how the money raised is spent. Trustees need to think about the impact their fundraising methods will have on public opinion and the reputation of their charity.

The Commission is not the primary regulator of fundraising; fundraising is self regulated, which means fundraisers and the sector set and follow their own standards of fundraising practice. Self regulation is supported through the self-regulatory codes developed by the Institute of Fundraising (IoF), through the work of the independent complaints body, the Fundraising Standards Board (FRSB) and the Public Fundraising Regulatory Association, the charity-led membership body that self-regulates all forms of direct debit face-to-face fundraising.

However, while we are not the regulator of fundraising methods, we may get involved where there are serious concerns about trustee oversight or serious concerns about a charity's wider governance that are connected to its fundraising activities. Concerns around fundraising governance featured in **9** investigations concluded this year (out of a total of 85).

### **Case study 1: Statutory inquiry into Alzheimer's UK Research Education and Care Ltd (charity number 1115434)**

The charity was set up to preserve and protect public health through the promotion of research leading to a cure for Alzheimer's and the relief of those suffering with the disease. We received a complaint about the remuneration of the acting CEO in relation to the level of charitable expenditure. After considering further information obtained from the charity's trustees by order, the Commission had serious concerns about the use of charity funds and the governance of the charity.

The Commission therefore opened an inquiry which examined the appointment of the acting CEO and her relationship with companies providing services to the charity; the use of charity funds, in particular the proportion being applied to charitable activities; the appointment of the trustees; and the general governance of the charity. The inquiry established that in the two financial years ending 31 March 2007 and 31 March 2008, over 92% of the charity's expenditure was accounted for by the costs associated with fundraising mail shots and the acting CEO's salary. None of the charity's funds had been spent on charitable activities since its registration in July 2006. The charity had become no more than a fundraising vehicle. During the course of the inquiry, the Commission took steps to protect the charity's property by 'freezing' its bank accounts<sup>3</sup>.

The charity had engaged two private companies, previously known to the acting CEO, at a significant cost, to raise funds. These funds were then used to pay the salary of the acting CEO and to pay for further fundraising contracts. The trustees had failed to oversee and properly scrutinise the activities of the charity, the acting CEO and the fundraising strategy.

The Commission concluded that the trustees had not managed the charity effectively; they met infrequently; had little input into the running of the charity; had no control over its finances; and relied too heavily on the CEO.

The Commission decided to give the trustees authority to wind the charity up. The Official Receiver appointed to the charity, advised the Commission that the remaining funds would not be enough to cover the charity's debts, and consequently no money would be available to be distributed for charitable purposes. The charity has now been removed from the Register of Charities.

<sup>3</sup> Freezing a charity's bank account does not prevent it from operating; trustees or interim managers can ask for our permission to access their funds

## Lessons from this case

Trustees themselves will not always raise funds for the charity or organise fundraising on a day-to-day basis. However, they retain overall responsibility for every aspect of the charity's activities and they should have proper mechanisms for delegating activities such as fundraising, with clear terms of reference for those exercising the delegated authority. Trustees should take an active interest in the fundraising activities run by the charity and ensure that they receive regular reports on performance targets in order to exercise proper oversight. For small charities, it may not be appropriate to have formal mechanisms in place such as terms of reference. However, it is essential that trustees of small charities are still aware of their responsibility to ensure any proposed fundraising appeal is well planned and well executed. The Commission has produced guidance on fundraising *Charities and Fundraising (CC20)*.

### Case Study 2: Regulatory compliance case into Sunrise Radio South East Asia Disaster Appeal

On-air fundraising appeals for humanitarian disaster relief were made by radio stations after the 2004 Indian Ocean tsunami and the 2005 Pakistan earthquake. By November 2005 the two appeals had together raised over £160,000. We received complaints that the funds had not been used for the charitable purposes for which they had been raised. Although neither radio station is a registered charity, we established that the funds raised by the appeals were held for charitable purposes and accordingly fell within the Commission's regulatory jurisdiction, and that the signatories to the bank accounts were therefore trustees of the funds and had the legal duties and responsibilities of trustees. We opened an investigation to examine these concerns.

In November 2010 we found that these funds had still not been used for the causes for which they had been raised. The trustees had not considered at the time of the appeals how the funds were to be used and whether this was clear to donors. We considered that donors would have expected the funds to have been applied quickly and not five to six years after the disasters.

The funds (in excess of £180,000) have now been awarded to two charities working in the areas affected by the tsunami and earthquake. We provided the trustees with regulatory advice and guidance regarding charitable appeals generally and specifically on their legal duties and responsibilities as trustees of charitable funds.

## Lessons from this case

It is important that trustees plan properly for any fundraising appeal. This is particularly important when raising funds for those affected by disasters, where the need for humanitarian relief is immediate. The public often responds generously to such appeals and expects, given the urgent need for relief, that the funds will be applied quickly. Before launching a disaster appeal trustees should consider whether their charity or organisation is able to deliver services where the disaster has occurred. It may be more appropriate to raise funds on behalf of another charity that is in a position to do so.

More generally, when embarking on an appeal for a particular purpose trustees should also ensure they have provisions in place to cover all eventualities, including what will happen if the appeal fails to reach its targets and how any excess funds might be spent. This should be made clear when promoting the appeal. Donors should be able to give confidently, knowing how their donation will be used.

We have published new guidance on [Starting, running and supporting charitable disaster appeals \(CC40\)](#). It is intended to provide information and advice to charities as well as members of the public who want to give much needed help to people affected by a disaster or other humanitarian crisis.

## Fraud and financial crime

Any fraud and financial crime against charities is unacceptable, and while charities are no worse affected than other sectors of the economy, our case work and research by the National Fraud Authority (NFA) show that financial crime continues to affect the work of too many charities (see above for further information about the NFA survey and our approach to tackling the risk of fraud against charities).

Concerns about fraud featured in:

- **18 investigations** concluded this year (out of a total of 85)
- **364 Reports of Serious Incidents** made this year and (out of a total of 1,027)
- **56 whistleblowing reports** (out of a total of 121).

Trustees are legally responsible for ensuring that their charity's funds are properly used and that they manage the risk of financial abuse, including fraud and other financial crime. Sound financial controls, good management and oversight are key to ensuring this. It is also important that trustees report suspected fraud to Action Fraud, which is the national reporting centre for fraud and internet crime on behalf of the police. Reporting incidents to Action Fraud will mean charities get a crime reference number and will help the police tackle organised crime.

### Case study 1: Statutory inquiry into Brent Educational and Recreational Support Youth Challenge (BEARS) and Gate Lane Community

The charity BEARS (former registered charity number 1057993) worked with disadvantaged children, aiming to support their participation in mainstream society and reduce the risk that they would get involved in violence and gun crime. The activities of the charity Gate Lane Community (former registered charity number 1106853) focused on creating a community centre.

After investigating concerns raised with us about BEARS, we referred possible criminal activities to the police. The Chair and Director were later found to have misappropriated funds for personal use and subsequently admitted a number of offences.

Our inquiry into BEARS found that there had been serious mismanagement and misconduct in the administration of the charity. The inquiry also identified that BEARS had ineffective governance and financial controls in place, which had enabled the trustees and the Director to obtain unauthorised benefits. There had been a clear breach of duty by three of the charity's trustees as a result of conflicts of interest and unauthorised trustee benefits, which they had failed to resolve.

The inquiry into Gate Lane Community found that there had been mismanagement, unmanaged conflicts of interest and that the decisions taken by the trustees were invalid. It was also unclear to what extent the charity had furthered its charitable objects for the public benefit.

The Commission removed both charities from the online Register as they had ceased to operate.

A lack of any financial controls had allowed significant and sustained fraud to take place. The Chair and the Director of BEARS have since been convicted of theft. The police initiated confiscation proceedings against the Chair to recover the stolen money but found that he did not have any assets. The Director had already paid back the money taken from BEARS.

### Lessons from this case

Misapplying charitable funds for private benefit amounts to breach of trust and may be theft. It can also do serious damage to public trust and confidence in the charitable sector.

Trustees cannot receive any benefit from their charity in return for any service they provide to the charity unless they have express legal authority to do so. 'Benefit' includes any property, goods or services which have a monetary value, as well as money. Such legal authority can come either from a clause in the charity's governing document or, where there is no adequate clause in the governing document, from the Commission or the Courts.

Trustees must act only in the interests of their charity, and not for their own private interest or gain. Even the appearance of a conflict of interest can damage the public trust in a charity, so conflicts need to be managed carefully.

Trustees must take ultimate responsibility for directing the affairs of a charity, and ensuring that it is solvent, well-run, and delivering the charitable outcomes for the benefit of the public for which it has been set up. They must act with integrity, and avoid any personal conflicts of interest or misuse of charity funds or assets. They must use charitable funds and assets reasonably, and only in furtherance of the charity's objects. Information on good governance can be found in the Commission's publications *The Essential Trustee: What you need to know (CC3)* and *The Hallmarks of an Effective Charity (CC10)*.

See our guidance *Charities and Risk Management (CC26)* and *Internal financial controls for charities (CC8)* for more information. Chapter three of our online compliance toolkit, *Protecting Charities from Harm*, focuses on *Fraud and financial crime* and provides guidance for trustees on how to reduce the likelihood of such crime occurring in their charity.

### Case study 2: Statutory inquiry involving African Cultural Media and Leisure Group

Our investigation into this charity was conducted as part of a class inquiry into over 30 charities, about which the Big Lottery Fund raised concerns with the Commission and the police. It was for the police to investigate allegations of criminal offences. Our role as regulator was to determine whether we needed to take steps to protect charity assets and ensure the charities were being properly managed. We have chosen to focus on one of the charities involved in that class inquiry.

The African Cultural Media and Leisure Group (ACMLG) had objects to promote charitable purposes for the benefit of people in the London Borough of Haringey, especially of refugees and asylum seekers from Africa.

Our inquiry into ACMLG examined concerns about mismanagement and misconduct in the administration of the charity. While our investigation found that the charity did carry out some charitable activity, we found that the charity had poor internal controls in place, which put its assets at serious risk.

For instance, we found that the charity's funds were transferred into the personal bank account of one of the trustees. As we did not receive a satisfactory explanation for these transactions, they were taken as evidence of financial mismanagement. Our inquiry also found that the charity had entered into a number of financial transactions with private companies in which some of the charity's trustees had personal interests. The trustees were not able to explain to the Commission how these conflicts of interest were managed and how the payments to these companies were in the charity's best interests. Our inquiry concluded that there had been financial mismanagement by the charity's trustees and that they had failed in their duty to put in place sufficient internal financial controls, file the charity's accounts with the Commission and properly manage conflicts of interest. During the course of the inquiry we used our statutory powers, including to freeze the charity's bank accounts. One of the trustees of the charity has since been convicted of a criminal offence in connection to the charity. The charity was removed from the online Register in July 2011.

## Lessons from this case

Trustees are under a legal duty to ensure their charity's funds are applied solely in furtherance of its objects. They must also be able to demonstrate this is the case. Trustees must put in place adequate internal financial controls to protect their charity's assets.

The Charities Act also requires trustees to keep accounting records that show and explain its transactions and its financial position. This means that trustees must keep records and maintain an adequate audit trail to show that the charity's money has been properly spent on furthering the charity's purposes for the public benefit.

The abuse of charities for fraudulent purposes is absolutely unacceptable. When we find evidence that a criminal offence may have been committed, we will share that evidence with the police or other appropriate law enforcement agencies.

The governing documents of many charities include provisions for handling conflicts of interest. Where these exist, trustees must adhere to them when making decisions about payments to connected parties. When charities' governing documents do not include such provisions, it is best practice that conflicted trustee(s) remove themselves from the decision making process. The independent trustees should also seek quotes from alternative service providers to establish that the use of the connected companies/individuals is in the best interests of the charity. Otherwise, the trustees concerned may be liable to make good the payments.

## Concerns about safeguarding vulnerable beneficiaries

While the Commission is not responsible for regulating safeguarding issues or investigating child abuse, our interest is in whether trustees have acted responsibly and complied with their charity law duties. Trustees of charities which work with children and vulnerable adults have a duty of care to their charity which will include taking the necessary steps to safeguard and take responsibility for those children and vulnerable adults. They must always act in their best interests and ensure they take all reasonable steps to prevent any harm to them. Trustees also have duties to manage risk and to protect the reputation and assets of the charity.

Our casework this year demonstrates that many trustees do not fulfill their duties towards their charities in this regard. We still see cases where there are serious concerns about the safety of vulnerable beneficiaries resulting from a lack of oversight or governance by charity trustees. In particular we see incidents where trustees have failed in their responsibility to ensure that policies and procedures are put in place and implemented to protect any vulnerable beneficiaries the charity works with. However, we also see instances where some charities and trustees are acting appropriately as the case study below highlights.

Concerns about safeguarding featured in:

- **47** of the 1,374 assessment cases
- **11** investigations concluded this year (out of a total of 85)
- **394** Reports of Serious Incidents made this year and (out of a total of 1,027)

## Case study

This case study provides an example of a charity responding appropriately to an alleged safeguarding incident and provides a model of best practice for other charities to learn from.

### **Report of a serious incident by an educational charity**

The charity runs a school providing a specialist environment for children and young people with autism.

The charity submitted a serious incident report (RSI) to us, following an incident of the alleged use of unacceptable physical intervention by a teacher during a lesson. The school's designated safeguarding officer was notified, and the teacher, who was a temporary member of staff, was immediately suspended. The charity sought employment advice and referred the matter to the Local Safeguarding Children Board, which determined that there was no allegation of criminal wrongdoing and referred the matter back to the charity for an internal investigation.

By this time, the suspended member of staff's temporary contract had been terminated.

The trustees' internal investigation sought to establish whether an incident had taken place; what events led up to the alleged incident, whether any action could be taken to prevent another such incident arising in future, whether misconduct took place and whether any further action should have been taken, had the staff member remained employed by the school.

The charity's investigation concluded that it was not clear whether the incident was an act of gross misconduct. However, it also concluded that the alleged intervention did not use a strategy recognised by the school and, had the staff member continued to be employed by the school, a verbal warning, retraining and subsequent supervision would have been appropriate.

The charity presented the Local Safeguarding Child Board and local authority HR department with a summary of its investigation and made a formal referral to the Independent Safeguarding Authority, which in turn made a referral to the Teaching Agency, acting on behalf of the Secretary of State for Education.

## Lessons from this case

In taking the steps explained above, including by reporting the matter to us as an RSI, the charity's trustees were able to demonstrate that they were meeting their statutory and charity law duties. They acted in a timely manner to deal with the incident and worked with the other specialist agencies. We sometimes see trustees simply viewing such incidents as criminal matters. This can mean that, if the police and safeguarding agencies do not act, the trustees disengage and are not comfortable looking at matters themselves. This was not the case here; the trustees acted appropriately in terms of governance and oversight. The trustees were also able to provide assurances that they had followed appropriate internal procedures, regulations and statutory procedures. We would expect trustees of other charities finding themselves in similar situations to respond as this charity did.



Some charities are nervous of reporting these sorts of incidents to the Commission because they may face another investigation and they are concerned about dual regulation. However, this example shows that this is not the case. The Commission needed to be aware of the incident to check that there was not a risk to other charities and to ensure that the trustees were acting responsibly and the other specialist agencies were informed and engaged, which is what happened.

## Failures to monitor and verify the end use of funds

Charity trustees have a duty to ensure their charity's funds are used for legitimate purposes and are reaching the intended beneficiaries. This means trustees have a duty to carry out appropriate due diligence checks on individuals and organisations that give money to or receive money from their charity. If they identify risks, they must take steps to manage these. These risks can be particularly high for charities working internationally, not least because many such charities work with and through local partners.

Charities working overseas in high risk areas need to have strong controls in place to provide protection for the charity's assets and funds and this affords the best defence for trustees against the charge of failing to protect the charity's assets and funds. However, our case work demonstrates that this does not always happen, and trustees fail to maintain high standards of governance and accountability that safeguard a charity from a range of potential abuse, including fraud, financial abuse and terrorist abuse, and make the organisation generally less vulnerable.

Concerns about accounting issues - including concerns about proper accounting records and due diligence - featured in **26** of 85 investigations closed this year; concerns about alleged connections to terrorism featured in **5** of 85 investigations closed this year.

### Case study: Statutory inquiry into Crescent Relief

The charity's main activities included emergency relief and reconstruction work in Pakistan following the 2005 earthquake and Indonesia following the tsunami.

Our inquiry was opened to examine the charity's financial management and its supervision of overseas activities to investigate concerns that funds had been unlawfully used. Our statutory powers were used to freeze the charity's UK bank accounts to safeguard charitable funds while these concerns were being investigated.

From the information examined by the investigation we concluded there was no evidence that the trustees diverted charitable funds for unlawful or non-charitable purposes. However, the investigation concluded that the trustees were unable to satisfactorily verify the end use of funds in Pakistan and Indonesia. We also determined that measures taken to control, monitor and document the use of charitable funds overseas by third parties were insufficient. Consequently, we made an Order to direct the trustees to carry out a governance review of the administration and management of the charity and implement the outcomes of that review. We monitored compliance with the review and will be publishing a report shortly.

## Lessons from this case

Trustees have a legal duty to protect their charity's assets. Where a charity gives money to partners or beneficiaries, or uses partner and delivery agents, trustees must carry out proper due diligence checks. Trustees must also monitor use of the charity's funds, checking both that funds reach their destination and that they are used for the purposes intended. Our compliance toolkit chapter 2 on *Due diligence, monitoring and the verification of the end use of funds* includes practical tools to help trustees understand risk and assess their charity's systems.

Charity trustees must also keep adequate financial records for the receipt and use of funds and audit trails of decisions. Records of domestic and international transactions must be detailed enough to show that funds have been spent properly and in line with the charity's objects.

The Finance Act 2010 says that, when transferring funds to a non-UK body, trustees must take 'such steps as are reasonable' to ensure the funds will be applied for purposes recognised as charitable under English law. This revised legislation makes it clear that such steps have to be reasonable in the view of Her Majesty's Revenue and Customs (HMRC). This means that charities working internationally need to ensure that their practices for assessing grant applications and monitoring donations overseas stand up to scrutiny. Visit [HMRC's website](#) for more information.

Charities that set up disaster funds and spend often large amounts of money quickly, in areas affected by disasters are likely to be at more risk of fraud and other financial crime than charities operating in more stable environments. They may be operating in countries where the physical and financial infrastructure is affected. They may be starting operations in a new area or working with new partners. They may need to place an unusual reliance on cash transfers or use financial intermediaries. It may be more challenging for charities to maintain the same standards of transparency and accountability as would apply in the UK, but they must strive to do this.

## Concerns about sham charities

It is rare for the Commission's casework to uncover concerns that a charity has been deliberately set up for illegal or improper purposes - organisations that might be called 'sham charities'.

However, criminals do sometimes set up charities for the purpose of abusing them to generate private profit or gain.

This is totally unacceptable, and, when there is evidence to suggest this is the case, we take firm and decisive action. Suspicions about charities set up for illegal or improper purposes featured in **4** of the 85 investigations closed this year.

### **Case study: Regulatory compliance case into the registration applications of seven organisations causing concern**

The seven organisations that we investigated as part of this case were newly registered as charities but, following our investigations, were removed from the online Register. We identified common features in the registration applications of the organisations which caused concern about their claims to be legitimate charities.

As part of our monitoring procedures, we identified that the address given for the correspondent of one of the organisations was an unoccupied address. Further monitoring work subsequently identified that 35 separate online applications to register including the seven organisations had been made in a two week period from organisations based all over the country. These organisations and/or the details provided to us shared common features (for example, addresses of properties that turned out to be unoccupied; addresses which did not exist; non operational telephone landlines or mobile telephone numbers; and the same financial information repeated in different registration applications).

As a result of these concerns, 28 registration applications were put on hold and we opened investigations into all seven registered organisations to examine any inter-relationship and whether they were shams set up for illegal or improper purposes, or if not, whether they were capable of operating as charities and whether the trustees existed.

During these enquiries, we were unable to verify the accuracy of the information which had been provided by the seven organisations at registration and despite repeated attempts, were unable to contact any of the persons who were said to be their trustees or connected with their administration. As a result, we were unable to conclude that these were in fact legitimate organisations set up to operate as charities or that they legally existed.

We removed all seven organisations from the online Register and discontinued the registration process for the other 28 organisations.

Given the identified connections between the organisations we were concerned that the information provided may have been false. As it is an offence under section 60 of the Charities Act 2011 to provide false or misleading information to us, we therefore reported our concerns to the police.

### **Lessons from this case**

We have a statutory duty to remove from the online Register any organisation which we consider is no longer a charity, and any charity which has ceased to exist or does not operate. We sometimes also have to consider the possibility that a body which has been registered as a charity has, in fact, been set up for illegal or improper purposes. If this is the case, we will remove the organisation from the online Register.

The online Register plays an important role in assuring the public of the legitimacy of organisations and promotes transparency of activities and details of charities. It is therefore important that trustees update their charity's details on a regular basis.

Trustees can use our online services to update their details. Further information about how to do this can be found on our [website](#).

## Avoiding problems - working with your umbrella body

Our casework demonstrates that charities often experience problems that could have been avoided or mitigated had the charity made use of the support of their umbrella body.

Umbrella bodies usually have a wealth of experience in guiding charities through common challenges, and can provide tailored advice to charities that experience difficulties. Some also offer legal support to their members.

Their support becomes increasingly important to charities as we as regulator step back from providing tailored support or advice to charities on issues that are within trustees' decision making remit. The case study below, based on a real case, demonstrates how important it is for charities to consult, and seriously consider, expert advice.

### Case study - An almshouse charity

The charity was principally made up of a permanent endowment in the form of almshouse properties. The properties had fallen into disrepair and the charity was not able to fulfil its objects. It was clear that action was needed to rectify the situation - either by an injection of funding or the sale of the properties, allowing the charity to use the resulting funds to advance its objects.

Before seeking expert advice, the charity made contact with the local authority, which suggested a funding grant based on the PLACE scheme ('Private Lease Agreements Converting Empties'). These schemes require participating properties to be leased for a period of 5 years as social housing for people on the Council's housing waiting list.

The trustees recognised that they did not have the power to enter into the arrangements imposed by the PLACE scheme, primarily because the charity's beneficiary class would not benefit from it. The charity would also have lost control of its properties for the period of the lease and faced legal issues regarding tenants' rights at the end of this lease.

However, the charity came to us to request that we grant powers to allow the charity to enter into the agreement. Realising that the trustees had not sought expert advice, we advised them to contact the Almshouse Association, which has considerable expertise in evaluating funding packages for almshouse refurbishment and offers a wide range of practical support.

However, having contacted the Association, the charity decided it did not want to take its advice and continued to put pressure on us to grant authorisation, which we were not able to do, given the information provided.

After some time, the trustees decided that a sale and re-provision project would be the best way forward. The delay is likely to have caused the charity considerable financial losses due to the deterioration/devaluation of its empty properties. It is also likely that the new approach will not provide the same level of support available to beneficiaries as a refurbishment would have done. Our interaction with the charity lasted nearly a year.

### Lessons from this case

The Almshouse Association offers a one-to-one service to members seeking funding packages for refurbishment. Most of the available packages do not require special authorisation - charities can enter into them without changing their objects.

Had the charity consulted the Almshouse Association for constructive support and advice at the outset, before entering into detailed negotiations with the local authority, it might have avoided the delay and frustrations it experienced. All trustees should consider how their charities might benefit from the support and advice of their respective umbrella body. This is especially the case where trustees are making decisions that are likely to have a momentous impact on the future of their charity.

The Commission is working in partnership with umbrella bodies, and will shortly be making a list of umbrella bodies available on our website. In the meantime, we would encourage trustees to talk to their peers and find out which umbrella body might be able to offer them most support and advice.

## Lessons from a principal regulator

### Background

On 1 June 2010, the Higher Education Funding Council for England (HEFCE) became the principal regulator of higher education institutions (HEIs) in England which it funds and which are exempt charities<sup>4</sup>. In the year to 31 July 2012<sup>5</sup> there were 110 such institutions, whose total income came to £22.6 billion. The smallest HEIs have incomes of around £7 million, the largest incomes of over £1 billion.

As a condition of funding, English HEIs are required to report to HEFCE all 'material adverse changes' such as significant threats to their financial position, significant and novel frauds, or major accounting breakdowns. On becoming principal regulator, HEFCE extended this obligation to include serious incidents affecting HEIs as charities. This includes incidents of harm to beneficiaries and terrorist or extremist activity serious enough to need the intervention of the police<sup>6</sup> or another regulator and which might harm the reputation of the institution itself, the higher education sector in general, or the wider charity sector.

### Serious incidents

As noted above, HEFCE extended a long-standing obligation for HEIs to report serious adverse changes in their circumstance to require exempt charity HEIs to report serious incidents in a way analogous to the Commission's requirement for registered charities (including HEIs).

Between 1 June 2010 and 31 March 2012 HEFCE has either identified or been notified of 28 serious incidents. These are summarised in the table below.

Category of incident	Number of reported incidents	
	01/06/2010 to 31/03/2011	01/04/2011 to 31/03/2012
Financial fraud	4	20
Data security failure	2	1
Harm to institutional reputation	1	-

4 Exempt charities are those identified in the Schedule 3 of the Charities Act 2011 and whose regulatory arrangements as charities are set out in Sections 22 to 28 of that Act.

5 All HEIs have the same accounting year: 1 August to 31 July

6 Many HEIs have daytime populations as large as towns: staff, students, contractors, visitors. HEFCE has tried to exclude from the reporting requirement incidents of 'petty' crime, disorderly behaviour or other perceived or actual nuisance by students away from campus, etc. unless the scale or frequency impact on the institution's reputation locally or nationally.

In all cases that have reached a conclusion, the institution was able to satisfy HEFCE that its own investigations and remedial actions were timely and effective. This will have included internal reporting to the institution's audit committee and, where appropriate the engagement of the police or, in the case of data loss or release, with the Information Commissioner. Some of the data security failures were reported in local or regional media, but without serious impact on the institution's reputation.

### **Example of reputational harm**

The highest profile incident was the involvement of the London School of Economics with Libya and, in particular, Saif al Gaddafi. This led to the resignation in December 2010 of the LSE's Director, who took responsibility for the harm to the School's reputation. The School itself commissioned an independent inquiry chaired by Lord Woolf, whose report was published in 2011 and which made recommendations that the School has accepted in full. HEFCE maintained contact with the School throughout that year and is satisfied that controls have been implemented to significantly reduce the risk of a similar incident occurring in future.

### **Examples of fraud in HEI charities**

The table above shows most incidents in both years were financial frauds. Of those, 11 involved third-parties who wrote to finance departments fraudulently trying to change the bank account details of genuine suppliers. Some of the attempts were blocked by HEIs' internal control systems, but HEFCE is aware of two cases where the fraud succeeded even after the HEIs had tightened their processes. In both of those the controls failed because relevant staff members were absent and their temporary replacements were not aware of the risk and/or the correct process. HEFCE knows that HEIs made payments to fraudulent bank accounts totalling £6.6 million. The actual losses were much less - some £450,000 - because of prompt action in response to secondary controls, cooperation from the clearing banks and, in some instances, successful insurance claims. HEFCE worked with HE sector finance professionals to raise awareness and tighten controls, and with the Commission to alert the wider charity sector.

The other frauds reported - where a value could be identified - totalled £1.6 million. Some £800,000 of this was reported to HEFCE by an institution that is a registered charity and led eventually to the conviction of the finance director who had abused her position of trust and power to perpetrate several different frauds over many years. It was reported to HEFCE in their role as funder, rather than principal regulator, but their need to consider broad issues of accountability and governance at the institution meant HEFCE engaged closely with both senior management and members of the governing body (the trustees). The institution made a serious incident report to the Charity Commission. However, rather than the Commission investigating, HEFCE agreed to keep its compliance team informed about its engagement with the institution and its response to the incident. The Commission accepted HEFCE's assessment of the institution's actions and did not take action of its own. This was a good example of co-regulators working together to reduce duplicate regulatory action.

## D. Annexes - Key statistics from the Commission's investigatory work - 2011-12

### Annex 1 - Investigations and Enforcement performance headlines and impacts 2011-12

Performance headlines	2011-12	2010-11	2009-10	2008-09	2007-08
Number of new Assessment cases opened	1252	1845	2434	1504	988
Number of Assessment cases closed	1374	1912	2615	848	799
Number of new Investigations opened <sup>7</sup>	54	144	180	168	170
Total number of Investigations closed	85	167	121	188	200
Number of Statutory Inquiries opened	12 <sup>8</sup>	3	9	19	19
Number of Statutory Inquiries closed	9	9	15	21	29
Average duration of closed Statutory Inquiries (days)	715	519	395	358	414
Number of Statutory Inquiries closed which had significant involvement from other regulators	0	0 <sup>9</sup>	2	5	5
Average duration of closed Statutory Inquiries involving other regulators (days)	N/A	N/A	703	457	351
Number of Statutory Inquiry Reports published	43 <sup>10</sup>	13	15	23	42
Percentage of Statutory Inquiry Reports published within 3 month target	95%	81% <sup>11</sup>	80%	74%	31%
Number of Regulatory Case Reports	12 <sup>12</sup>	8 <sup>13</sup>	5	4	-
Number of new Regulatory Compliance Cases opened	42	141	171	149	153
Number of Regulatory Compliance Cases closed	76	156	106	167	171
Average duration of closed Regulatory Compliance Cases (days)	282	172	162	158	149
Number of active Investigations at year end	64	119	140	77	104
Number of new monitoring cases opened	72	276	306	211	-
Number of monitoring cases closed	215	297	141	81	-
Number of monitoring visits	12	21	20	14	-
Number of Accounts Scrutinies carried out	203	277	236	320	-

7 ie the total number of statutory inquiries and regulatory compliance cases.

8 Investigations and Enforcement only investigate issues of the most serious concern under Statutory Inquiries. Therefore Investigations and Enforcement only open Statutory Inquiries.

9 There were also 2 regulatory compliance cases closed during 2010 - 11 where there were delays because of the involvement of other regulators.

10 We published 7 reports of Statutory Inquiries in 2011-12. In total, these reports covered 43 inquiries, as some reports covered more than one inquiry and thus more than one charity."

11 During both 2010-11 and 2011-12, Regulatory Case Reports were also included within the target to publish all reports within three months of the end of the substantive investigation.

12 We published 6 RCRs in 2011-12. In total, these reports covered 12 regulatory compliance cases, as some reports covered more than one case and thus more than one charity.

13 These relate to investigation cases only.



<b>Performance Impacts</b>	<b>2011-12</b>	<i>2010-11</i>	<i>2009-10</i>	<i>2008-09</i>	<i>2007-08</i>
Charity assets directly protected in our investigation work	<b>£5m</b>	<i>£8m</i>	<i>£29m</i>	<i>£47m</i>	<i>£16m</i>
Charity income directly overseen through either Statutory Inquiry or Regulatory Compliance Cases	<b>£255m</b>	<i>£900m</i>	<i>£521m</i>	<i>£461m</i>	<i>£106m</i>
Number of cases where Commission action protected vulnerable beneficiaries	<b>6</b>	<i>49</i>	<i>20</i>	<i>30</i>	<i>9</i>
Number of cases protecting the reputation of individual charities	<b>20</b>	<i>71</i>	<i>50</i>	<i>70</i>	<i>38</i>
Number of cases protecting the reputation of the sector	<b>27</b>	<i>49</i>	<i>35</i>	<i>41</i>	<i>27</i>
Number of cases dealing with issues arising from conflicts of interest	<b>6</b>	<i>20</i>	<i>19</i>	<i>21</i>	<i>26</i>
Number of cases where advice and guidance provided to ensure the charity's governance improved	<b>26</b>	<i>59</i>	<i>43</i>	<i>47</i>	<i>61</i>
Number of cases involving concerns about fundraisers	<b>5</b>	<i>11</i>	<i>8</i>	<i>11</i>	<i>9</i>
Number of cases where an internal dispute was resolved and the charity is properly functioning again	<b>7</b>	<i>10</i>	<i>11</i>	<i>21</i>	<i>11</i>
<i>Charity no longer operating or applying funds outside its trusts<sup>14</sup></i>	<b>17</b>	<i>8</i>	<i>-</i>	<i>-</i>	<i>-</i>
<i>Useful and effective regulatory advice and guidance given</i>	<b>49</b>	<i>91</i>	<i>-</i>	<i>-</i>	<i>-</i>
<i>Charity is now complying with the legal requirements</i>	<b>1</b>	<i>2</i>	<i>-</i>	<i>-</i>	<i>-</i>
<i>Greater transparency in the charity's operations and published reports and accounts</i>	<b>1</b>	<i>3</i>	<i>-</i>	<i>-</i>	<i>-</i>
<i>Moribund charity is now functioning</i>	<b>0</b>	<i>0</i>	<i>-</i>	<i>-</i>	<i>-</i>
<i>Charity's relationships with third parties is now properly managed in the best interests of the charity</i>	<b>1</b>	<i>1</i>	<i>-</i>	<i>-</i>	<i>-</i>
<i>Direct charitable expenditure has increased or targets are in place to increase this expenditure</i>	<b>0</b>	<i>0</i>	<i>-</i>	<i>-</i>	<i>-</i>
Number of occasions where Commission's statutory regulatory powers were used, including use of information gathering powers	<b>188</b>	<i>208</i>	<i>514</i>	<i>707</i>	<i>490</i>

These impacts relate to investigation cases closed during the year.

<sup>14</sup> This indicator and the following six indicators were first introduced in 2010-11.

## Performance Indicators ('KPIs')

We report on the performance of our investigations and related regulatory work using a number of indicators as defined below:

Performance is divided into three areas:

- Detection
- Investigation, Sanction and Redress
- Prevention and Deterrence

### Detection

	Target	Achievement
Complete 90% of compliance assessments correctly in 30 working days	90%	77%
Carry out a minimum number of compliance visits annually, to charities which are subject to monitoring and identified following a risk assessment	20 visits (Compliance unit target).	10 visits during the first eight months year
	6 visits (Investigations and Enforcement target).	2 visits during the final four months of the year

### Investigation, Sanction and Redress

	Target	Achievement
Complete all regulatory compliance cases (excluding statutory inquiries) within an average of six months	183 days	282 days
Ensure 90% of all investigations result in at least one of the specified beneficial impacts (see Annex 1) which protect charities from mismanagement, misconduct or abuse	90%	94%

### Prevention and Deterrence

	Target	Achievement
Publish 90% of reports on the results of investigations within three months of the end of the substantive investigation process	90%	95%
Publish an annual report on the 'Themes and Lessons from the Charity Commission's Compliance Work' which includes the duration of each statutory inquiry, the impact of investigations, the use of sanctions (including legal powers of remedy and protection), and the operation of our investigatory work	Publish report before end of third quarter of financial year.	Published 22 September 2011

## Annex 2 - Published statutory inquiry reports 2011-12

This table highlights key issues of concern in these investigation cases; notes the use of Charity Commission powers; and records the overall duration of investigations.

CHARITY	ISSUES <sup>15</sup>											STATUTORY POWERS							Statutory inquiry durations <sup>16</sup>		
	Accounting issues	Disputes	Fraud allegations	Fund-raising	Governing document compliance	Land/Property	Political activities	Terrorism allegations	Trading/commercial	Trustee benefits/conflicts of interest	Trusteeship and governance issues	vulnerable beneficiaries	Orders/Directions for information/evidence	Suspend trustees, officers etc	Remove trustees, officers etc	Freeze bank accounts	Interim manager	Direct Trustees to Act	Other Orders + schemes	No powers used	Months
Al Ikhlas (1047844) <sup>17</sup>				✓	✓						✓	✓									Not applicable - Supplementary report.
Alzheimer's UK Research Education and Care Ltd (1115434)				✓	✓						✓	✓			✓				✓		22.9 months
Brent Educational and Recreational Support Youth Challenge (BEARS) (former registered charity number 1057993) and Gate Lane Community (former registered charity number 1106853)	✓		✓		✓					✓	✓	✓	✓		✓	✓			✓		28.8 and 4.2 months respectively.
Brotherhood of the Cross and Star Limited (270034)		✓			✓	✓					✓	✓			✓	✓			✓		22.7 months
Crescent Relief (1087724)	✓				✓			✓		✓		✓			✓			✓	✓		36.5 months
Report published into charities awarded grants by Big Lottery Fund	✓		✓		✓					✓	✓	✓	✓	✓	✓				✓		Various
The Needy Children International Foundation (1117654)				✓							✓	✓									27.6 months
TOTALS	3	1	2	3	6	1	0	1	0	2	7	0	7	2	1	5	2	1	5	0	

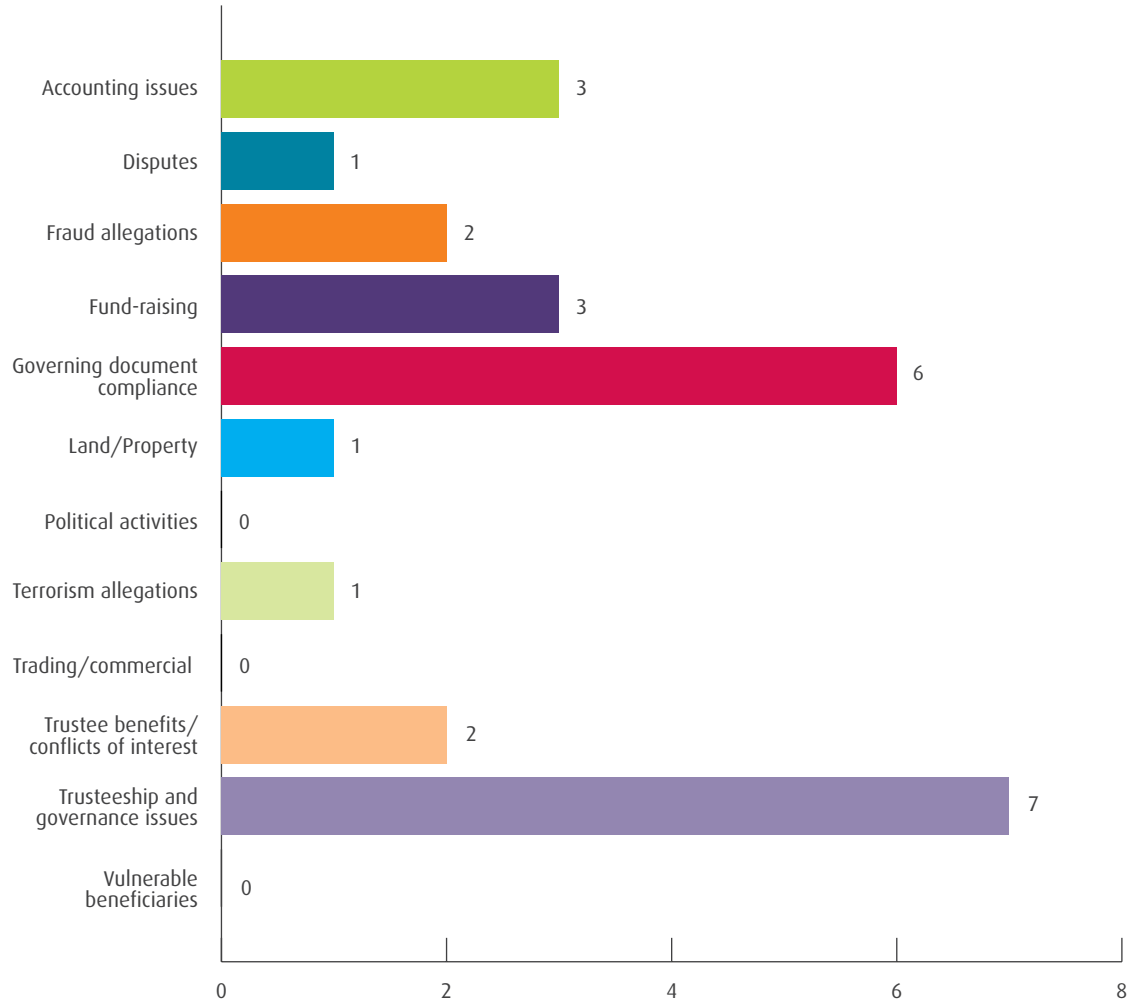
15 The issues noted within this chart detail the concerns that the investigations examined, it is not necessarily the case that these concerns were upheld.

16 The case duration shown in this column is the **total** period from the opening of a statutory inquiry to the date on which the substantive inquiry was closed, disregarding any delay which may have been related to the work of other regulators or legal proceedings or other external factors.

17 Following attempts to confirm with the trustees that the charity had ceased to operate, the Commission removed Al Ikhlas from the Register under s.3(4) of the Charities Act 1993 (s.34(1)(a) of the Charities Act 2011), when no response to our communications was received.

## Annex 2.1 - Published statutory inquiry reports - the type and frequency of issues of concern

Note that most statutory inquiries involve more than one issue.<sup>18</sup>

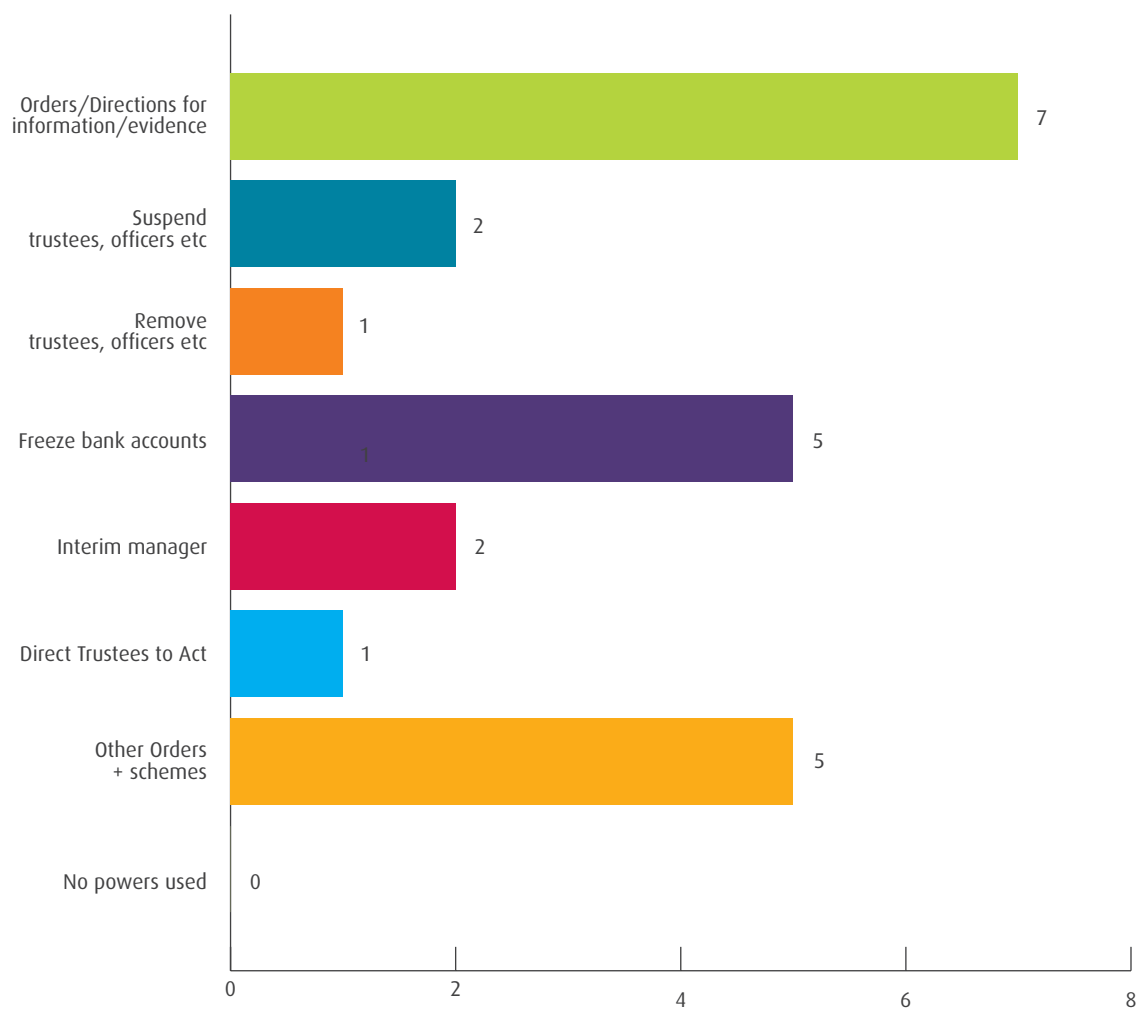


Baseline: seven reports

<sup>18</sup> The category 'Trusteeship and Governance issues' includes issues such as: suitability, eligibility, management controls, financial controls, non co-operation of trustees, and dominant trustee.

## Annex 2.2 Published statutory inquiry reports - the frequency of use of different Charity Commission powers

Note that more than one power is used in most cases.



Baseline: seven reports

## Annex 3 - Regulatory Case Reports (RCRs) 2011-12

We publish RCRs on our investigations where there is significant public interest in the issues involved and the outcome, and where there are lessons that other charities can learn from. The criteria we apply when deciding whether to publish a report is set out on our [website](#).

CHARITY	ISSUES <sup>19</sup>											POWERS			Regulatory Compliance Case durations <sup>20</sup>	
	Accounting issues	Disputes	Fraud allegations	Fund-raising	Governing document compliance	Land/Property	Political activities	Terrorism allegations	Trading/commercial	Trustee benefits/conflicts of interest	Trusteeship and governance issues	Vulnerable beneficiaries	Orders/Directions for information/evidence	Other Orders + schemes	No powers used	Months
Association for Reaching and Instructing Children in Africa (1079952)	✓									✓	✓	✓			✓	14.2 months
Charitable funds held in the name of 'Sunrise Radio South East Asia Disaster Appeal'				✓									✓			5.5 months
The Knotty Ash Special School Trust (Now known as Bright Park) (526085)						✓					✓			✓		4.9 months
Plymouth Argyle Supporters Training and Development Trust (1056117)					✓					✓	✓				✓	6.9 months
Regulatory report into seven organisations (various) <sup>21</sup>			✓												✓	Various
Wildlife Aid (297610)						✓				✓	✓				✓	6 months
<b>TOTALS</b>	<b>1</b>	<b>0</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>2</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>3</b>	<b>4</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>4</b>	

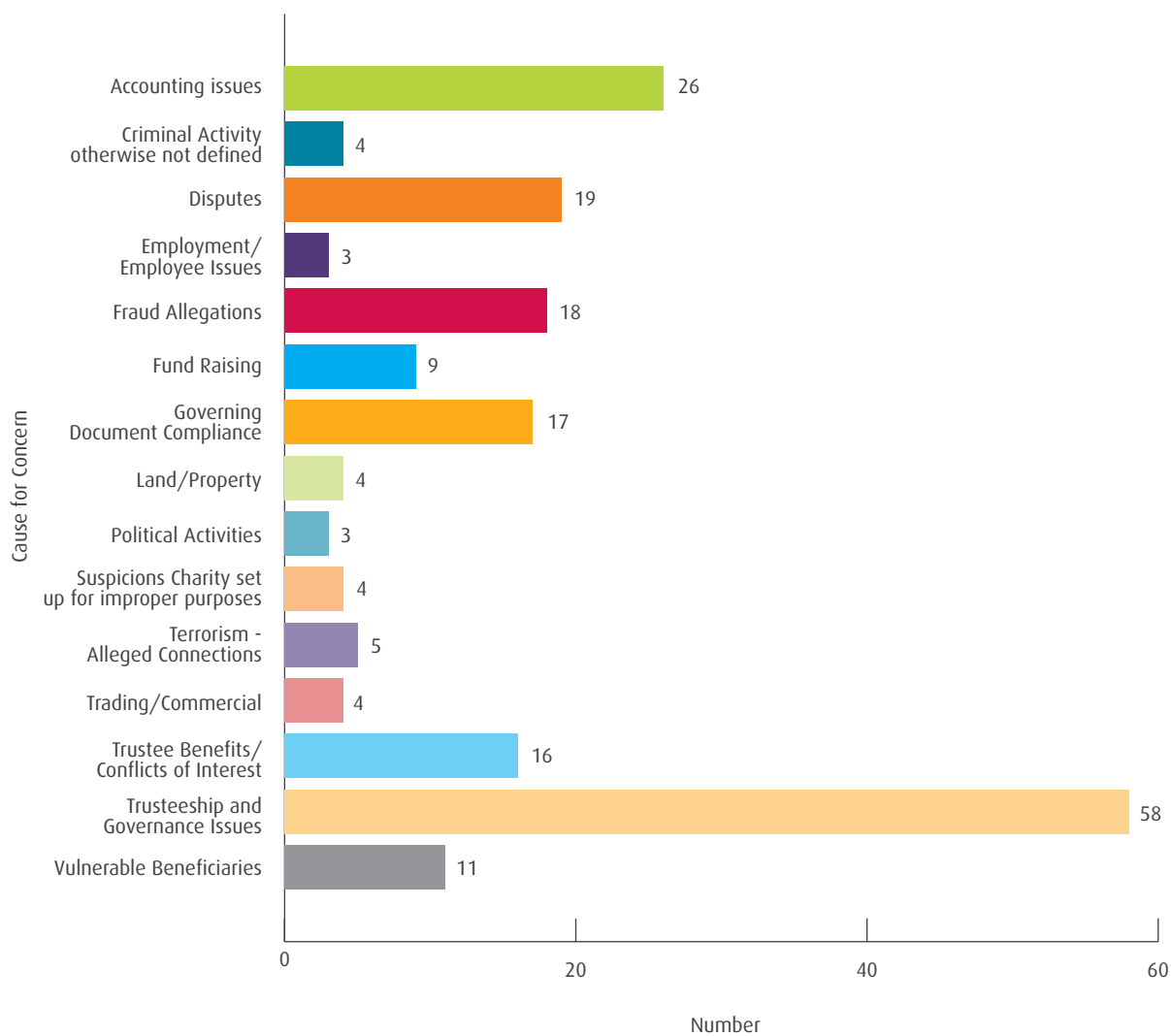
19 The issues noted within this chart detail the concerns that the investigations examined, it is not necessarily the case that these concerns were upheld.

20 The case duration shown in this column is the **total** period from the opening of a Regulatory Compliance Case, to the date on which the substantive investigation was closed, disregarding any delay which may have been related to the work of other regulators or legal proceedings or other external factors.

21 Section 3(4) of the Charities Act 1993 (s.34(1)(a) of the Charities Act 2011) places a statutory obligation on the Commission to remove from the Register any institution which it no longer considers is a charity and any charity which has ceased to exist or does not operate. The Commission removed the seven organisations from the Register in March 2011.

## Annex 4 - Investigations completed 2011-12 - the type and frequency of issues of concern

Note that most cases involve more than one issue.<sup>22</sup>

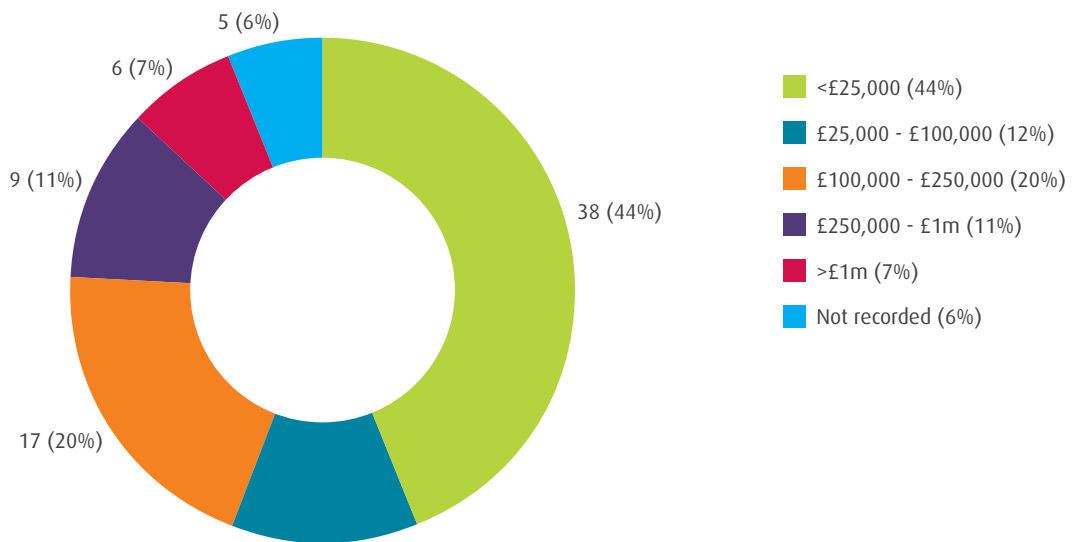


Baseline: 85 investigations

<sup>22</sup> The category 'Trusteeship and Governance issues' includes issues such as: suitability, eligibility, management controls, financial controls, non co-operation of trustees, and dominant trustee.

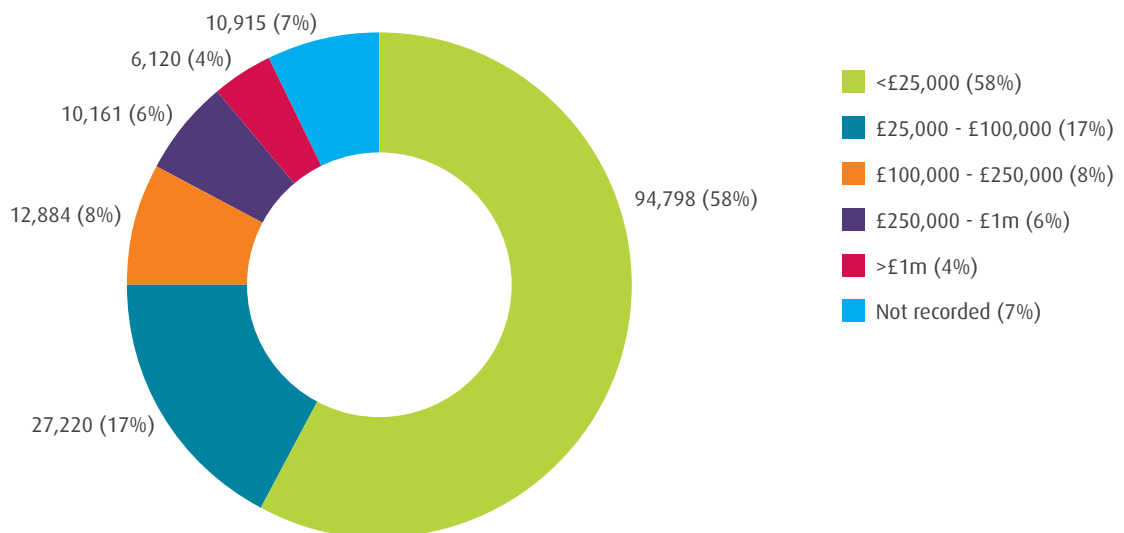
## Annex 5 - Investigations 2011-12 - the number of charities by income band <sup>23</sup>

### Cases by income of charity



Baseline: 85 charities

### Sector-wide income



Baseline: 162,098 charities

<sup>23</sup> Income may not be recorded for a variety of reasons, such as the charity is non-compliant, or is newly registered and so has not been required to submit accounts.

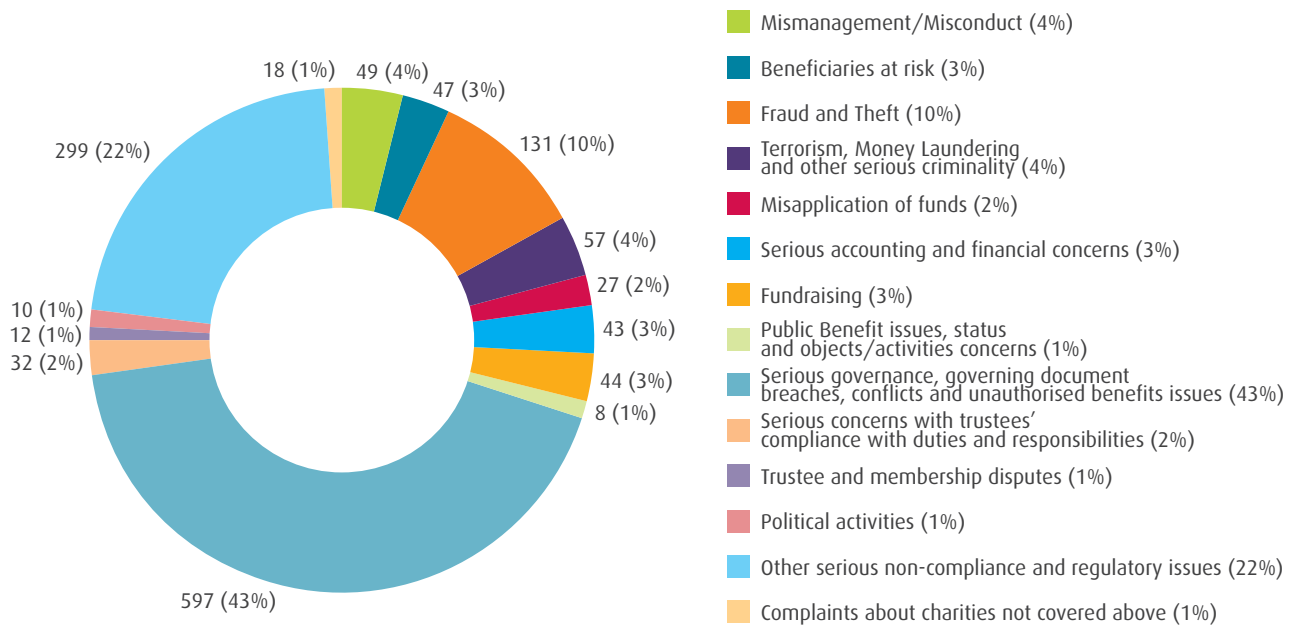


## Annex 6 - Use of Commission powers in all compliance cases 2011-12

All Statutory Inquiry and Regulatory Compliance Cases - breakdown of the number of individual Orders or Directions under the Charities Act 1993	2011-12	2010-11	2009-2010	2008-09	2007-08
S8 (3) - (a) Furnish information/answers	2	0	11	9	40
S8 (3) - (b) Furnish copies/documents	0	2	4	3	25
S8 (3) - (c) Attend and give evidence	0	0	11	7	5
S9 (1) - (a) Furnish information	21	18	94	75	50
S9 (1) - (b) Furnish copies/documents	74	140	288	543	246
S18(1) - (i) Suspend trustee, officer, etc.	1	1	1	1	7
S18(1) - (ii) Appoint additional trustee	0	0	1	1	3
S18(1) - (iii) Vest property in the Official Custodian for Charities	1	0	22	1	0
S18(1) - (iv) Not to part with property	2	4	12	11	18
S18(1) - (v) Not to make payment	0	1	0	0	0
S18(1) - (vi) Restrict transactions	2	5	7	0	10
S18(1) - (vii) Appoint Interim Managers	0	1	2	2	2
S18(2) - (i) Remove trustee, officer, etc.	0	0	0	1	6
S18(2) - (ii) Establish a scheme	0	0	0	1	0
S18(5) Appoint trustee(s)	11	3	11	11	9
S19 (a) Specific Direction to protect charity	8	4	7	4	0
S26 Regulatory consent	24	8	9	9	8
Others (including Discharge Orders)	42	21	34	28	61
<b>TOTAL</b> Orders/Directions issued in period	<b>188</b>	208	514	707	490

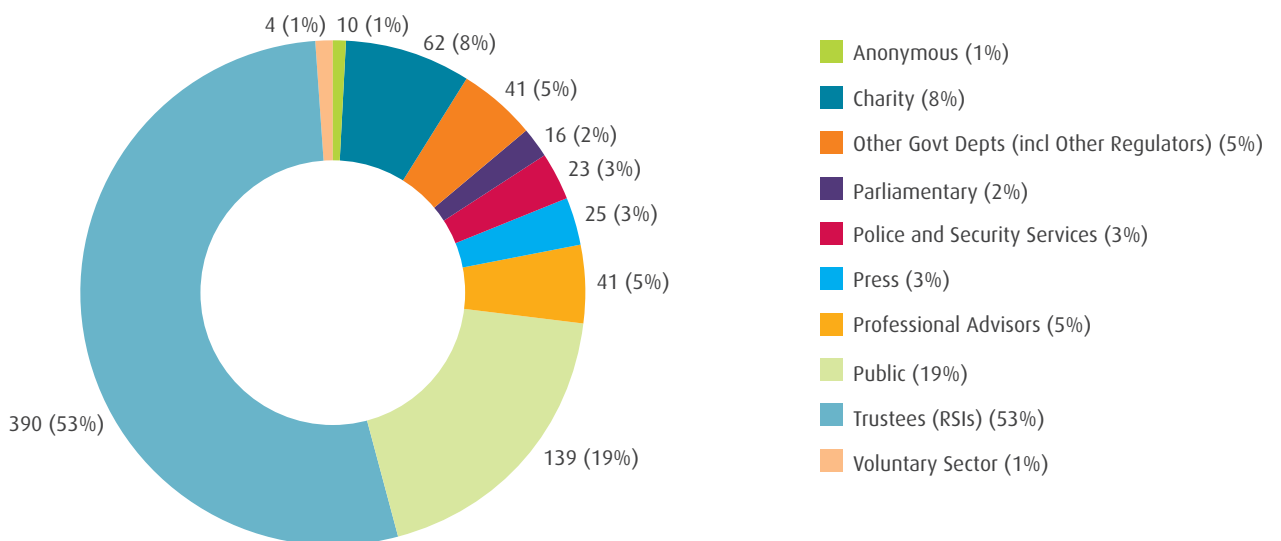
## Annex 7 - Analysis of all completed assessment cases 2011-12

### Annex 7.1 - Causes of serious concern dealt with by our Investigation and Enforcement function



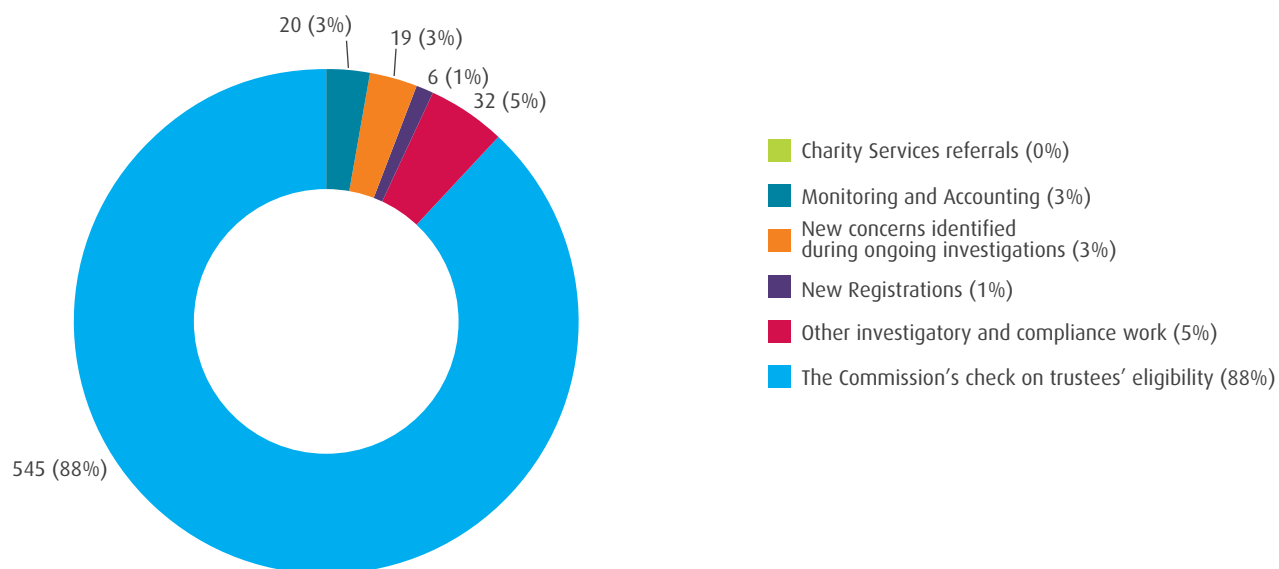
Baseline: 1,374 completed assessment cases.

### Annex 7.2 - Sources of serious concern - external sources



Baseline: 751 cases

## Annex 7.3 - Sources of concern - identified proactively by the Commission



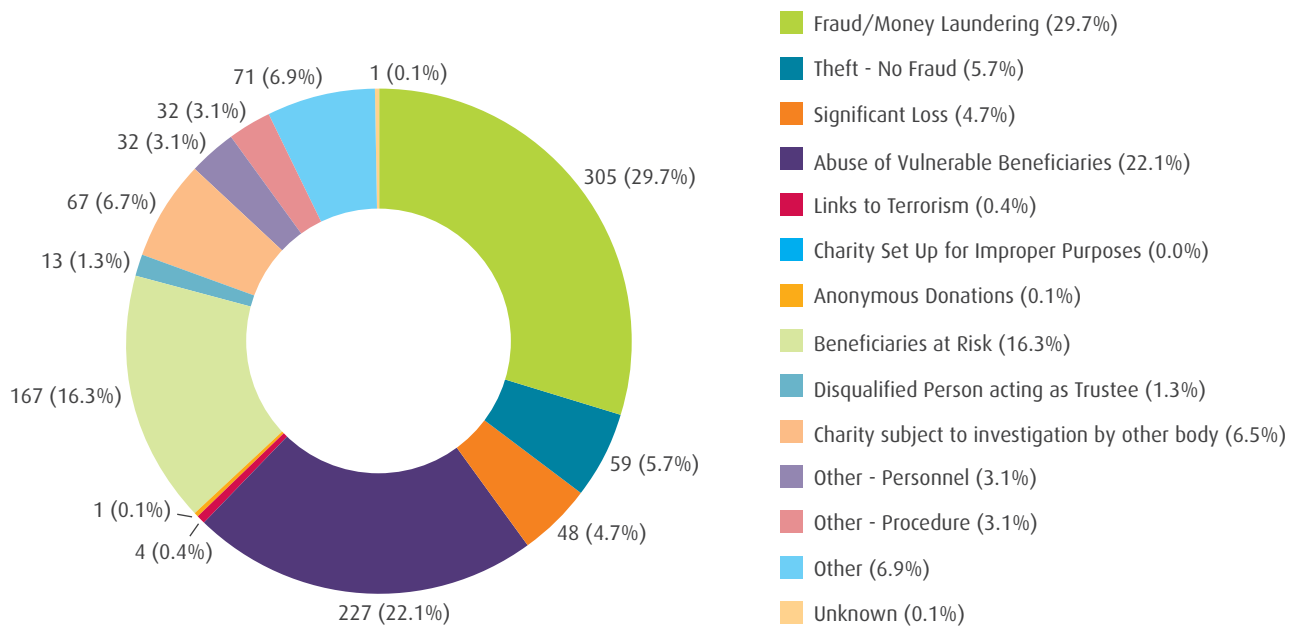
Baseline: 623 cases

## Annex 8 - Reported concerns about charities 2011-12

### Annex 8.1 - Reports of Serious Incidents

The following chart shows the principal issue only.

#### Reports of Serious Incidents: Issues identified during 2011-12



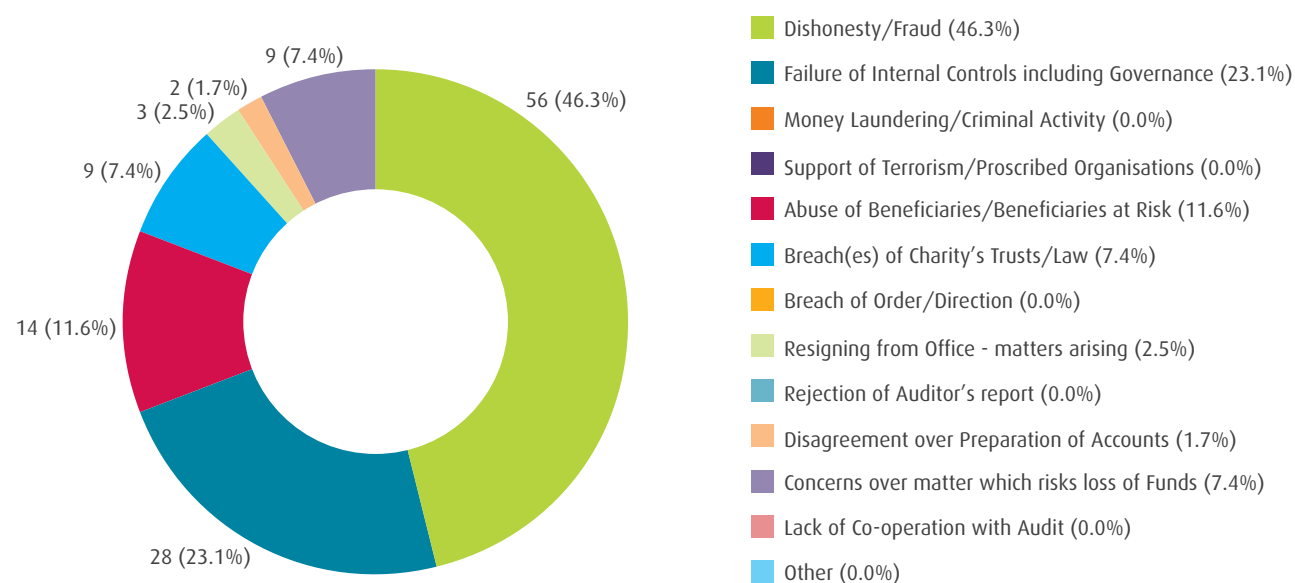
Baseline 1,027<sup>24</sup>

<sup>24</sup> The figures here show individual reports. Some charities reported RSIs in batches, so some "completed assessment cases" (Annex 7.2) were in fact concerned with multiple reports by individual charities.

## Annex 8.2 - Whistleblowing reports

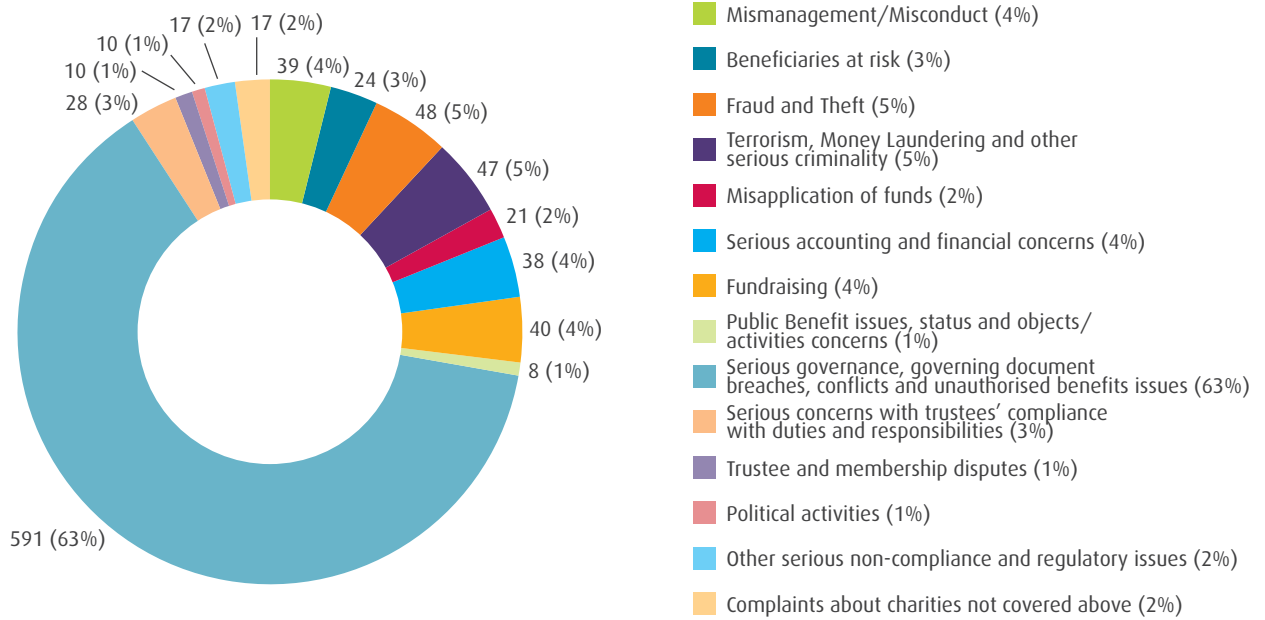
There were 121 Whistleblowing reports received by the Commission in the year (53 last year), the majority of which were dealt with by the Assessment Unit. The key issues in these reports were as follows, showing the principal issue only.

### Whistleblowing: Issues identified during 2011-12



Baseline: 121 reports

## Annex 8.3 - Concerns about charities identified or reported from other sources



Baseline: 938 completed assessment cases.





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