

The collapse of Kids Company: lessons for charity trustees, professional firms, the Charity Commission and Whitehall – Public Administration and Constitutional Affairs Committee Report

On 1 February 2016 the Public Administration and Constitutional Affairs Committee (“PACAC”)¹ published its report entitled “The Collapse of Kids Company: lessons for charity trustees, professional firms, the Charity Commission and Whitehall” (“the Report”).

Keeping Kids Company (known as “Kids Company”) was founded in 1996 by the high profile and well connected Camila Batmanghelidjh. Camila Batmangelidjh was also the charity’s CEO. The charity’s chair of the past 12 years was the well known television executive and presenter, Alan Yentob, who was until December 2015 the BBC’s Creative Director.

Kids Company, a registered charity with charitable objects for preservation of health for children and young people in need of counselling, support and therapeutic use of the arts by reason of their social or family circumstances, closed on 5 August 2015. Kids Company closed on the same day as the launch of a police investigation into allegations of sexual abuse at the charity.² The closure and the investigation of Kids Company also coincided with the payment to the charity of £3 million of Government funding, which was intended to enable an emergency restructure of the charity amid concerns about the governance of the charity and its financial mismanagement.

Over the course of its existence, successive governments provided Kids Company with grants of at least £42 million and allowed Camila Batmanghelidjh privileged access to Ministers. In making such grants, governments failed to carry out adequate due diligence and released the charity from the competitive processes to which other charities are subject.

In response to contact from Kids Company’s management and negative press coverage, the Charity Commission did discuss with the charity its finances at several points during the year leading up to its collapse. However, the Charity Commission did not open a formal statutory inquiry until 21 August 2015, more than two weeks after the charity’s closure³. At the time of writing this paper, publication of the Charity Commission’s inquiry report is awaited.

The PACAC confirms that “Our prime purpose of this Report is to identify lessons to be learned from the collapse of Kids Company”⁴. The full Report is 68 pages long and can be downloaded from the link below. The purpose of this paper is to highlight the Report’s key recommendations and the implications not only for charity trustees but also for auditors and other professional advisers, for

¹ The PACAC is appointed by the House of Commons whose function is, amongst other things, to consider matters relating to the quality and standards of administration provided by civil service departments, and other matters relating to the civil service; and to consider constitutional affairs.

² On 28 January 2016 the Metropolitan Police announced that the investigation had been dropped after confirming that there was no evidence to “justify a referral to the Crown Prosecution Service”.

³ The Charity Commission can only use its wide ranging powers to call for information/documentation and instigate its protective powers once a formal statutory inquiry has been opened.

⁴ Paragraph 4 of the Report

the Charity Commission and for Government.

Link to the Report:-

<http://www.publications.parliament.uk/pa/cm201516/cmselect/cmpubadm/433/433.pdf>

Charity trustees

Ultimate responsibility

The Report confirms that “Primary responsibility for Kids Company collapse rests with the charity’s Trustees”⁵ - the legal position being that it is the trustees of a charity who are ultimately responsible for the management and control of their charity. In other words “the buck stops with them.”⁶

The Report also serves as a reminder to charity trustees that governance of their charity cannot be delegated to the chair of trustees or to specific trustees (unless done so in accordance with any provision in the charity’s governing document or agreed delegated authority). This is the case irrespective of (a) the position that a chair or other trustee may hold outside the charity and (b) how influential and/or domineering he/she may be either in connection with the charity or in his/her field of work. It should also be remembered that members of the trustee body are collectively responsible for the governance of their charity and thus they may find themselves personally liable in relation to any loss arising from any breach of duty or responsibility.

Neither should charity trustees let the lines become blurred between their role and responsibilities and those who are not charity trustees: eg the charity’s founder, CEO, patron or president. The Report reminds trustees that they must not allow their judgment as trustees to be swayed by the personality, charisma or connections of others. The Report recognises that so called “founder syndrome” is not uncommon in charities. This often occurs where the founder’s passion for his/her charity is so dominant that it overshadows sound judgment and decision making and prevents the trustees from acting in the best interests of their charity.

How do charity trustees ensure that they are fulfilling their duties and responsibilities?

As the regulator for charities, the Charity Commission has numerous statutory objectives and functions, including (a) the objective to promote compliance by charity trustees with their legal obligations in exercising control and management of the administration of their charities and (b) the function of encouraging and facilitating the better administration of charities. To this end, the Commission has power to give such advice or guidance (general or specific) as it considers appropriate.

Consequently, the Charity Commission publishes a host of guidance documents for trustees in order to help them fulfil their duties and responsibilities. While extremely comprehensive, the sheer number of such guidance documents can be daunting, even for the most seasoned charity trustee. In my view, greater clarity is needed from the Commission regarding which of the many guidance

⁵ Second paragraph of the Introduction to the Report.

⁶ The legal duties and responsibilities of charity trustees are wide ranging. The key duties and responsibilities are summarised in the Charity Commission’s guidance CC3 entitled *The essential trustee: what you need to know, what you need to do*.

documents are regarded as key guidance and thus relevant to all charity trustees. Having said that, it is encouraging to note that in its press release on 29 January 2016⁷, the Charity Commission confirmed that it will be undertaking a full review of its guidance later this year.

Since publication of the Report there has been commentary in the media and from those involved in the charity sector as to what additional help or assistance charity trustees might need in the light of the Report's findings. On the day that the Report was published, Sir Stephen Bubb, Chief Executive of the Association of Chief Executives of Voluntary Organisations ("ACEVO") said that a "Centre for Charity Excellence" should be established as it was feared that hundreds of charities will cease to function unless good governance and leadership are bolstered. As details of this, and other, proposals are as yet unclear, it is difficult to comment on their desirability and/or potential efficacy.

However, irrespective of the proposals referred to in the above paragraph, charity trustees should act now to ensure that their "houses are in order" and take specialist advice as they consider appropriate. Various tools that charity trustees might utilise to assist them fulfil their governance responsibilities include (a) the Charity Commission online guidance, (b) induction/trustee training packs, (c) external trustee training courses or a combination of all of the aforementioned.

The need to have trustees with relevant expertise

The Report recommends that in order to fulfil their duties and responsibilities as trustees (especially with regard to financial controls and the appropriateness of significant expenditure), charities of Kids Company's size and complexity should have trustees with relevant expertise in the field in which they operate and that the Charity Commission should consider how it can better impress this need upon charities.

While the above seems like an eminently sensible suggestion on the face of it, in my view one does have to remember the voluntary nature of charity trusteeship and the difficulties that charities sometimes encounter when trying to retain and/or recruit new trustees.

Managing charity finances and reserves

The Report highlights failures in Kids Company's financial management procedures, not least the lack of sufficient reserves. It concluded that:

"Trustees must have ultimate responsibility for ensuring that a charity has a responsible approach to reserves but the Charity Commission must do more to help to make Trustees aware of their responsibilities in this area."⁸

In fact three days before publication of the Report, on 29 January 2016, the Charity Commission issued a press release confirming that it had updated three sets of guidance:-

- *Managing a charity's finances: planning, managing difficulties and insolvency (CC12);*
- *Charity Reserves: building resilience (CC19);* and
- *Charity governance, finance and resilience: 15 questions trustees should ask.*

⁷ See the section below headed "Managing Charity Finances and Reserves" for further details of the Charity Commission press release.

⁸ Paragraph 110 of the Report

In the press release, Sarah Atkinson, Director of Policy and Communications at the Charity Commission, stated:-

“These guidance updates are designed to help trustees make the right call and support them, not to overburden them. That’s why there are also guides on how to set a good reserves policy for small and large charities. As regulator there is a limit on how much we can do as these are individual decisions for trustees to make. But these tools will help them manage any difficulties properly and with confidence.”

The press release and the three updated sets of guidance can be downloaded from the link below:-

<https://www.gov.uk/government/news/trustees-must-engage-with-finance-guidance-says-charity-regulator>

Charity accounts

The Report states that Kids Company was “wrong to take comfort”⁹ from the fact that the charity had 19 years of statutory audits. In the audited accounts the charity was signed off as a going concern, but there were repeated warnings from the auditors about the precariousness of the charity’s finances and its dependency upon future government grants.

The Report therefore serves as a warning to trustees that audited accounts do not necessarily give the charity a clean bill of health. Charity trustees must consider carefully and action accordingly any advice or warnings given by the charity’s auditors, whether in the form of a formal management letter or otherwise. Furthermore, it must be remembered that statutory accounts are audited and published long after the event and do not show the current state of a charity’s finances.

Use of professional advisers

A salutary warning is also given to charity trustees about the use of professional advisers in that they “are no substitute for the exercise of judgement.”¹⁰ Three firms of chartered accountants (Kingston Smith LLP, PKF Littlejohn LLP and PricewaterhouseCoopers LLP) were engaged at various stages by Kids Company. The Report confirms that although all three professional firms identified matters of concern, not one of them reported the scale of the risk carried by the charity to the trustees, the Cabinet Office or to the Charity Commission. The Report observes that:-

“They [the professional advisers] tend to limit the scope of the terms of their investigation in order to limit their own exposure to risk. In this case, they were able to avoid making any examination of the wide issues that threatened the charity’s existence. In the partial assurances they offered, the resulting reports may actually have obscured more than they revealed to those who read them.”¹¹

⁹ Paragraph 21 of the Report

¹⁰ Paragraph 98 of the Report

¹¹ Paragraph 98 of the Report

Safeguarding issues and increased statutory regulation

Not all of the facilities of Kids Company were registered with specialist regulators and thus not subject to inspection and scrutiny by those regulators. In the light of this, the Report concludes that:

“There is a strong case for statutory regulation of charities who have safeguarding responsibilities for children or vulnerable adults and we recommend that the Government considers how such regulators as Ofsted and the Care Quality Commission can assume these responsibilities as quickly as possible.”¹²

If the above recommendation is adopted, charities which are not currently registered with and regulated by Ofsted and/or the Care Quality Commission may need to do so.

Auditors

The Report reminds auditors of charity accounts that they have a duty pursuant to section 156 of the Charities Act 2011 to report a matter to the Charity Commission if during the course of an audit, the auditor has reasonable cause to believe that a matter has arisen which will have material significance for the Charity Commission in relation to the Commission’s power to institute a statutory inquiry and power to act for the protection of charities.¹³

The Report recommends that the Charity Commission amends its guidance to auditors so that the duties of auditors pursuant to section 156 of the Charities Act 2011 are appropriately conveyed.

Charity Commission

Guidance

As mentioned above, the Report recommends that the Charity Commission (a) revises its guidance (i) on charity reserves (which it has already done) and (ii) to auditors regarding their reporting duties to the Charity Commission and (b) considers how it can better impress upon trustees the need to ensure that the Board includes those with appropriate experience in areas relevant to the charity’s activities.

The Charity Commission’s involvement prior to closure of Kids Company

The Report also focuses on the Charity Commission’s rather limited involvement, in the circumstances, with Kids Company before its closure. The Report indicates that there are various reasons for this including the fact that the Charity Commission seems to have been (erroneously) comforted by the charity’s close connections with Government and its Ministers. The Report then goes on to say that the Charity Commission “must make its own judgment about a charity, rather than simply relying on government engagement with an organisation as evidence of a charity’s good governance and effectiveness.”¹⁴

Another factor identified in the Report which contributed to the Commission’s limited involvement, is the number of witnesses who had grave concerns about the charity but did not alert the Charity

¹² Paragraph 155 of the Report

¹³ Paragraph 77 of the Report

¹⁴ Paragraph 106 of the Report

Commission. This is important because if the Charity Commission had received more complaints it may well have opened a formal inquiry and been able to institute protective measures to change the operating model of the charity before it was too late. The Report recommends that the Charity Commission must do more to (a) make members of the public aware that they can and should take their concerns about a charity to the Commission and (b) encourage journalists to make formal complaints to the Commission.

Additional powers

The Charities (Protection and Social Investment) Bill (which at the time of writing is awaiting Royal Assent following which it will become an Act of Parliament), will give the Charity Commission additional protective powers. These include a new power to remove a charity trustee and disqualify a person from, in the future, either holding office as a charity trustee or holding a senior management position within a charity. Currently, the Charity Commission can only remove a trustee or officer of a charity (a) in specified circumstances set out in the Charities Act 2011 (e.g. if a trustee becomes bankrupt or he/she is incapable of carrying out his/her role as trustee because of a mental disorder)¹⁵ or (b) by instigating its protective powers following the opening of a statutory inquiry.¹⁶ The Report welcomes the new powers set out in the Bill and recognises that when enacted, the powers may be applicable to Kids Company in that the trustees of the charity might be prohibited from accepting roles as charity trustees and senior management positions within charities in the future.

Review of charity accounts

The proposals in this regard are set out below:-

“While it is not be possible for the Charity Commission to interrogate deeply the 60,000 sets of accounts it reportedly receives from charities each year, high risk charities – those with a large number of employees or a vulnerable client base – must be under greater scrutiny. We await with interest the Charity Commission’s technology transformation plan¹⁷, which would enable the Charity Commission to scrutinise high risk charities.”¹⁸

Future funding

Crucially, the Report recommends that the Treasury and Cabinet Office address the future funding of the Charity Commission “so that it can carry out its functions in the way that Government, charities and the public expects.”¹⁹

Charity Commission’s response to the Report

¹⁵ Sections 80 to 85 of the Charities Act 2011

¹⁶ Sections 76 and 79 of the Charities Act 2011

¹⁷ In January 2015 the National Audit Office approved the Charity Commission’s transformation programme. The programme includes improvements to the Commission’s business processes, supported by technology and culture change. There are two strands: implementing risk-regulation and increasing the digitisation of the Commission’s services.

¹⁸ Paragraph 109 of the Report

¹⁹ Paragraph 122 of the Report

In its response to the Report, also published on 1 February 2016, the Charity Commission said that it welcomes the Report and confirmed that it is raising its awareness of its regulatory role with the public and will explore the other recommendations made, including the ease with which people can make complaints.

In the light of the findings of the Report including the recommended increase in funding for the Charity Commission, coupled with the fact that in its strategic plan for 2015 – 2018 (published in June 2015) the Commission said that it had already “shifted resources into monitoring and investigations, increasing the number of statutory inquiries and the use of our most serious enforcement powers”, it seems that implementing its regulatory regime will be a key priority for the Charity Commission going forward.

Government – relationship with the charity and grant making procedures

The Report notes that:-

“Ms Batmanghelidjh and Kids Company appeared to captivate some of the most senior political figures in the land, by the force of the Chief Executive’s personality as much as by the spin and profile she generated for the charity. As a consequence, objective judgments about Kids Company were set aside. The Government’s relationship with Kids Company was forged outside the usual decision-making processes of Whitehall departments and there is little doubt that the high profile support of Prime Ministers for Kids Company had an impact on decision making across Whitehall²⁰..... It is also a matter of considerable concern that the knowledge of high-level political patronage enjoyed by Kids Company may have deterred other individuals from coming forward with concerns about the charity.”²¹

In the light of the above, the Report recommends that it should be the relevant Government departments who control grants to charities, rather than the Cabinet Office (which is the department most closely under the Prime Minister’s control) or another department which does not have direct policy responsibility for the sector in question. To enable greater objectivity, accountability, transparency and continuity the Report also (unsurprisingly) recommends that Government should re-evaluate its grant-making processes in relation to charities. In addition it is recommended that the Government improves the way it monitors and evaluates the performance of grant-funded organisations.

It is also recommended that the Government reviews whether sufficient safeguards are in place to ensure that the Libor Fund (which administers fines levied from UBS, Rabobank, Barclays and Lloyds banks among others towards military good causes and service related charities) is administered in line with the above principles of objectivity etc.

The Government receives a similar warning to that given to charity trustees in that audited accounts should not be relied on as an assurance that a charity is financially well managed:-

²⁰ Paragraph 42 of the Report

²¹ Paragraph 43 of the Report

“At the very least, Government must request sight of a charity’s management letters, and should seek direct assurance from the charity’s auditors.”²²

However, should not the above apply to all potential grant-makers – be they individuals, businesses or charitable organisations? Furthermore, in the interests of increasing the public trust and confidence in charities²³, would it be sensible/practicable if the reporting requirements for charities were amended so that charities would be obliged to give additional information in their annual report and accounts in relation relevant matters arising in management letters or the like?

What next?

The Report illustrates how seemingly easy it was for Kids Company to operate in a “twilight world” and escape the full scrutiny that charities would ordinarily face both from the Charity Commission as regulator and the Government as grant-maker. Clearly there are lessons to be learned not only for the Charity Commission and the Government but for charity auditors and other professionals and for charity trustees. However, the PACAC very importantly emphasises in its Report that:-

“The failure and public criticisms of Kids Company must not be allowed to taint the whole charitable sector; we have no reason to doubt that that the majority of Trustees and charities act responsibly and in accordance with their charitable purposes.”²⁴

If ever there were a time for the Charity Commission to strive to deliver on its statutory objective “to increase public trust and confidence in charities” it is now. However, let’s hope that the Commission strives to achieve this objective in a balanced and measured way, using its existing and its new protective powers where appropriate, but equally importantly by promoting compliance through encouraging and facilitating better administration of charities.

Although the Report serves a reminder to charity trustees that they are ultimately responsible for all aspects of their charity’s activities, it must also be remembered that a unique feature of the charity sector is that, on the whole, charity trustees are volunteers. The bar must be set high, but not so high that we see a mass exodus of trustees from the sector. We may then find ourselves having to abandon the general principle of voluntary trusteeship: an unpopular idea which was most recently suggested in Lord Hodgson’s 2012 review of the Charities Act 2006 and which many feel goes against the very nature of charity and charity trusteeship.

Sarah Chiappini

Director and non-practising solicitor

3 February 2016

filanthropiaconsulting
for charities and not for profit organisations

²² Paragraph 165 of the Report

²³ Increasing public trust and confidence in charities is one of the five statutory objectives of the Charity Commission

²⁴ Paragraph 8 of the Report