Brexit and charities:
What should charities be considering?

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Naziar joined Crowe in September 2008 from a Big Four Firm as a specialist Non Profits partner and is now Head of Non Profits.

In addition to providing assurance services she also provides advisory services to a range of charities. These include assignments from risk and finance function reviews, systems, benchmarking and performance measurements and governance reviews.

Naziar leads Crowe's work on Donor Audits and has knowledge of institutional funding requirements having produced reports for a variety of institutional and governmental donors. Naziar also carries out training for charities and lectures and writes on a range of topics relevant to Trustees and management.

Much has been written about the possible impact of the EU referendum on the UK economy, on business and charities. However given the uncertainties around the UK's exit negotiations it is not possible to fully evaluate the impact. This makes planning for the future hard particularly given other challenges the UK charity sector has been facing over the last year.

The only certainty then is that there will be uncertainty, at least in the medium term and charities like all other businesses need to factor this into their future planning. Organisations that survive and even flourish will be those that cope with the uncertainties and make good lasting decisions.

Below are six areas you should be revisiting in these uncertain times.

1. Strategies and scenario planning

Charities need to revisit their strategies to ensure that these are still 'fit for purpose' and achievable in light of the uncertainties. Scenario planning and decision trees are important tools which can be employed in profoundly uncertain times. However care needs to be taken that the focus is on shorter financial planning cycles than those which have traditionally been used, given that it is unreasonable to make accurate assumptions about the future.

Scenario planning will enable you to gain perspective on critical issues facing the charity and make decisions about capital investments and budgeting. It will also enable you to identify those events that will create substantial negative impacts for the charity allowing you to build a contingency in your budgets. Decision trees will help managers to structure and consider the sequencing of their decisions.

2. Management structures and skills including those of Trustees

Organisations that survive and flourish will be those led by individuals with the right knowledge, skill, and experience to act decisively when the time is right. It will be important to identify those who hold pivotal roles in your charity and ensure they regularly meet to share their knowledge.

Providing an opportunity to discuss and deliberate issues and challenges, make decisions and to then act together to successfully communicate and implement those decisions.

You will also need to consider how your charity can make decisions within shorter time scales. The two tier structure of Trustees and Executive can promote sub-optimal decisions made on a consensus. There may be an elongated path to decision making which can cause delayed response to the charity's immediate challenges and opportunities. You should consider your charity's decision making protocols.

There will also be a need for continuous horizon scanning and the sharing of information between the senior management team and Trustees. Time should be set aside at key meetings to ensure that issues are surfaced, information is shared and important matters are fully debated.

3. Budgeting and planning

There will need to be a shift away from rigid annual planning and budgeting cycles. Budgets are an important tool in enabling managers to make decisions within agreed parameters to deliver expected results. However in profoundly uncertain times the usual strengths in budgeting and reporting against the budget become its weaknesses. Assumptions are often made invalid by the continual changing events and emerging issues and if not careful budgets can become straitjackets. One approach might be to allow for a range of outcomes by using a base case, an optimistic case, and a pessimistic case. Another approach is to use rolling budgets which will help to keep plans current.

Consideration should also be given to setting aside contingency funds to both provide a cushion against downsides or to allow your charity to take advantage of emerging opportunities in a timely way.

4. Performance management

There is a great need for management to act collectively to make decisions which are in the interests of the charity and its beneficiaries. This may therefore mean performance measures need to be re-evaluated to include areas of interest, such as:

- encouraging individuals to identify issues even if they fall outside of their remit or
- encouraging sharing of intelligence on threats and opportunities.

5. Reserves policy

In the uncertain economic conditions there is necessarily a greater emphasis on financial monitoring and ensuring that charities are setting the right reserves policy.

The Charity Commission's recent press release reiterates the Commission's view that Trustees must actively engage with charity's finance "through regular monitoring, asking the right questions and getting professional help where needed." The Charity Commission has therefore updated the following guidance notes all of which are available from their website:

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

It is worth highlighting that a key change in the updated Commission guidance on CC19 is that:
"Trustees should develop a reserves policy that:

- reflects the risks of unplanned closure associated with the charity's business model, spending commitments, potential liabilities and financial forecasts
- helps to address the risks of unplanned closure on their beneficiaries (in particular, vulnerable beneficiaries), staff and volunteers".

In our view some aspects of the above will need to be revisited and the Commission has indicated that there will be further revisions to this guidance note later this year.

Reserves policies cannot and should not be developed in isolation to the charity. The current uncertainties mean that it will be important to revisit your reserves policy to ensure that it continues to link with the charity's risk management and forecasting process. You will also need to re-assess the charity's understanding of why the organisation needs reserves, what is the appropriate level and fully understand the reasons why it may be necessary to dip into reserves whilst analysing the available options.

Matters to consider include:

- Income: how volatile is it and what is the level of at risk income?
- Expenditure: what is its nature and can it be cut back easily?
- The nature of the reserves: what is their ability to be realised and what is the impact of doing this?
- Sensitivities and risk associated with assumptions made.
- Are reserves cash-backed where appropriate?
- Have other financing options available been considered?
- Are reserves being held for contingencies already provided for in budgets?
- Has the timing of cashflows been adequately considered?
- What is the impact of changes to the risk profile of projects and their funding structure?
- What is the cost of continuing programmes that are not fully funded? How quickly could programmes be shut down?
- How flexible is the use of restricted funding?

6. Risk registers

The uncertainty provoked by the EU referendum and other issues currently impacting charities will mean that it will be vital for you to revisit the charity's risk registers. Charities should focus on the risks that could impact on organisational strategic aims and focus on the uncertainties that might prevent them from achieving stated goals and objectives.

It goes without saying that new risks will need to be added (as discussed later) but it will also mean that you will need to re-assess the scoring of the charity's risks in light of the uncertainties.
Risk management needs consideration of risk vulnerability especially when events are rare or unprecedented; where the rules are unknown or rapidly changing; or where causes are driven by external factors beyond the charities' control. In such instances, the concept of vulnerability and risk interaction should assume prominence in both the risk assessment and risk management processes.

You will need to make a re-assessment of the charity's risk vulnerabilities. For those using traditional risk management methodology it may be time to move to new methodologies where there is greater importance on the impact of risks. This contrasts to traditional methodologies which consider both impact and likelihood of a risk and giving them equal importance.

Consideration of linked risks and the 'domino' effect or risk 'cascades' should be made. Most major value losses involve the interaction of more than one risk. Similarly, the exposure to a portfolio of risks needs to be considered. An isolated concentration on value at risk could result in not spotting 'risk contagion' – where one low impact risk leads to another and another so that the cumulative impact is catastrophic.

There will also be a need to revisit (or for some to establish) risk appetite and risk tolerances. In charities where there are usually two tiers with a non-executive Board supported by an executive management team. It is vitally important for the management team to understand and re-visit the initiatives and risks that the

Board are prepared to accept and which risks need to reduce and by how much. You can further guidance in our briefing ‘Setting risk appetite’.

Charities will also need to ensure that they do not focus solely on what can go wrong as this may lead to missed opportunities which stop the charity from innovating, driving growth and creating value for their stakeholders. In these uncertain times it is important for charities to have a robust process that allows them to manage opportunities and seek to exploit, share or enhance the benefit of the opportunity for their organisations.

Impacts to consider

Charities and their Trustees should, in the short- to medium-term, consider the threats or the downsides arising from the general macroeconomic impacts of Brexit. These some of the areas charities may need to consider in their strategic planning, budgeting, forecasting and risk registers.

1. Fall in interest rates will mean a fall in investment income impacting resources available for grant making trusts and foundations and those holding investments.
2. Fall in interest/bond rates will mean a fall in discount rates and therefore a rise in pension deficits/liabilities.
3. Fall in property prices will impact property funds held as investments and also properties sold as part of legacies.
4. A reduction in disposal incomes (as a result of falling interest rates and general shrinking of the economy) may lead to a fall in charitable giving and donations.
5. Tightening of public finances may lead to a fall in government funding for services and/or a requirement to deliver more for less.
6. The uncertainty may mean that some corporates will be focusing more on their own commercial returns and there may be less available for social responsibility programmes or corporate giving.
7. The UK has enshrined in law its commitment to spend 0.7% of its Gross National Income (GNI) on aid every year. In tightening fiscal conditions, there is a possible reduction in the GNI which will therefore mean a reduction in the amount available for the aid budget.
8. Rise in demand for services provided by charities as there may be a tightening of public finances and an increase in unemployment.
9. Tightening of immigration rules on EU citizens will most impact charities reliant on employing EU citizens such as those in the care and nursing sectors, those employed in research and artists and entertainers. The care and nursing sectors are the sectors currently most under stress of recruiting and retaining staff and have been impacted by the Living Wage which is set to increase again next year. In any case a number of charities employ EU citizens and their position is as yet unclear. More information on the Brexit consequences for employers of overseas staff is available on our Brexit Hub.
10. The UK is a draw for foreign students and for students from the EU zone. The tightening of immigration rules may impact this flow.
11. Charities receiving grants or funding from the European Union will be impacted and will need to set up or utilise branches within the EU zone or consider collaborating and partnering with EU based charities.
12. The fall in the value of sterling compared to the Euro and US dollars will impact programme delivery for overseas charities who will be able to deliver less as costs will be higher.

Notes

Start the conversation

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