Six insights for Trustees

Lessons learnt from Kids Company and others

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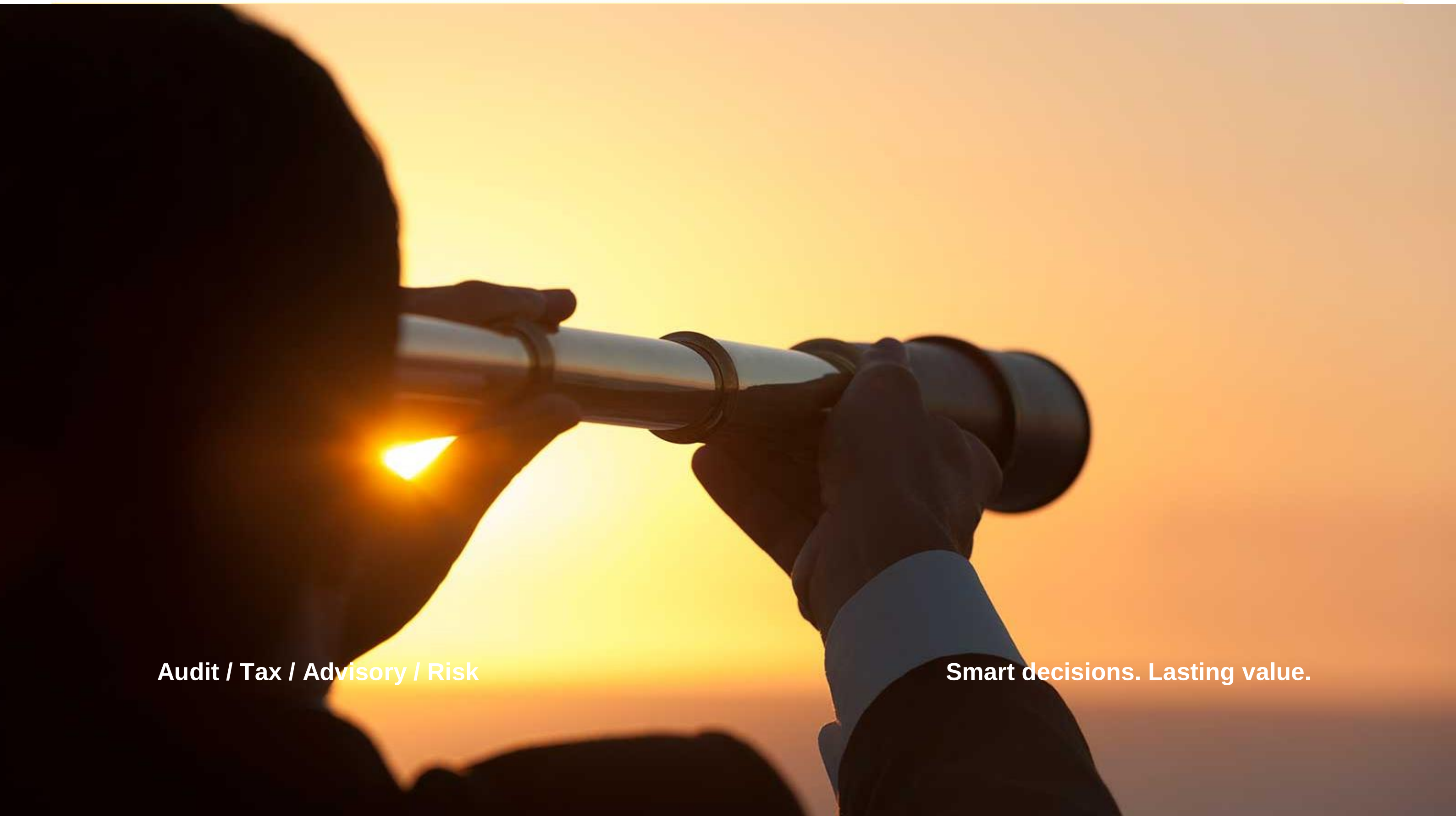

Introduction

The high profile collapse of Kids Company has led to an increased focus on charities, their structures and the role of Trustees. Rather than focus solely on Kids Company which is still subject to a statutory inquiry by the Charity Commission, we reviewed the Charity Commission's operational case reports published in 2015 to look at the lessons for Trustees and for charities.

At the outset, it is important to clarify that Kids Company is not typical of most charities and that the points discussed in this document will not be learning for most charities. However, it is the exception rather than the rule that often helps to reinforce what we already know and should be doing.

1. Trustee oversight: relationship with chief executive

It is fair to say that an area of particular focus with respect to Kids Company has been in relation to trustee oversight and the relationship of the Board and the Chair with the Chief Executive of Kids Company.

This matter was raised and discussed at length in the Select Committee hearings on Whitehall's relationship with Kids Company. Alan Yentob, the Chair of Kids Company, was asked how often he challenged decisions made by the Chief Executive and when the last time he challenged the Chief Executive was. The emphasis was on the challenge that the Board and its Chair had exercised over the Chief Executive and whether assumptions and judgements were adequately challenged. There was also focus on the personality of the Chief Executive and whether there was dominant influence which may have impacted the decisions made by the Board.

This point is a common refrain in some of the Charity Commission's operational case reports. For example, in the case of the Ambulance Service, the Commission said that it found that Trustees did not exercise sufficient controls over the CEO in relation to the two incidents of concern and, "that there were unclear reporting procedures and that the Trustees appeared over-reliant on the CEO and their chair and did not appear fully aware of their responsibilities to act as a collective body." In the lessons for other charities, the Commission reiterates the need for Trustees to "clearly understand their role and responsibilities. This includes understanding the different roles of, and interaction between, the charity's senior staff and the Trustees. Trustees should ensure that employees, particularly senior staff members such as the CEO, understand what is expected of them."

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Trustees may need to delegate decisions on day-to-day management matters to employees and the scope of the authority should be clearly stipulated with effective reporting back protocols.

The six main duties of charity Trustees are set out in the Charity Commission guidance CC3: The Essential Trustee. The theme underlying the guidance provided by the Charity Commission is that Trustees should be prepared to challenge and ask questions (as the guidance states, even those questions which may appear awkward or stupid). Trustees should also ensure that they are receiving timely information in a format that can be understood.

2. The role of the chair

Most major corporate failures have their roots in failures of corporate governance.

It has been over 20 years since the publication of the Cadbury report on Corporate Governance. The report's main findings hold as true today as they did 20 years ago; not only in the case of charity failures but also other major corporate failures since then. The report noted that: "Tests of board effectiveness include the way in which the members of the board as a whole work together under the chairman, whose role in corporate governance is fundamental, and their collective ability to provide both the leadership and the checks and balances which effective governance demands."

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The role of the Chair of a Board of Trustees varies between charities. Charity Commission guidance is clear that: "A chair can only make decisions in accordance with any provision in the governing document or delegated authority agreed by the Trustees, and should notify the other Trustees of any decisions made."

3. Tenure of Trustees and the chair

The Select Committee hearing into Whitehall's relationship with Kids Company examined the tenure of the Chair of Trustees.

Alan Yentob had been Chair of Kids Company since 2003. He was asked whether he considered that had been a long time to sit as the chair of the Trustees. He was asked: "One of the responsibilities of Trustees is to try to refresh and bring in new ideas and look at new approaches. Did you consider at any stage that perhaps you had passed your sell-by date, or had you become so involved so strongly in this charity that it was almost impossible for you to separate yourself from that?"

In fact, six of the Trustees of Kids Company had been on the Board between eight and 12 years. The question of whether there should be fixed tenure of Trustees to safeguard charities and the sector from the 'sell-by date' problem has been debated in the charity sector for some time. In his 2012 report Trusted and Independent: Giving charity back to charities — Review of the Charities Act 2006, Lord Hodgson recommended that: "Trusteeship should normally be limited in a charity's constitution to three terms of no more than three years' service each, and the Charity Commission and umbrella bodies should amend their model constitution documents to reflect this. Any charity which does not include this measure in its constitution should be required to explain the reasons for this in its annual report."

With regard to Kids Company, of course not only had a number of Trustees been in post for a number of years, the Chief Executive was also the founder and so it could be argued that there were not enough fresh perspectives, limited scrutiny and challenge from new pairs of eyes.

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The Charity Commission does not give any guidance on tenure of Trustees or chairs. In its operational case report on The Priory of England and The Islands of the Order of St John, the Commission stresses the importance of charities regularly reviewing their governance structures and sometimes undertaking a wider strategic review to ensure that the charity "remains effective, fit for purpose and accords with best practice".

The Good Governance Code for the Voluntary and Community Sector sets out the key principles of good governance practice. Principle 3 focuses on effective boards providing "good governance and leadership by working effectively both as individuals and as a team." An important element for consideration it states is "maintaining a strategy for board renewal that will meet the organisation's changing needs." It goes on to explain that: "This will cover maximum terms of office and succession planning, particularly for the Chair and other key positions/skills."

4. Reserves and cashflow management

Charities need reserves to support fulfilment of their missions and strategic decision making, to give them financial flexibility to respond to emergencies, to improve cash management and reduce stress as well as giving them the ability to respond to unanticipated opportunities.

Charity law requires income received by a charity to be spent within a reasonable period of receipt. The balance is in ensuring that the Trustees make what the Commission states in its guidance: “balanced and adequately informed decisions, thinking about the long term as well as the short term”. In other words, setting a reserves policy that considers future sustainability, balancing what is needed now with what will be needed in the future and “provides assurance that the finances of the charity are actively managed and its activities are sustainable”.

The challenge for Kids Company was its rapid growth from a charity with £2.4 million of income from 2004 to £23 million in 2013. In the years ending 2010 to 2013, it raised approximately £72 million of which unrestricted income was approximately £58 million. Despite this, it only turned its free reserves from a deficit of £32,000 to a surplus of £272,000 in 2012 and in the year ending 31 December 2013, its free reserves was £434,000, less than a week’s expenditure but the highest level ever reported in its accounts.

The issue seems to have been what the parliamentary inquiry report calls the ‘demand led model’ and the charity’s operating model which ‘carried the constant risk that the charity would not be able to ensure that its commitments would be matched by its resources’ which meant that the charity collapsed at the first hint of reputational trouble. The report goes on to state: “Kids Company relied on a hand-to-mouth existence and by refusing to prioritise the building of any significant reserves, the Trustees failed to exercise this duty of care towards the charity’s clients, employees and donors”.

The issue seems to have been what the Chair of the parliamentary inquiry into the charity’s relationship with Whitehall called the ‘demand led model’ and therefore the ‘fundamental risk’ in the charity’s business model which meant that the charity collapsed at the first hint of reputational trouble.

In a report on its operational compliance case report into BeatBullying which went into liquidation in November 2014, the Charity Commission stated: “BeatBullying was not in compliance with its own reserves policy and had no reserves. It was therefore quickly affected by the cancellation of anticipated funding. The Trustees had recognised they needed to build up reserves and had plans to do this, which could have helped tide the charity over until more funding applications could be made and granted. However, many grants have conditions attached to them such as the time period over which the grant should be spent. Therefore, it may be very difficult for a grant-funded charity to put aside money and build it up into reasonable reserves.

There is a clear argument that Trustees cannot assume receipt of funding — this issue was arguably the crux of the charity’s problems. However, the suggestion to be more conservative needs to be balanced with the reality of the environment in which charities operate, and the nature of applying for funding.”

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In response to and in advance of the publication of the parliamentary inquiry report into Kids Company, the Charity Commission has updated its CC19 guidance on reserves called ‘Building resilience’. The updated guidance states that the Trustees should develop a reserves policy that “reflects the risks of unplanned closure associated with the charity’s business model and spending commitments, potential liabilities and financial forecasts” and “helps to address the risks of unplanned closure on their beneficiaries (in particular, vulnerable beneficiaries), staff and volunteers”. There is increased emphasis in the guidance on the consideration of future uncertainties and the need for charities “to hold some reserves to meet an unexpected call on funds or opportunities that may present themselves”. The updated guidance also emphasises that “Trustees choosing to adopt a ‘zero level’ reserves policy must say in their annual return that they have adopted such a policy and should explain why”.

Commentators have remarked that updated guidance should have been put out to full consultation because of the increased focus on the points discussed in the paragraph above. The fear is that the balance may now be towards building reserves at the risk of delivering charitable objectives or taking advantage of rising opportunities.

In our view, there is no one size fits all yardstick for charity reserves but to set an effective reserves policy, Trustees must link reserves with the risk management and forecasting process and consider the charity’s operating realities.

5. Risk management and financial controls

With regard to Kids Company, there were questions around financial controls, distribution of funds to beneficiaries and the appropriateness of payments and expenditure to beneficiaries which were raised at the parliamentary inquiry.

A firm of accountants were called in to carry out a forensic audit following allegations that the charity had received from the Charity Commission but they did not complete their work.

On World Mission Agency-Winners Chapel International, the Commission found that concerns raised were unsubstantiated, but in their report the Commission reiterates as lessons for other charities, the need to put in place robust internal financial controls and for Trustees to regularly review and assess the risks faced by their charity in all areas of its work and plan for the management of those risks.

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The Charity Commission has useful guidance around financial controls and risk management and there is much that is written on these topics sector wide and more generally.

The absolute minimum for any well run organisation is robust effective systems, processes and controls as well as a sound risk management process. However, as Hallmark 4 of the Charity Commission's guidance CC10 states: "An effective charity is always seeking to improve its performance and efficiency, and to learn new and better ways of delivering its purposes. A charity's assessment of its performance, and of the impact and outcomes of its work, will feed into its planning processes and will influence its future direction."

In other words, an effective charity will always be looking at how it can improve in order to find better ways of delivering its desired outcomes to achieve the maximum impact and the learning from this process is an integral part of planning for the future.

6. Measuring and reporting performance

All well run organisations measure their performance to ensure they drive performance towards their strategic objectives. Charities also do so in order to show their stakeholders the difference they have made.

Interestingly, whilst acknowledging that Kids Company did do valuable work with vulnerable clients, the report states that: “It is both sad and disappointing that robust evaluation of the outcomes of Kids Company’s work is lacking” and that the charity “invested so little in highlighting and evaluating the outcomes of its work”. In their published report, the select committee into Kids Company state: “It has proved impossible to reconcile Kids Company’s claims about its caseload with evidence from other sources. The evidence is that the figures were significantly over-inflated”. They explain that in their view based on the evidence they were presented part of the problem was Kids Company’s practice of calculating its ‘reach’ which in their view, was ‘misleading to donors’. The report states: “The Trustees were either ignorant of this exaggeration or simply accepted it, because it helped to promote the charity’s fundraising”.

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SORP 2015 explains that “in reviewing achievements and performance, charities may consider the difference they have made by reference to terms such as inputs, activities, outputs, outcomes and impacts, with impact viewed in terms of the long-term effect of a charity’s activities on both individual beneficiaries and at a societal level. Charities are encouraged to develop and use impact reporting (impact, arguably, being the ultimate expression of the performance of a charity), although it is acknowledged that there may be major measurement problems associated with this in many situations.”

As anyone who has tried to measure impact will tell you, it is not an easy task. There are issues around attribution and contribution to consider as well as ‘evaluability’ which as HM Treasury explains, is “the extent to which activities can be measured to produce reliable evidence based judgements of performance, impact and value for money.”

The key issues for Trustees are to satisfy themselves of the value for money aspects of their activities as well as the impact of their work and to get assurance over the process which management have adopted in the collection and verification of the data. This includes assessment of impact and how these compare to sector practice. Trustees and management must ensure that anything that they have said about achievements and performance can be justified and verified. This means that they must be ready to ask the ‘how do we know?’ and ‘what evidence do we have’ questions.

10 Questions every Trustee should consider

1. Do you delegate to management within a clearly defined and appropriate scope of authority?

2. Do you have effective reporting mechanisms and do Trustees receive timely information in a format that is understandable?

3. Do you challenge robustly and ask questions (even the awkward and stupid ones)?

4. Do you clearly articulate the role of the chair and have the checks and balances which effective governance demands?

5. Do you consider the ‘sell-by-date’ of Trustees i.e. do you consider the tenure of the Trustees and the chair?

6. Do you consider the reserves to make adequately informed decisions considering future sustainability balancing what is needed now with what will be needed in the future?

7. Do you regularly review internal financial controls to ensure they are robust and fit for purpose?

8. Do you seek to improve performance and efficiency, considering outcome and impact of your charity’s work?

9. Do you assess whether there are new and better ways of delivering your charity’s purpose?

10. Do you consider accountability and how your charity communicates with its key stakeholders?

Notes

Start the conversation

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