National Audit Office

Report
by the Comptroller
and Auditor General

Charity Commission

Follow-up on the Charity Commission

HC 908 SESSION 2014-15 22 JANUARY 2015

Key facts

£21.1m	164,000	64
annual budget of the Charity Commission in 2014-15	main registered charities in England and Wales overseen by the Charity Commission	statutory inquiries into charities opened by the Commission in 2013-14

652	times the Charity Commission used its information gathering powers in 2013-14 (200 in 2012-13)
56	times the Charity Commission used its enforcement powers in 2013-14 (3 in 2012-13)
1	trustee removed in 2013-14 (0 in 2012-13)
£8 million	additional funding secured for the Charity Commission's 3-year transformation programme
1,746	exchanges of information between the Charity Commission and other public bodies in 2013-14 (1,539 in 2012-13)

Summary

1 The Charity Commission (the Commission) regulates charities in England and Wales. It is an independent, non-ministerial department responsible for regulating more than 164,000 registered charities. Its statutory objectives include promoting public trust and confidence in charities and regulating their compliance with charity law.

2 The Commission's regulatory activities are:

- registering charities;
- protecting and recovering charitable assets where there has been mismanagement or misconduct;
- granting permission for charities to do certain things such as dispose of assets;
- providing regulatory guidance; and
- maintaining a public register of charities.

3 In December 2013, we published a report, *The regulatory effectiveness of the Charity Commission*, which concluded the Commission was not regulating charities effectively and was not delivering value for money.

4 Our report formed the basis of a hearing of the Committee of Public Accounts (the Committee). In its report on the hearing,[1] the Committee shared our conclusion that the Commission was failing to regulate charities effectively. The Committee also expressed concern about whether the Commission was capable of transforming itself and tackling its significant failings.

5 Appendix Three summarises our and the Committee's recommendations from our last reports which included: the need for the Commission to set out a clear strategy and plan for transforming itself into a proactive regulator; improve its understanding of its costs; make better use of the data it holds; and make better use of its statutory powers.

1 HC Committee of Public Accounts, *The Charity Commission*, Forty-second report of Session 2013-14, HC 792, February 2014.

Report scope

6 Following our last report, the Committee asked the Commission to appear before it again, prior to the general election in May 2015. To aid that hearing, this report sets out the Commission's progress in transforming itself into an effective regulator of registered charities. Specifically we consider:

- the Commission's plans to transform itself (Part One);
- its actions to become a more proactive regulator through better risk assessment and use of data (Part Two);
- its use of its statutory powers and follow-up of regulatory issues (Part Three); and
- board oversight and performance indicators (Part Four).

7 We did not examine in detail the guidance the Commission produces, its advice or permissions work, or its work maintaining the public register of charities.

8 This report takes an early look at the Commission's progress. In many areas we are limited to describing the actions taken because it is too early to say whether or not they will deliver the necessary change. Our audit approach and evidence base are at Appendices One and Two.

Key findings

Transforming the Commission

9 **The Commission has stated its intent to become a rigorous and proactive risk-based regulator.** The Commission has said publicly it will concentrate on promoting compliance with legal obligations and accountability of trustees to fulfil its statutory objectives. It has committed to taking robust and decisive action where necessary, making better use of data and being bold in using its statutory powers. The Commission has communicated its new approach to staff and the charity sector (the sector) (paragraphs 1.4 to 1.8).

10 **The Commission has appointed a new chief executive to lead its change.** Following an open competition, a new chief executive with information technology (IT) and change management expertise was appointed. The board's early engagement with the issues raised in our last report, and commitment to transforming the Commission prepared the ground for her arrival. This enabled her to act quickly and decisively when she formally joined the Commission in June 2014 (paragraphs 1.9 and 4.5).

11 The Commission has developed a new business model that supports its aim of using risk assessment and data analysis to guide its work. The new model focuses more of the Commission's resources on regulating high-risk cases and using automated processes for low-risk transactions. The Commission recognises that devoting more resources to high-risk cases means it will spend less on supporting the sector. The model is necessarily high level and there is further detailed work to be done (paragraph 1.10 and Figure 1).

12 In September 2014, the Commission began a 3-year change programme designed to transform it into the robust regulator it wants to become. The change programme aims to establish improved systems and processes and bring about the organisational and cultural change necessary to support its aim of becoming a proactive regulator. Key aspects of good programme management are in place but it is very early days and much more remains to be done, in particular finalising the organisation design and IT requirements, and recruiting the skills needed to support the transformation. The Commission plans, in due course, to establish user groups and seek feedback on relevant elements of the programme, particularly new digital services (paragraphs 1.13 to 1.15 and Figures 3 and 4).

13 The Commission has secured £8 million of transitional funding from HM Treasury to support its change programme. The Commission's 2014-15 budget is £21.1 million. In October 2014, the Treasury announced a further one-off commitment of up to £8 million over 3 years. This funding is to help the Commission improve its IT systems and risk profiling, support proactive monitoring and investigations, provide more services online and fund its transformation programme. The Treasury also announced an additional £1 million to boost the Commission's annual budget in 2015-16 to fund immediate resource needs in the Commission's monitoring and enforcement work (paragraphs 1.16 and 1.17).

14 The Commission has made a start in understanding the cost of regulating the sector effectively, but has more to do. The Commission developed unit costs for its 30 key activities using 2013-14 data. It has also prepared high-level forecasts of its potential 2016-17 unit costs based on broad assumptions about planned productivity improvements from its new regulatory model. The Commission has not quantified the relative benefits of different activities, limiting its ability to take informed decisions about where best to direct its resources. It is important for the Commission to develop a good understanding of its unit costs to aid future funding negotiations with HM Treasury (paragraphs 1.18 to 1.20).

15 The Commission is improving its skills and capability. As well as recruiting a chief executive with change management experience, it has appointed 7 new board members with relevant experience in fraud prevention, counterterrorism, data mining and risk management. The board currently lacks a member with IT expertise. The chief executive is recruiting externally for 2 senior management posts to bring in operations and corporate services skills (paragraphs 1.11 and 4.3 to 4.5).

Becoming a more proactive regulator

16 **The Commission is updating its approach to assessing regulatory risk.** The Commission is piloting a new risk model that will enable it to assess every registered charity against key regulatory risks. The new model links the Commission's strategic objectives to enduring sector risks as well as new and changing risks, for example novel ways a charity could be used as a vehicle for tax avoidance (paragraphs 2.3 to 2.5).

17 **The Commission is making better use of data.** The Commission became a member of the fraud prevention service Cifas in April 2014. This has enabled it to access and match its own data against the National Fraud Database. The Commission has also agreed a data sharing exercise with HM Revenue & Customs (HMRC) to cross-check registered charities with charities claiming gift aid. The Commission has begun a project to make wider use of data and improve its ability to detect fraud in charities (paragraphs 2.8 to 2.10).

18 **The Commission is exchanging more information with other public authorities, but it typically makes twice the number of disclosures that it receives.** In 2013-14, the Commission made 1,152 disclosures of information to more than 50 public bodies, but received information only 594 times. In the first half of 2014-15, the Commission made 3 times more disclosures to HMRC than it received. HMRC told us it expects its disclosures to the Commission to increase in the second half of the year, although it remains to be seen whether information exchange is more balanced by the year end. The Commission passes information to organisations such as HMRC relating to non-charitable spending, unauthorised investments and tax avoidance. The Commission's most effective information sharing arrangement is with the police (paragraphs 2.11 to 2.14 and Figures 5 and 6).

Follow-up checks and use of powers

19 **The Commission is making more effective use of its powers.** The number of statutory inquiries it has opened increased from 15 in 2012-13 to 64 in 2013-14. The 64 statutory inquiries in 2013-14 included a class inquiry into 24 charities that had not filed their accounts. The class inquiry has led to £47 million of charitable funds being accounted for. The Commission used its information gathering powers 652 times in 2013-14 compared to 200 times in 2012-13. It used its enforcement powers 56 times in 2013-14 compared to 3 times in 2012-13, protecting £31.3 million of charitable assets through investigations completed in 2013-14, which included the recovery through litigation of £1 million for charities. The draft Protection of Charities bill proposes giving the Commission additional statutory powers (paragraphs 3.10 to 3.18, 3.21 and Figures 9, 10 and 11).

20 **The Commission has improved its follow-up checks but it does not follow-up all issues we might expect it to.** The Commission created a new team in October 2013 to carry out follow-up checks on registration and operations cases, alongside its existing investigations monitoring. The new team's work led to 10 charities being removed from the register and prevented 17 suspicious registration applications from being progressed. However, in our review of a small sample of cases we found some where we might have expected the Commission to follow-up to check that trustees had acted on its instructions, but where instead the Commission closed the cases (paragraphs 3.7 to 3.9).

21 **The Commission is taking longer to register charities.** The number of applications to register a charity rose from 5,949 in 2012-13 to 6,661 in 2013-14, and the average time the Commission took to register charities also increased. The target for registering medium-risk cases within 30 days has not been met in the last 18 months. The target for registering high-risk cases within 50 days has not been met in the last 4 months. Long-term staff sickness and the need for registration staff to train their colleagues following an internal reallocation of low-risk registrations have contributed to the failure to achieve internal performance targets on speed of registration. The Commission has recently established a dedicated team to process overdue applications, but it remains to be seen whether these measures will eliminate the backlog by the end of January 2015, as the Commission intends (paragraphs 3.3 to 3.6 and Figure 8).

Oversight of the Charity Commission

22 **The Commission's board played a more executive role following criticism of the Commission from the Committee of Public Accounts and the NAO.** There is a tension between the Charities Act 2011 which permits the Commission's board to act executively, and the Corporate Governance Code which states that boards should not stray into executive activities, although the board considers it must be guided above all by the Act. The board's involvement in executive functions from late 2013 to mid-2014 can be justified by the need to tackle the serious issues facing the Commission and cover the transition to the new chief executive. However, there is a risk that the board's continuing involvement in executive matters for an extended period could limit its independence and ability to hold the executive to account effectively (paragraphs 4.7 to 4.8, 4.10 to 4.19 and Figure 13).

23 **The Commission has strengthened its performance indicators but has yet to align them with its new business model.** The Commission has substantially revised its performance indicators for 2014-15, and has introduced a new measure of public trust and confidence in the Commission. The Commission met all its externally reported targets in 2013-14. It recognises it has more to do to align its performance measures with its new business model (paragraphs 4.20 to 4.23 and Figure 14).

Conclusion

24 The Commission has made good, early progress in addressing all of the recent recommendations made by the Committee of Public Accounts and the NAO. It has clearly stated its strategic intent to become a robust regulator. In support of this, it has developed a credible high-level business model and transformation programme to deliver the necessary change. It is using its statutory powers more to tackle abuse of charitable status. It is also working to improve the way it assesses regulatory risk and uses data.

25 However, much hard work and significant challenges lie ahead. Internally, the individual transformation projects need to be developed and implemented – in particular the automation of low-risk work which is essential if the Commission is to become more effective within its constrained resources. The Commission needs to understand the costs of its new regulatory model to enable it to put a persuasive case to HM Treasury at future budget negotiations. It also needs to strengthen its work to check trustees have acted on its instructions.

26 Externally, the Commission needs to show stakeholders how its new regulatory approach is enabling it to regulate the sector more effectively. It also needs to persuade other bodies to share information with it more readily. The Commission needs to actively manage public and charity sector expectations as to how it will perform its services and what issues it can realistically engage with and in what ways.

Recommendations

27 The Commission should:

a **Continue to press forward with planned changes. Specifically it should:**

- finalise detailed plans including the organisational design and IT requirements; and
- secure the necessary skills and capacity to ensure effective transformation.

b **Develop a strategy to persuade more public authorities to more willingly share relevant information with the Commission.** Senior management should lead engagements with key partners such as HMRC.

c **Develop a better understanding of the costs and benefits of effective regulation.** To support more effective future decision-making, and budget settlement discussions with Treasury it should determine the unit costs of activities under its new business model, and test them for sensitivity to key assumptions. It should also quantify the relative benefits of directing its resources at different activities.

d **Continue to tackle the delays in registering charities, especially medium- and high-risk cases.** It should analyse current registration processes to identify blockages and process improvements.

e **Continue to strengthen its work to check trustees' assurances.** It should build on the work of the operational functional monitoring team, and conduct a review across all its divisions of the criteria used to identify cases for follow-up to ensure cases that require further action receive attention.

f **Finalise its performance measures to ensure they align with the new business model.** It should include a measure for the effectiveness of its risk framework.

g **In the longer term, evaluate the impact of its revised regulatory approach, which should include feedback from a broad range of charities.** It should seek to determine whether it is achieving its aim of becoming a more rigorous and proactive risk-based regulator, and communicate this publicly.

28 We make 3 recommendations to the Commission's board:

h **Keep under review its level of involvement in executive decision-making.** To ensure good governance the board should remain alert to the impact of its involvement in executive decision-making on its independence and ability to hold the executive to account effectively.

i **Discuss with the Cabinet Office options for bringing someone with IT expertise on to the board.** It should consider the need to co-opt or buy-in IT expertise to effectively monitor and challenge IT improvements, which are central to transforming the Commission.

j **Complete the review of the governance framework and assessment of board effectiveness as soon as current governance arrangements have bedded in.** It should act on the findings of these reviews to further strengthen its governance arrangements and help ensure effective oversight of the executive.