



National Audit Office

Report

by the Comptroller
and Auditor General

Home Office and the Charity Commission

Report on the funding and governance of Broken Rainbow

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National Audit Office

Home Office and the Charity Commission

Report on the funding and governance of Broken Rainbow

Report by the Comptroller and Auditor General

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Commons in accordance with Section 9 of the Act

Sir Amyas Morse KCB
Comptroller and Auditor General
National Audit Office

25 April 2017

This report looks into the funding and oversight of the charity Broken Rainbow. The report reviews the financial management and oversight of the charity, the clarity of its grant agreements, and the role of the Charity Commission and other public bodies who were concerned with the charity.

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This report can be found on the
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Key facts

£1.4m

of Home Office funding for Broken Rainbow between 2004 and 2016

243

days after 1 April 2015 on which Broken Rainbow had less than £500 in its bank account

463

average number of helpline calls Broken Rainbow answered each month between July 2015 and March 2016

| | |
|-----------------------|---|
| £ 13.8 million | of general grant funding the Home Office awarded to non-profit organisations in 2014-15, the latest year for which figures are available |
| £970 million | of general grant funding awarded by the whole of government to non-profit organisations in 2014-15, the latest year for which figures are available |
| 144 | grants overseen by the Home Office in 2015-16 |
| 165,334 | charities overseen by the Charity Commission as at March 2016 |
| 1 March 2016 | date on which Companies House issued the first public notice threatening to close Broken Rainbow by 1 June 2016 |
| 7 April 2016 | date on which the Home Office provided funding to Broken Rainbow for 2016-17 |
| £34,403 | amount Broken Rainbow owes to HM Revenue & Customs in unpaid PAYE, National Insurance contributions and other charges |

Summary

1 In July 2016, Bernard Jenkin MP, chair of the House of Commons Public Administration and Constitutional Affairs Committee wrote to the National Audit Office asking us to investigate the collapse of Broken Rainbow, a charity funded by the Home Office.¹ Press articles had alleged excessive spending at the charity and weaknesses in its governance arrangements. The former CEO of the charity refutes these allegations. Mr Jenkin was also interested in whether lessons from *Principles Paper: Managing provider failure* and *The Government's funding of Kids Company* had been learned.^{2,3}

2 The Broken Rainbow LGBT Domestic Violence Service UK, known more widely as Broken Rainbow, was a charity founded in 2004. It provided support to lesbian, gay, bisexual and transgender (LGBT) victims and perpetrators of domestic violence, primarily through a national helpline and email support. The charity received most of its funding through grants, principally from the Home Office which provided most of its income in most years, including an annual grant of £120,000 since 2010. The Home Office signed a new grant agreement in April 2016, but in June 2016 Broken Rainbow closed and went into liquidation.

3 After conducting some preliminary inquiries, we decided to conduct a full inquiry into the facts surrounding the collapse of Broken Rainbow, and the actions of the various public bodies that had contact with the charity. While the amount of grant funding from the Home Office to Broken Rainbow was small, grant funding to the charitable sector from the whole of government totalled £970 million in 2014-15. Accordingly, there may be wider lessons from this example.

4 This report sets out:

- the funding, financial management and collapse of Broken Rainbow (Part One);
- the oversight of Broken Rainbow and its interactions with government (Part Two); and
- comparisons with Kids Company, and observations on the risks of grant payments to small charities (Part Three).

¹ Letter from Bernard Jenkin MP to Sir Amyas Morse, regarding the charity Broken Rainbow, 12 July 2016. Available at: www.parliament.uk/documents/commons-committees/PACAC/Correspondence/Sir-Amyas-Morse-Broken-Rainbow-12-07-16.pdf

² Comptroller and Auditor General, *Principles Paper: Managing provider failure*, Session 2015-16, HC 89, National Audit Office, July 2015.

³ HC Committee of Public Accounts, *The Government's funding of Kids Company*, Eighth Report of Session 2015-16, HC 504, November 2015.

5 A number of other organisations are currently investigating the closure of Broken Rainbow, including the Charity Commission and the insolvency practitioner charged with liquidating the charity. While we have spoken to these authorities for our own inquiries, this report does not discuss the findings of their investigations, which are ongoing. The Insolvency Service is not currently investigating the closure of Broken Rainbow, but may choose to do so after reviewing the insolvency practitioner's findings and any new information. We have worked closely with these authorities to ensure that our report findings do not impede their work or any action they may wish to take. We have not assessed the value for money of Broken Rainbow itself.

6 We found that Broken Rainbow had been struggling financially for a number of years, and that its overall management processes were ineffective. Some of this was evident from public documents, but none of the government bodies with which it had contact were fully aware of the difficulties, or had a clear remit to intervene. There are some straightforward steps departments could take to improve their monitoring of similar organisations.

Key findings

Management of Broken Rainbow

7 Broken Rainbow had been spending much more than its income for a number of years before its closure. Its reserves policy required it to keep three months' worth of expenditure, in case of unforeseen problems. However, its reserves shrank by 97% in two years, from £80,083 in 2012-13 to £2,307 in 2014-15, despite income increasing by 52% over the same period. The biggest increases in spending over that period were not on core helpline activities, but on consultancy (which increased by £16,000), research (£27,000), campaigns (£25,000) and total staff costs (£17,000). Several trustees have told us that the charity was also subject to employment tribunals at this time (paragraph 1.9 and Figure 2).

8 Broken Rainbow was operating 'hand to mouth', for at least a year before it closed. Between April 2015 and its closure in May 2016, Broken Rainbow had less than £500 in its bank account on most days. More than half of each grant payment from the Home Office, intended to cover costs for the following three months, was spent within 24 hours of receiving it. Most of the payments were spent completely within three days of receipt. When Broken Rainbow went into liquidation, it owed money to its suppliers and staff, and to government (paragraphs 1.11, 1.26, 1.27 and Figure 3).

9 The management of Broken Rainbow was chaotic and did not comply with regulatory requirements over a number of years. The charity had few organisational policies in place, and those that were in place were not followed. For example, staff were asked to put office expenses on personal credit cards because suppliers had not been paid; and conflicts of interest and grievance procedures were not managed effectively. We found that Broken Rainbow missed filing deadlines, and that the Charity Commission's website contained errors about the charity. Similarly, Companies House did not notice that the list of directors in Broken Rainbow's annual report included people not registered as directors. Companies House did, however, actively pursue Broken Rainbow for outstanding information, and this probably led to the charity's difficulties coming to light (paragraphs 1.16, 1.19 to 1.22 and 2.28 to 2.38).

10 There was a high turnover of trustees, and some trustees told us they did not feel able to get the help they considered they needed. Of the five Broken Rainbow trustees in post when it closed, three had become involved with the charity only at the beginning of 2016. Some trustees told us that they had contacted the Charity Commission seeking advice on how to manage the problems they found at Broken Rainbow, but had received no response (paragraph 2.5).

Oversight by government

11 Many different parts of government had some information about Broken Rainbow's difficulties, but none had the complete picture. For example, Companies House, which is responsible for publishing information about registered companies, had published in March 2016 notice of its intention to close Broken Rainbow, but the Home Office was unaware of this when it signed a grant agreement in April 2016 (paragraphs 1.23, 2.28 to 2.41 and Figure 5).

12 The Home Office did not meet its own requirements for monitoring the grant. The grant agreement signed by the Home Office and Broken Rainbow required Broken Rainbow to submit an annual report and quarterly information on the performance of the helpline. No annual report was ever received and many of the quarterly returns contained no performance data and the data reported did not contain quality measures (paragraphs 2.15 to 2.20 and Figure 8).

13 The helpline transferred from Broken Rainbow to a new provider, Galop, without a break in service, but only because Galop provided the service for free for a month. The Broken Rainbow helpline transferred to a new provider overnight. There was no break in service to the vulnerable individuals supported by the service. The Home Office had paid Broken Rainbow for the helpline until the end of June, but Broken Rainbow collapsed at the beginning of June. The Home Office did not lose any money because Galop inherited and paid the wages owing to helpline staff who transferred across, and provided the service for free for the first month. In March 2017, the Home Office confirmed it was processing payment to Galop to reimburse the charity for some of these costs (paragraphs 1.24 and 3.7).

Lessons for grant-giving to small charities

14 Government has very limited resources for monitoring grant payments, but there are steps it can take to provide better scrutiny. Departments do not have the resources to manually monitor other government websites that may contain information about grant recipients. They could, however, consider making better use of automated monitoring of publicly available information and use this to trigger alerts, which would help to target scrutiny. For example, if the Home Office had automated monitoring of the Companies House website it would have known that Companies House was proposing to close Broken Rainbow before it agreed to extend the grant (paragraphs 1.23 and 3.15).

15 Government could be more ambitious in the information it asks for from recipients of its grants. We have only examined the monitoring information provided by Broken Rainbow to the Home Office, but this was much more limited than the information Broken Rainbow provided to its other funders. Government could routinely ask to see the format of monitoring information provided to other funders to allow it to reach an informed judgement about how to balance the need for proper scrutiny of grants without imposing significant additional costs on recipients (paragraphs 2.25 to 2.27 and 3.14).

Concluding remarks

16 There are rules about how to run small company charities, but in the case of Broken Rainbow they were not enforced. In some instances this was because an organisation or individual did not fulfil their clear responsibilities. However, in other instances it is not clear how existing processes would have detected that Broken Rainbow was failing to comply with the rules. Nor is it clear if any organisation is responsible for addressing non-compliance, either through support or enforcement. These gaps in the governance arrangements potentially affect all small charities.

17 Light-touch regulation reduces the administrative burden on charities, but increases the risk that public money may be misspent. We note that government has recently announced plans to give an additional £102 million from fines from criminal activity in the banking sector (the LIBOR fines) to charities and good causes over the next four years. The government has made a number of changes to the supervision of grants since the collapse of Broken Rainbow, but more could be done to ensure that it makes the best use of the information it holds.

Part One

The funding and financial management of Broken Rainbow

1.1 This part describes Broken Rainbow's:

- aims and services;
- funding;
- financial management;
- problems; and
- closure.

Broken Rainbow's aims and services

1.2 Broken Rainbow was founded and registered as a charity in 2004. It sought to relieve the distress and suffering caused by and to lesbians, gay men, and bisexual and transgender (LGBT) people by domestic violence and abuse, through:

- raising awareness in the LGBT community and elsewhere of the impact of homophobic and same sex domestic violence on the lives of LGBT people;
- offering advice, support and referral services to LGBT people experiencing homophobic and same sex domestic violence; and
- offering information, advice, and training to individuals responsible for domestic violence policy and practice in mainstream and specialist organisations.

1.3 Broken Rainbow's primary avenue of support was its national LGBT domestic violence helpline (the helpline), which operated for 38 hours a week, covering Monday to Friday. It also offered online support. Between July 2015 and March 2016, Broken Rainbow answered an average of 463 calls a month, and received an average of 849 contacts via its online service. In addition, Broken Rainbow ran an Independent Domestic Violence Advocate (IDVA) service, and campaigned on relevant issues.

1.4 The charity was managed by its chief executive officer (CEO), and overseen by its trustees.

The funding of Broken Rainbow

1.5 The Home Office began funding Broken Rainbow in 2004. It provided financial support for the helpline in line with its strategy for reducing violence against women and girls. Since then, it has provided around £1.4 million in grant funding to the charity. The grant agreement specified that Home Office funding was to “support the existence, maintenance and staffing of the Broken Rainbow LGBT Domestic Violence Helpline”.

1.6 The Home Office funding has varied over the years, both in amount and whether restrictions were placed on how it could be spent. In 2015-16 it paid the charity £120,000 and in April 2016 it paid £30,000 to fund the helpline from April to the end of June. Payments were made quarterly, in advance. The grant was renewed annually, and was not open to competition.

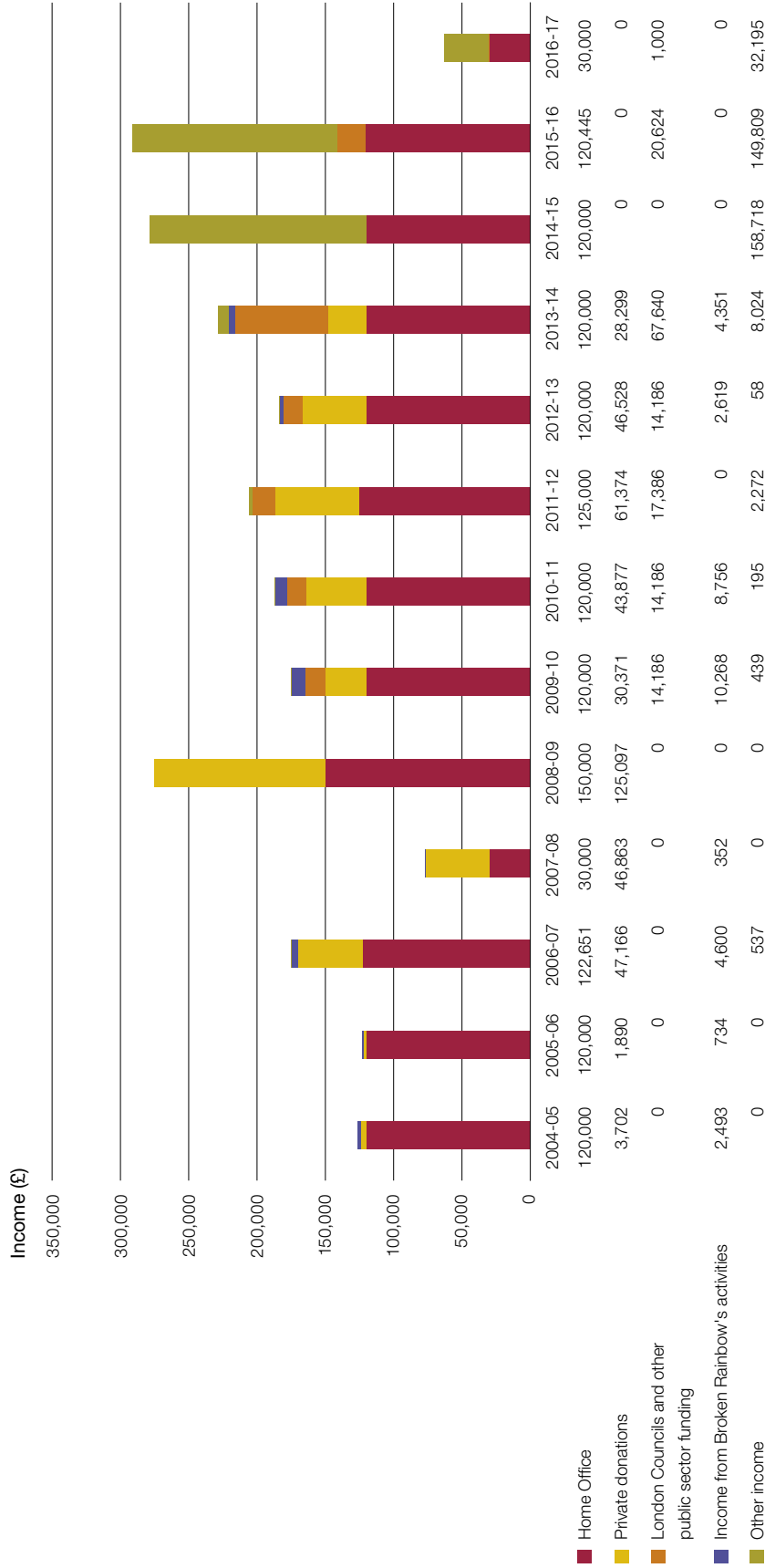
1.7 Although the majority of Broken Rainbow’s funding came from the Home Office, it also received funding from other public sector bodies. London Councils, a cross-party organisation representing London’s 32 borough councils and the City of London, told us it had provided Broken Rainbow with funding of between £14,000 and £19,000 a year since 2013-14. Funding also came from private donors (**Figure 1**).

1.8 Our analysis of Broken Rainbow’s accounts shows that the Home Office was a majority funder of the charity between 2004-05 and 2013-14. With the exception of the 2007-08 financial year, the Home Office provided more than half of Broken Rainbow’s income on an annual basis. In our work on *The government’s funding of Kids Company*, we set out the government’s ambition to secure its longer-term financial sustainability and reduce its dependence on central government grants.⁴ In some cases, government willingly acts as the lead funder of charities that it considers provide a specialised service, and that cannot easily attract other sources of funding. There is a risk to charities in being heavily dependent on government funding.

⁴ Comptroller and Auditor General, *Investigation: the government’s funding of Kids Company*, Session 2015-16, HC 556, National Audit Office, October 2015.

Figure 1
Broken Rainbow's income, 2004-05 to 2016-17

Broken Rainbow received funding from a number of sources, and the Home Office provided more funding than any other organisation



Notes

- 1 For 2004-05 to 2013-14, we have used Broken Rainbow's accounts. No detailed accounts were produced for 2014-15, so we have used the statement of income submitted to the Charity Commission to establish Broken Rainbow's total income, and Home Office records to establish the amount that came from the Home Office. For 2015-16 and 2016-17, no accounts were produced, so we have used a combination of Home Office records and an analysis of Broken Rainbow's bank statements.
- 2 Other income: from 2004-05 to 2013-14, this covers Gift Aid and miscellaneous income. For 2015-16 and 2016-17, this includes all sources of income that we could identify from the bank statements (so could include categories of income that were included in other categories in previous years).
- 3 Income from Broken Rainbow's activities include events, training, membership and consultancy work.

Source: National Audit Office analysis of Broken Rainbow's annual accounts and bank statements, and Charity Commission records

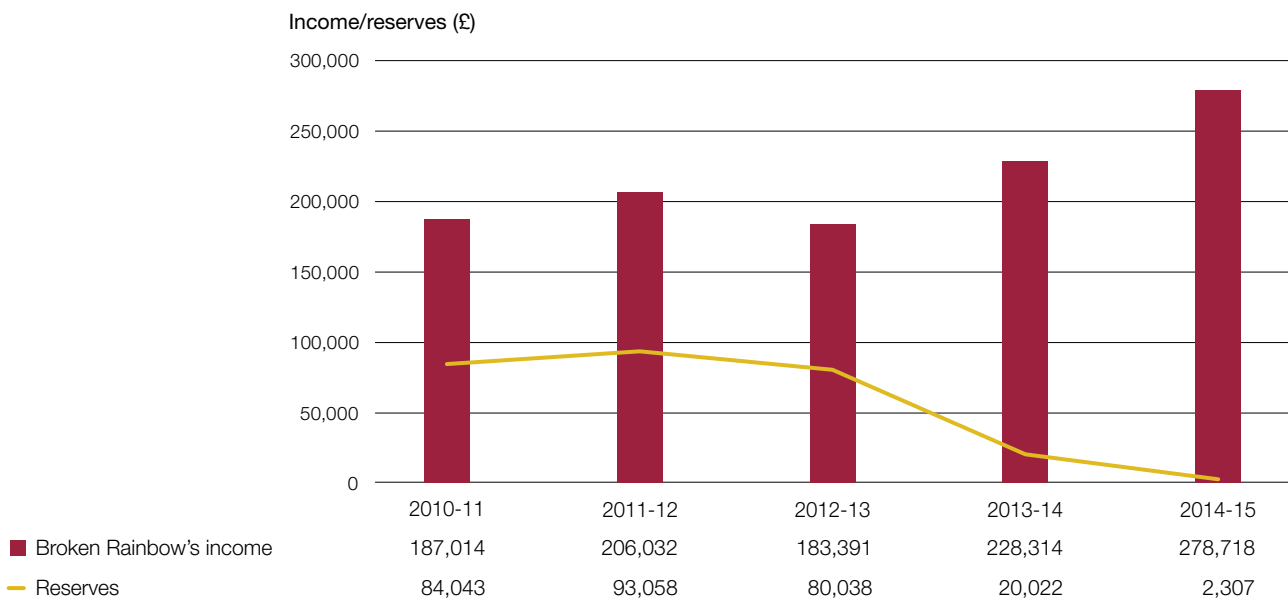
The financial management of Broken Rainbow

1.9 Broken Rainbow appears to have been struggling to manage its finances for a number of years. Its policy was to have enough reserves to cover three months' expenditure, which in 2013-14, the last year for which full accounts were produced, was around £70,000. Reserves are intended to provide resilience against risks, such as a drop in income. Broken Rainbow's annual accounts, which were filed with and published by Companies House, showed the charity's reserves decreased by 97% in two years between 2012-13 and 2014-15, from £80,083 in 2012-13 to £20,022 in 2013-14 and £2,307 in 2014-15, although its income increased by 52% over the same period (**Figure 2**). The biggest increases in spending over that period were not on core helpline activities, but on consultancy (which increased by £16,000), research (£27,000), campaigns (£25,000) and total staff costs (£17,000). No accounts have been produced for 2015-16.

Figure 2

Broken Rainbow's income against its reserves, 2010-11 to 2014-15

Despite big increases in income, Broken Rainbow's reserves decreased markedly from 2012-13



Source: National Audit Office analysis of Broken Rainbow's accounts

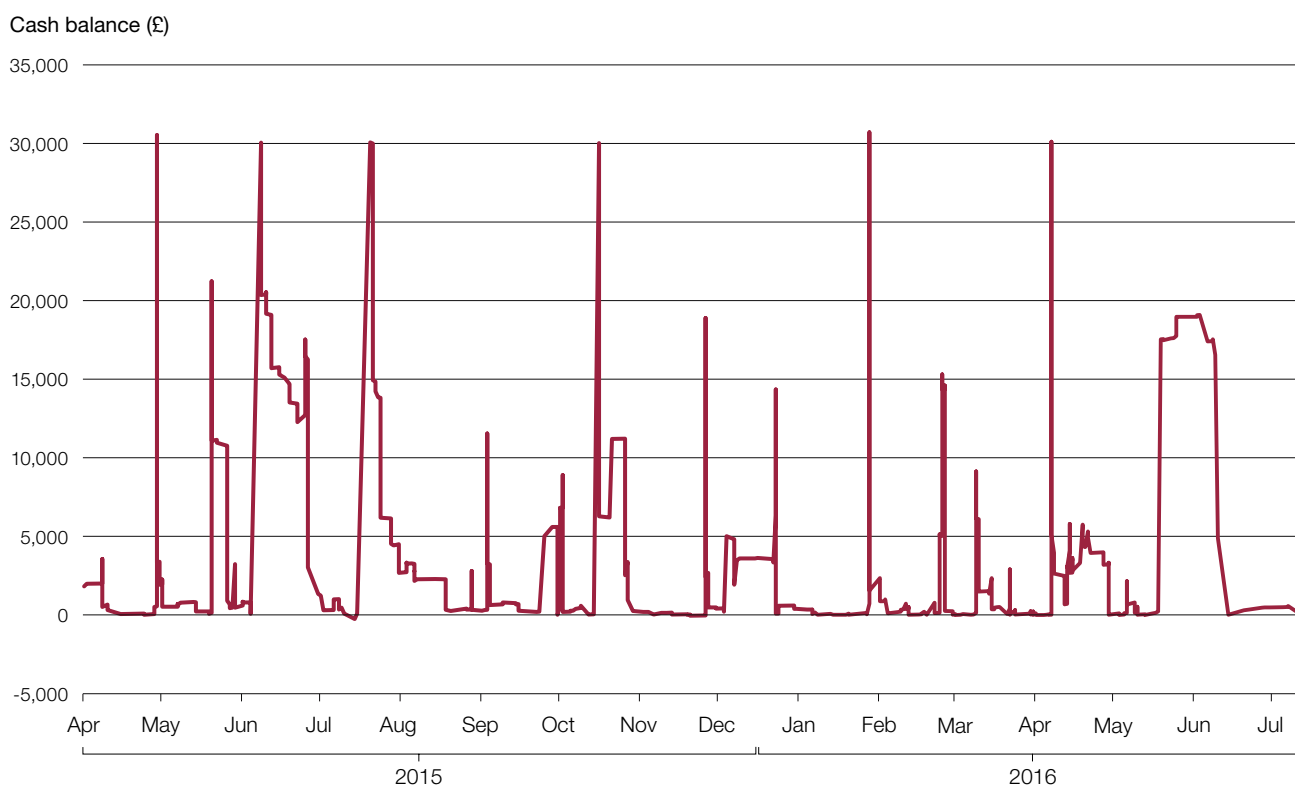
1.10 Former trustees and the former CEO of Broken Rainbow told us that some of the reserves had been spent on the legal costs of an employment tribunal in 2013, which they estimated at between £20,000 and £35,000. Our review of the evidence provided by the former CEO and trustees suggests that this was the fourth employment tribunal the charity had faced since its opening.

1.11 Our analysis of Broken Rainbow's cash flow also suggests that the charity was under considerable financial stress. We analysed money coming in and out of its bank accounts between April 2015 and July 2016. In many cases, large grant payments were spent within days of receipt (**Figure 3**). On 7 April 2016, the Home Office paid Broken Rainbow £30,000 to cover the costs of providing the helpline between April and the end of June. On the same day that the payment went in, the charity paid out £25,000, leaving £5,000 to cover the remaining costs for the next three months.

Figure 3

Broken Rainbow's cash flow, 2015 to 2016

Broken Rainbow's bank statements show money going out as soon as it comes in



Note

1 Broken Rainbow closed at the beginning of June 2016.

Source: National Audit Office analysis of Broken Rainbow's bank statements

1.12 The former CEO and some trustees told us that the Home Office routinely paid its quarterly grant late, which placed financial pressures on the charity. The Home Office paid the grant an average of 19 calendar days after the beginning of the period that it funded, which appears to be broadly within the terms of the grant agreement: this required the Home Office to pay the grant within 10 days of receiving performance information on the previous quarter and a request for payment from Broken Rainbow. There are no records of when this information was sent to the Home Office, but it means the payment was at most nine days late. The CEO also told us that the Home Office was kept well informed about Broken Rainbow's financial issues. In 2014, the charity wrote a letter of complaint to the Home Office citing 'concern and disappointment' over the way its funding had been dealt with. Nevertheless, the charity appears to have been operating 'hand to mouth'. On most days (243) after 1 April 2015, it had less than £500 in its bank account. On 129 days in that period it had less than £100.

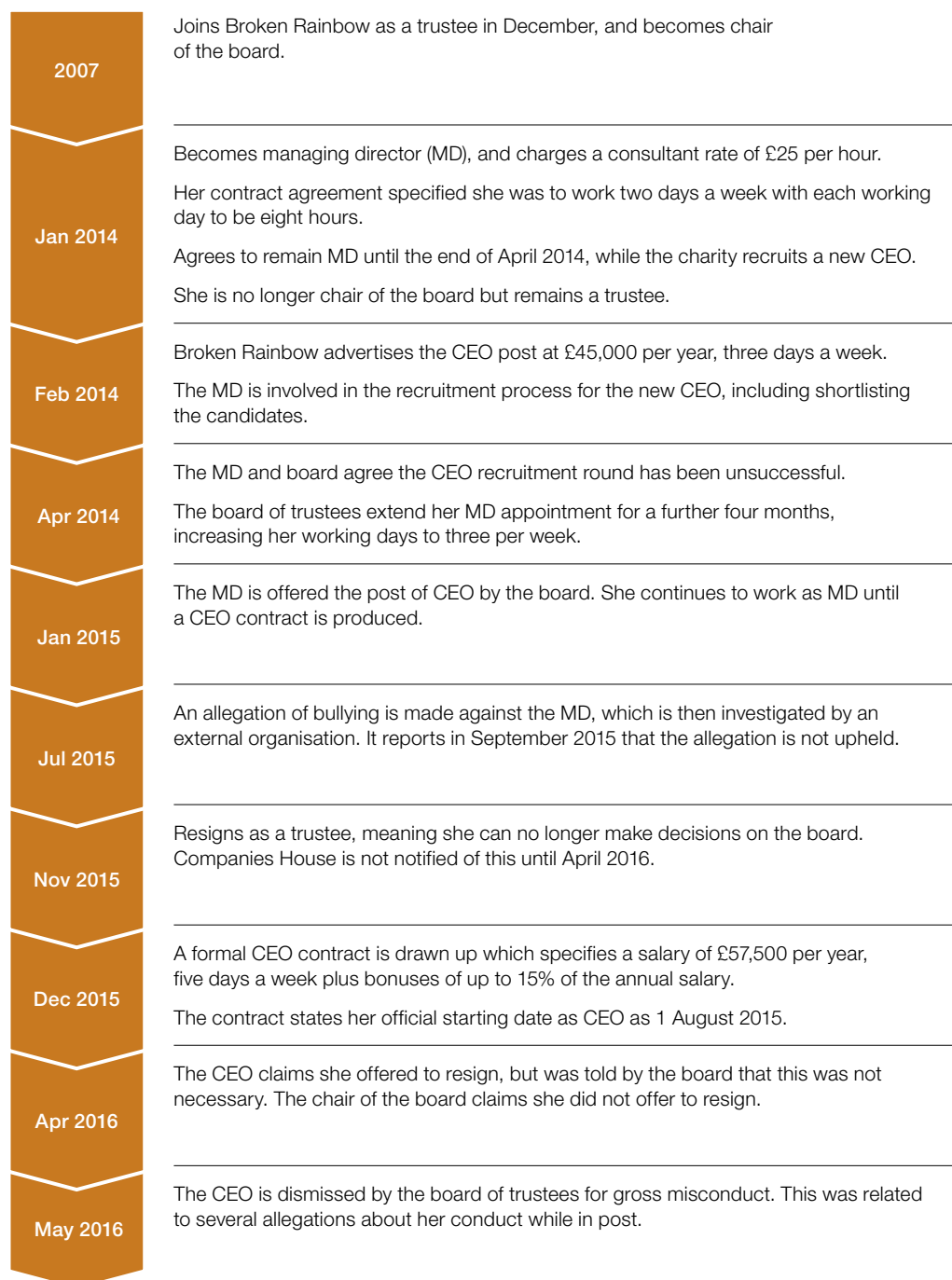
1.13 We have been unable to establish a complete picture of Broken Rainbow's finances in its final year as the charity's records were deleted remotely shortly after the liquidators seized the charity's computers. There is disagreement between the trustees and former CEO about who was responsible for this.

1.14 Between April 2015 and July 2016, 32% of payments (by value) from the charity's bank account went into the former CEO's bank account. This totalled £114,397.92. The former CEO told us that some of these payments covered her hourly fee as managing director, her £57,500 salary as CEO, and other expenses, including salary payments to a member of staff. This sum also included salary payments for her wife, who worked at Broken Rainbow (records held by the former CEO suggest this amounted to just under £12,000). The former CEO told us that she had a verbal agreement with the charity's treasurer to claim money including a backdated salary increase from August to December 2015, although the treasurer in place in August 2015 had left by October 2015 so was not in a position to authorise this in December. She also told us that her expenses were authorised by the treasurer. We have been told, both by the former CEO and trustees that there were lengthy periods where there was no treasurer in place, and none of the trustees we have spoken to recall authorising expense payments to the CEO's account.

1.15 The former CEO sent us copies of invoices she had issued to Broken Rainbow during her time as managing director – she worked part-time as a consultant on an hourly rate, before becoming a full-time salaried CEO (see paragraphs 1.17, 1.18 and **Figure 4**). The invoices show several instances where she worked longer than her contracted working day of eight hours, which incurred additional costs for the charity. The former CEO told us that she had a verbal agreement with the board to work the hours required to fulfil her role. This was confirmed by trustees we spoke to, though we were told this was to be 'within reason' and subject to agreement by trustees. The invoices are addressed to the organisation rather than an individual, and it is not clear who if anyone reviewed them before payment was made.

Figure 4

The former CEO's history at Broken Rainbow



Source: National Audit Office analysis

1.16 Although it is usual practice to require two signatures to authorise payment from charity bank accounts, from November 2015 onwards there was no second signatory on Broken Rainbow's account: the CEO alone authorised payments. The reasons for this situation are disputed: the CEO told us that the high turnover of trustees and the length of time taken by the bank in processing the paperwork for a second signatory meant that payments could not wait for a second signatory. Some trustees told us that they believed the CEO, whose signature was required to authorise a second signature, was herself the cause of delays.

Problems at Broken Rainbow

Recruitment of a chief executive officer

1.17 The former CEO of Broken Rainbow told us that there was a lack of clarity and formal agreement over her role, salary and working hours. During her time at the charity she was a trustee, worked as consultant managing director charging an hourly rate, and then became the CEO on an annual salary plus bonus. There appear to have been periods where she had no formal written contract. When she was formally appointed as CEO in December 2015, this was backdated to August 2015. Figure 4 describes key events in the employment history of the former CEO.

1.18 In May 2016, the then CEO was dismissed by the board for gross misconduct. The chair of the trustees told us that the board had been unable to dismiss her earlier because of challenges in obtaining the required evidence. The exact sequence of events is a matter of dispute: the former CEO told us that she offered to resign in April 2016, and was told by the board that this was not required, and that she was not given the opportunity to challenge the grounds of her dismissal. The chair of the board does not agree that the then CEO offered to resign. The chair also told us that the terms of the then CEO's dismissal were in line with the charity's staff policy, including an opportunity to appeal within five days, which the then CEO chose not to take up.

Poor internal governance

1.19 We observed instances where there were conflicts of interest in how the charity managed its operations, mainly involving the former CEO:

- In 2014, the then MD was involved in the recruitment process for her intended successor. She was eventually appointed to this post in 2015, at a salary 27% higher than that which had been advertised, with scope for a further 15% bonus. The former CEO (then MD) told us the higher salary was to reflect a change in the role and increased responsibilities in 2015. The role was not advertised publicly.

- The CEO line-managed the individual who line-managed the CEO's wife. The CEO's wife in turn managed the charity's online chat service. Former staff told us that this lack of boundaries in management made it difficult for them to raise concerns about their workloads. The CEO told us that while the situation was not ideal, a suitable management structure was put in place to minimise conflicts as a trustee was responsible for overseeing the situation. It is not clear who this trustee was.

Failure to comply with statutory requirements

1.20 As a company and a charity, Broken Rainbow was required to submit information to both the Charity Commission and Companies House. It repeatedly failed to notify those organisations of changes to the directors and trustees, and also to file its annual accounts on time. This is dealt with in more detail in paragraphs 2.28 to 2.38.

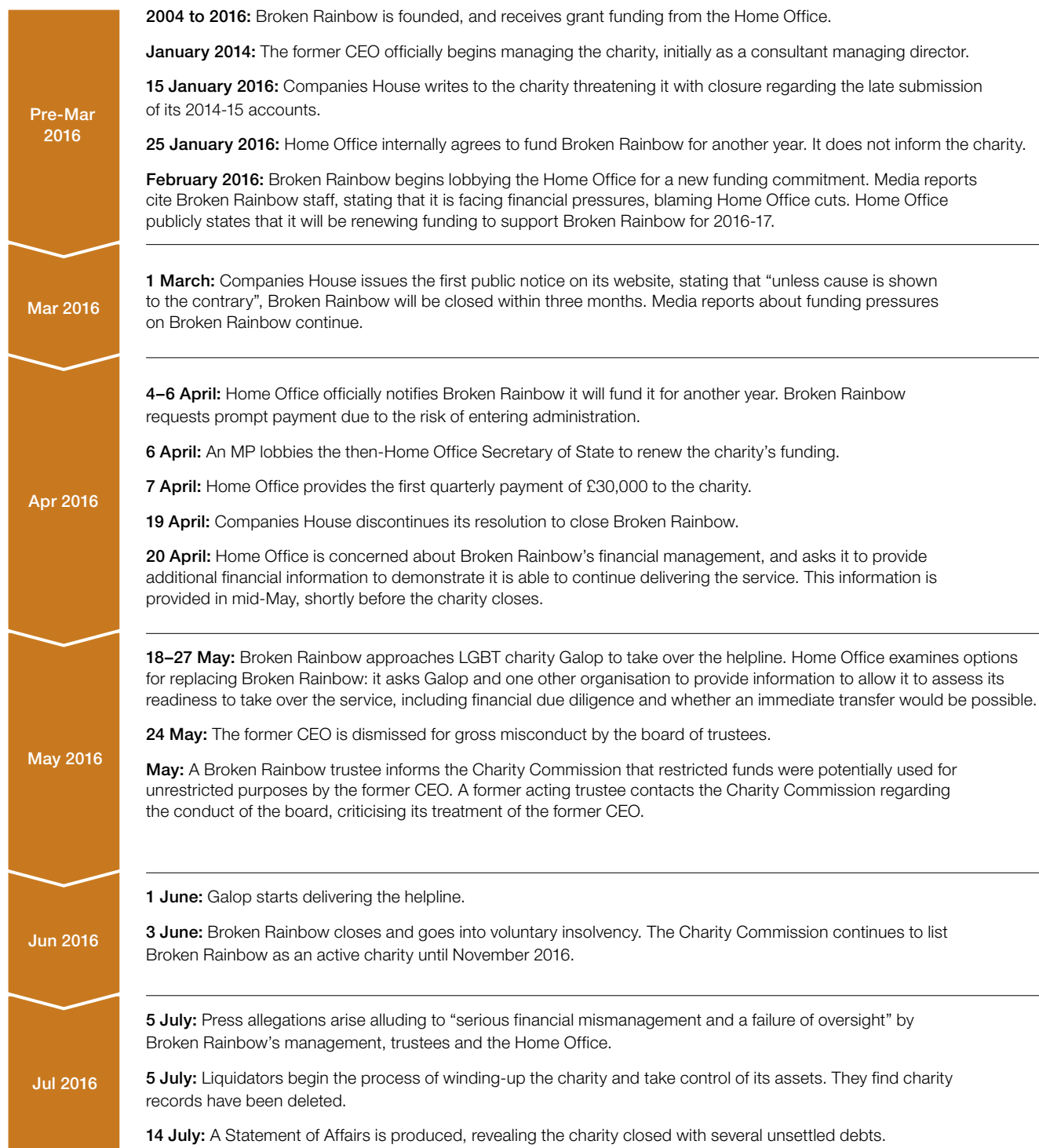
Breakdown of relationships between the trustees, CEO and the organisation

1.21 Relations between Broken Rainbow staff, the trustees and the former CEO were strained in the years running up to the closure of the charity. The former CEO told us that from the summer of 2015 her relationship with the board of trustees had broken down, following changes to the board's structure and operations. This made it difficult for her to do her duties effectively. Former staff also reported being asked to put office expenses on personal credit cards because suppliers had not been paid, and routine delays in being paid their salaries. These staff told us that despite this they continued to staff the helpline, because they were committed to delivering this important service. Concerns were also raised about failures in the conduct of the board, poor financial management and lack of the proper procedures and controls to allow staff to make complaints.

1.22 Multiple grievances were raised against trustees and staff members, alleging bullying, harassment and improper conduct. In September 2015, an external investigator reported on allegations of bullying and harassment made against the former CEO. The investigation found that the allegations were unfounded, but raised concerns about the blurring of professional lines and lack of effective management within the charity. It also discussed the low morale of staff. In May 2016, the CEO issued a grievance against the entire board. Later that month the CEO was dismissed by the board. From 1 June Broken Rainbow's helpline transferred to another charity. In July it went into liquidation (**Figure 5** overleaf).

Figure 5

The demise of Broken Rainbow – timeline of events



The closure of Broken Rainbow

Lack of coordination between different government bodies

1.23 Between March and July 2016 several different bodies engaged with the charity, unaware of the other interventions taking place and of how close Broken Rainbow was to closure (Figure 5). On 1 March 2016, Broken Rainbow was given notice by Companies House that unless it produced accounts for 2014-15, it would be closed down by the end of May. On 7 April, the Home Office made a grant payment for 2016-17. In May, Broken Rainbow's trustees asked another charity to take on the helpline. During this time the Charity Commission was investigating the governance and financial management of the charity. It only became aware that the charity had gone into liquidation in June 2016 from media reports. It told us that the trustees had failed to report this to the Commission as per its Serious Incident Reporting guidance.

The continuation of services

1.24 There has been a continuous service for users of the national LGBT domestic violence helpline. From 1 June 2016, the Home Office transferred the grant to the Lesbian, Gay and Bisexual Anti-Violence and Policing Group (Galop), which began to deliver the helpline with no break in service. The transfer included some former Broken Rainbow staff attached to the helpline. The Home Office undertook an assessment of financial due diligence to ensure that Galop was able to provide the service. When we spoke to Galop in November 2016, we were told that the transition was relatively quick, but that it had incurred additional unexpected costs. Galop told us it had inherited £9,500 in staffing liabilities from Broken Rainbow. In addition it provided the service for free for a month from 1 June, as its grant agreement covered funding from July 2016 onwards only. We estimate the cost of this month of service to be around £10,000. The Home Office decided to pay the charity in arrears, rather than in advance as it had done for Broken Rainbow. The Home Office told us that it only pays in advance for very small charities that might otherwise have cash flow problems. As of November 2016, Galop had received no funding from the Home Office for delivering the helpline since June. In March 2017, the Home Office confirmed it would reimburse Galop in-part towards the costs of the service it provided in June and the staffing liabilities it inherited.

1.25 Galop considers it has improved the service provision of the helpline at no additional cost to the Home Office. It analysed call patterns to the helpline and adjusted the service operating hours from 38 to 46 hours a week to meet demand. The Home Office sent us a report from Galop detailing its delivery of the helpline from June to September 2016. It provided more detail than the returns previously provided by Broken Rainbow, including anonymous case studies and geographical data on calls. The Home Office told us it asked Galop to provide detailed reports so it could better understand the benefit of the service it is funding.

Broken Rainbow's creditors

1.26 There are two registered public sector creditors to Broken Rainbow: HM Revenue & Customs (HMRC) and the National Insurance Fund. Before Broken Rainbow entered liquidation, its trustees prepared a Statement of Affairs. This document sets out a list of Broken Rainbow's assets, and the debts owed to those registered as creditors. Broken Rainbow owed its creditors £62,762 on its closure, of which more than half was owed to HMRC (£32,000) in unpaid PAYE and National Insurance contributions. HMRC told us that it made additional charges in December 2016, bringing the total amount owed to £34,403. These debts accrued across three years, from April 2014 to March 2017. Broken Rainbow was never registered for VAT nor was it required to be.

1.27 The only other registered public sector creditor is the National Insurance Fund, which paid £13,600 of public funds to support employees who would have otherwise faced loss of wages and redundancy payments. National Insurance Fund compensation for lost wages is capped at £479 per week for a maximum of eight weeks. Galop told us that it met the remaining compensation payments to staff attached to the helpline and involved in the subsequent transfer of the service. Only one member of staff, who was not involved in the helpline and so did not transfer to Galop, is registered as a creditor of Broken Rainbow. The other significant creditor is the Metro Charity, which was owed £15,000 by Broken Rainbow. The Home Office is not pursuing payment for the month of undelivered service, estimated at a cost of around £10,000. When Broken Rainbow closed in June 2016, it had delivered the helpline for two out of the three months for which it had received payment.

Ongoing investigations

1.28 The Charity Commission and the insolvency practitioner charged with liquidating the charity are conducting investigations into the closure of Broken Rainbow. These investigations can cover the conduct of the trustees and management of Broken Rainbow. The Insolvency Service is not currently investigating Broken Rainbow, but may choose to do so in light of new evidence. If as a result of their investigations these organisations determine that an individual has breached their legal obligations, they can impose a range of sanctions:

- the Charity Commission can, in certain circumstances, prevent individuals from acting as trustees in future;
- the Insolvency Service can strike off individuals and prevent them from acting as company directors in future; and
- the insolvency practitioner can seek to recover funds through the courts from either the trustees or the former CEO if it considers that they have acted illegally.

At the point of publication, these investigations are ongoing.

Part Two

The governance of Broken Rainbow

2.1 Broken Rainbow was not a public sector body. It was the role of its management and trustees to ensure that it was a well-run and sustainable organisation. However, various parts of government did interact with Broken Rainbow in its normal course of business. **Figure 6** overleaf outlines the various entities responsible for overseeing Broken Rainbow. These oversight arrangements are the same as we would expect to see for other government departments making grants to a charity with an income of less than £1 million.

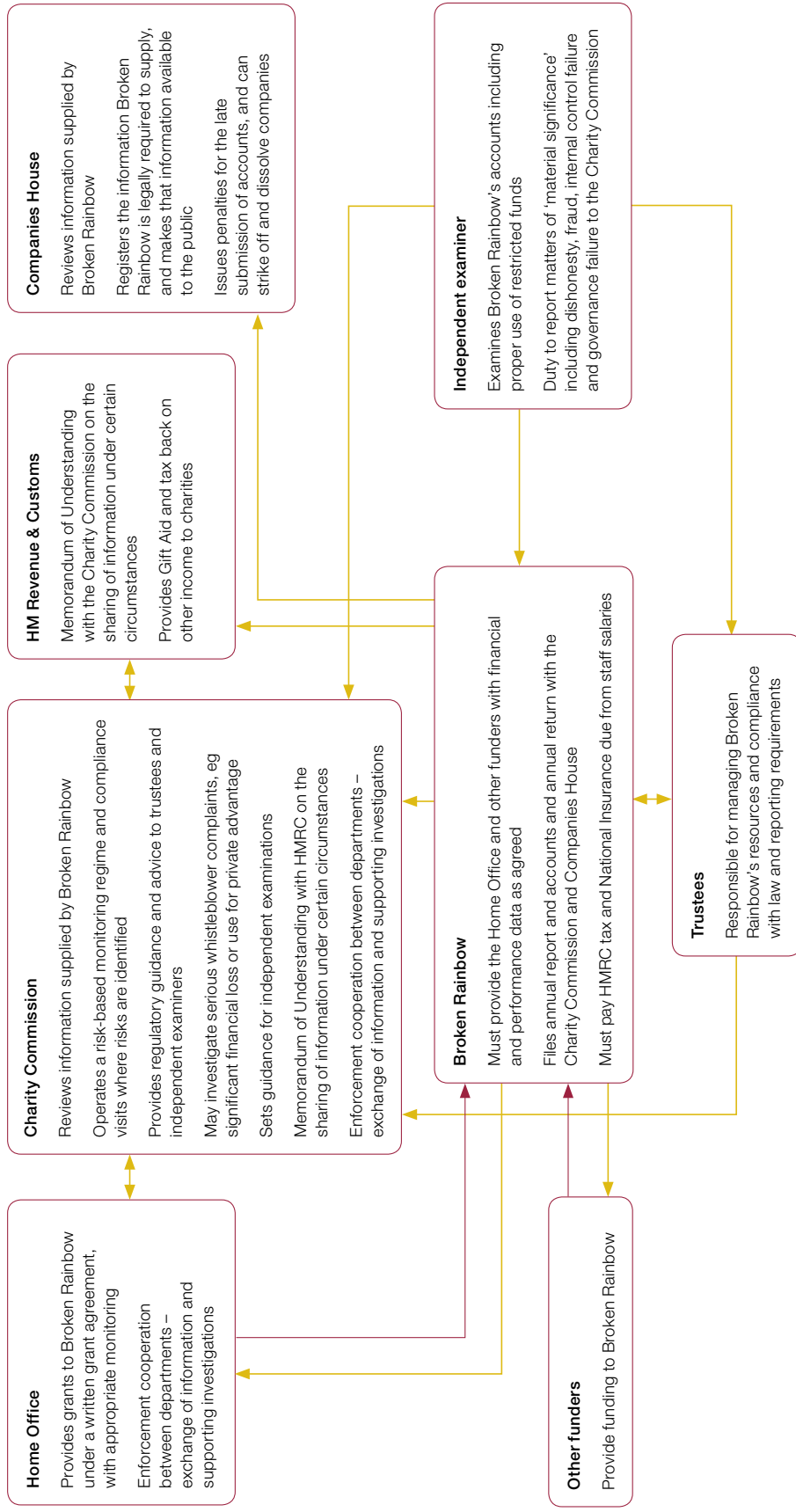
2.2 Each organisation overseeing Broken Rainbow had a different relationship with the charity; in some cases, they worked with one another. In this part, we discuss the role of:

- Broken Rainbow's trustees and the independent examiner;
- the Home Office and other funders;
- the Charity Commission;
- Companies House; and
- HM Revenue & Customs.

Broken Rainbow's trustees

2.3 Broken Rainbow's internal management and operations were overseen by its trustees. Trustees have independent control over, and legal responsibility for, a charity's management and administration. The trustees employed a managing director, who had been a trustee and who later became the chief executive officer (CEO), to run the organisation on a day-to-day basis (paragraphs 1.17 and 1.18). Trustees are dependent on the management of the charity for the information that they need to exercise their responsibilities.

Figure 6
The role of bodies that interacted with Broken Rainbow



→ Funding
→ Reporting

Note

1 This is the same oversight arrangement that we would expect for any government department making grants to a charity with an income of less than £1 million. If the charity had been larger, oversight would have included a full external financial audit, which would have provided more assurance about the financial management and position of the charity.

2.4 The Charity Commission has produced guidance on what the trustee role entails, including their main duties (**Figure 7**).⁵ The Charity Commission told us that it refers newly registered charities and their trustees to this and other guidance. It does not routinely issue guidance to new trustees, but sends a quarterly newsletter and other alerts to all trustees for which it has an email address. It has not assessed whether or how charities use its guidance. The former CEO told us that all trustees were provided with a copy of *The Good Trustee Guide* when they took up post.⁶ In March 2017, the Charity Commission updated its financial guidance to help trustees understand their basic financial responsibilities when running a charity.⁷

2.5 There was a high turnover of trustees at Broken Rainbow. Of the five trustees in place in May 2016, three had only been involved with the charity since the beginning of the year. None had been involved since the charity was set up, so none had been sent any guidance by the Charity Commission. The trustees we spoke to told us that the Charity Commission offered very little support when they approached it with concerns about how to deal with the challenges they were experiencing between 2015 and 2016. The Commission told us that they were only approached by one trustee, with whom they corresponded.

2.6 The trustee role is voluntary. The Charity Commission told us that it is responsible for ensuring trustees comply with their legal duties, but is mindful of its duty of proportionality and that the trustee role is voluntary in the vast majority of cases. While trustees have a legal responsibility to manage their charity's resources responsibly, there are no national or accredited assessments to test trustee proficiency or train them for the role. The trustees we spoke to felt that the charity struggled to find people with the right skills, there was a need for more clarity about the skills and experience necessary to fulfil the trustee role, and a need for more support for trustees.

Figure 7

The essential trustee – main duties:

- Before you start – make sure you are eligible to be a charity trustee.
- Ensure your charity is carrying out its purposes for the public benefit.
- Comply with your charity's governing document and the law.
- Act in your charity's best interests.
- Manage your charity's resources responsibly.
- Act with reasonable care and skill.
- Ensure your charity is accountable.

Source: Charity Commission, *The essential trustee: what you need to know, what you need to do*, July 2015. Available at: www.gov.uk/government/publications/the-essential-trustee-what-you-need-to-know-cc3/the-essential-trustee-what-you-need-to-know-what-you-need-to-do#trustees-duties-at-a-glance

5 Charity Commission, *The essential trustee: what you need to know, what you need to do*, July 2015.

6 National Council For Voluntary Organisations, *The Good Trustee Guide*, March 2015.

7 Charity Commission, *Charity finances: trustee essentials*, March 2017.

2.7 Broken Rainbow was both a charity and a company. Charities must submit financial information to the Charity Commission, and companies to Companies House. As a small company with an annual income of less than £500,000, Broken Rainbow was entitled to provide Companies House with summary accounts which included much less information about its financial position than accounts published by larger organisations.⁸ Broken Rainbow was also subject to less external scrutiny than a larger organisation would have been. While Broken Rainbow was required to send its annual accounts to the Charity Commission and Companies House on a timely basis, neither body has the capacity or capability to check every set of accounts it receives.

2.8 If a charity's gross income is between £25,000 and £1 million, charity law requires its accounts to be subjected to an independent examination. For charities with an income of between £25,000 and £250,000, the examination can be carried out by anybody whom the trustees consider has the relevant ability and experience. There is no statutory definition of relevant ability and experience, but the Charity Commission provides guidance and examples to help charities decide if someone is suitable. Charities with an income exceeding £250,000 must have their accounts examined by someone who is a member of a relevant profession.

2.9 An independent examination is a less in-depth form of scrutiny than an audit, and provides less assurance about the accounts. An examiner is only required to confirm that they have not seen any evidence of certain failings. Examiners include a statement in the accounts detailing their findings.

2.10 In most years, Broken Rainbow's income was between £25,000 and £250,000, so it was required to appoint an independent examiner but this person was not required to hold any particular professional memberships. Between 2004-05 and 2013-14, Broken Rainbow engaged an independent examiner without a formal accountancy qualification. It is not clear if the 2014-15 accounts were ever examined, and no further accounts have been produced.

2.11 The independent examiner must make a report to the Charity Commission if, in the course of their examination, they identify any matters of material significance. The Charity Commission told us that Broken Rainbow's independent examiner did not make any such reports.

Lack of effective external oversight

Home Office

2.12 Government departments use grants to fund external organisations and activities they wish to support, including voluntary and community sector (VCS) organisations.⁹ In 2014-15, the Home Office provided £13.8 million of general grant funding to non-profit VCS organisations. In 2015-16, the Department oversaw 144 grants. Some grants are split between multiple recipients.

⁸ Section 477 of the Companies Act 2006.

⁹ In our July 2014 report, we define a grant as a permanent transfer of funding for a specific purpose, which is used in accordance with a set of terms and conditions. Comptroller and Auditor General, *Government grant services*, Session 2014-15, HC 472, National Audit Office, July 2014.

2.13 The Home Office has provided funding to Broken Rainbow since the charity launched in 2004. The Home Office funded the charity as part of its strategy to tackle domestic violence. From 2004 to 2008, the funding provided was mostly unrestricted, meaning that Broken Rainbow could spend it as it wished. From 2009, the grant funding was restricted. Its purpose was to 'support the existence, maintenance and staffing of the Broken Rainbow LGBT Domestic Violence Helpline'. The former CEO told us that the Home Office had not established clear parameters for spending the grant, and that she had a verbal agreement with them that the grant payments could fund other activities and were not restricted to funding the helpline. The Home Office disagrees.

2.14 The Home Office's grant agreement with Broken Rainbow was awarded on an annual basis. The contract with Broken Rainbow was not re-tendered in the 12 years that the Home Office funded the charity.

Limited performance and expenditure monitoring

2.15 As a condition of the grant payment, Broken Rainbow was required to send quarterly monitoring information to the Home Office. At the end of the grant funding period, it was required to provide an overall report setting out how the charity had met its objectives during the funding period. The grant agreements for the 2014-15 and 2015-16 financial years specified that Broken Rainbow should provide information on:

- the performance of the helpline;
- whether Broken Rainbow was on course to spend the funding; and
- whether there was a risk of underspend.

2.16 We asked the Home Office to send us the monitoring information it received from Broken Rainbow from 1 April 2014 onwards. The Home Office sent us five out of eight quarters of Broken Rainbow's expenditure monitoring data.¹⁰ These reported several occasions when Broken Rainbow had spent beyond its budget set out in the funding agreement in certain areas. Across the five quarters, Broken Rainbow spent 13 times more than planned on travel and subsistence, four times more on staff salaries and recruitment, and three times more on software and online services. The Home Office agreed that the funding could cover half of the former CEO's salary costs until the charity found alternative funding. The grant agreement was not adapted to reflect this. The Home Office considered that no monitoring reports provided by the charity raised concerns about its solvency.¹¹

2.17 The amount of the grant had not been increased to reflect inflation since 2009. The Home Office did not carry out any benchmarking exercises to understand how Broken Rainbow's costs compared with those of other helplines.

¹⁰ The Home Office did not hold any financial monitoring information for March to June 2014, October to December 2014, or October to December 2015.

¹¹ Letter from Mark Sedwill, Permanent Secretary, Home Office to Bernard Jenkin MP regarding the charity Broken Rainbow, 4 August 2016.

2.18 The Home Office also sent us eight quarters of performance monitoring forms, as sent to them by Broken Rainbow covering the period from 1 April 2014. Only three of the eight included any performance data; the relevant section on the other five returns were blank. Where data were included, they covered the number of calls to the helpline, and contacts made in person via the Broken Rainbow office and online email support. This did not meet the requirements set out in the grant agreement. It is not possible to know whether the Home Office ever received the information about the remaining five quarters, spanning 15 months of service.

2.19 We analysed the performance data from the three quarters for which the Home Office had data, which covered July 2015 to March 2016 (**Figure 8**). The Home Office paid Broken Rainbow £90,000 during this period, within which:

- nearly half (47%) of all recorded contacts were via the Broken Rainbow office, online chat or helpline emails – the grant agreement specified that funding was for the helpline; it did not refer to face-to-face or online support;
- of calls made to the helpline during its opening hours 78% were answered; and
- overall, 52% of calls made to the helpline were not answered (1,476 out of 2,866). This was either because the helpline was closed (39%), or it was busy during its opening hours (14%).

2.20 It is not clear from the monitoring data whether the number of ‘helpline contacts’ only included emails and individuals to whom Broken Rainbow replied, or all emails and contacts, regardless of whether Broken Rainbow provided any support. The Home Office has not been able to clarify this. It did not request information from Broken Rainbow on the quality of the service provided, or on any other aspects of the helpline’s performance. The former CEO told us that all contacts were responded to, but in the absence of any records it is not possible to verify this. The former CEO also told us that Broken Rainbow had previously provided more detailed monitoring information to the Home Office, but stopped doing so as the Home Office said it was too detailed. She told us the charity also invited the Home Office to visit its premises and see the service it provided, but that these invitations were declined.

Weaknesses in the grant agreement

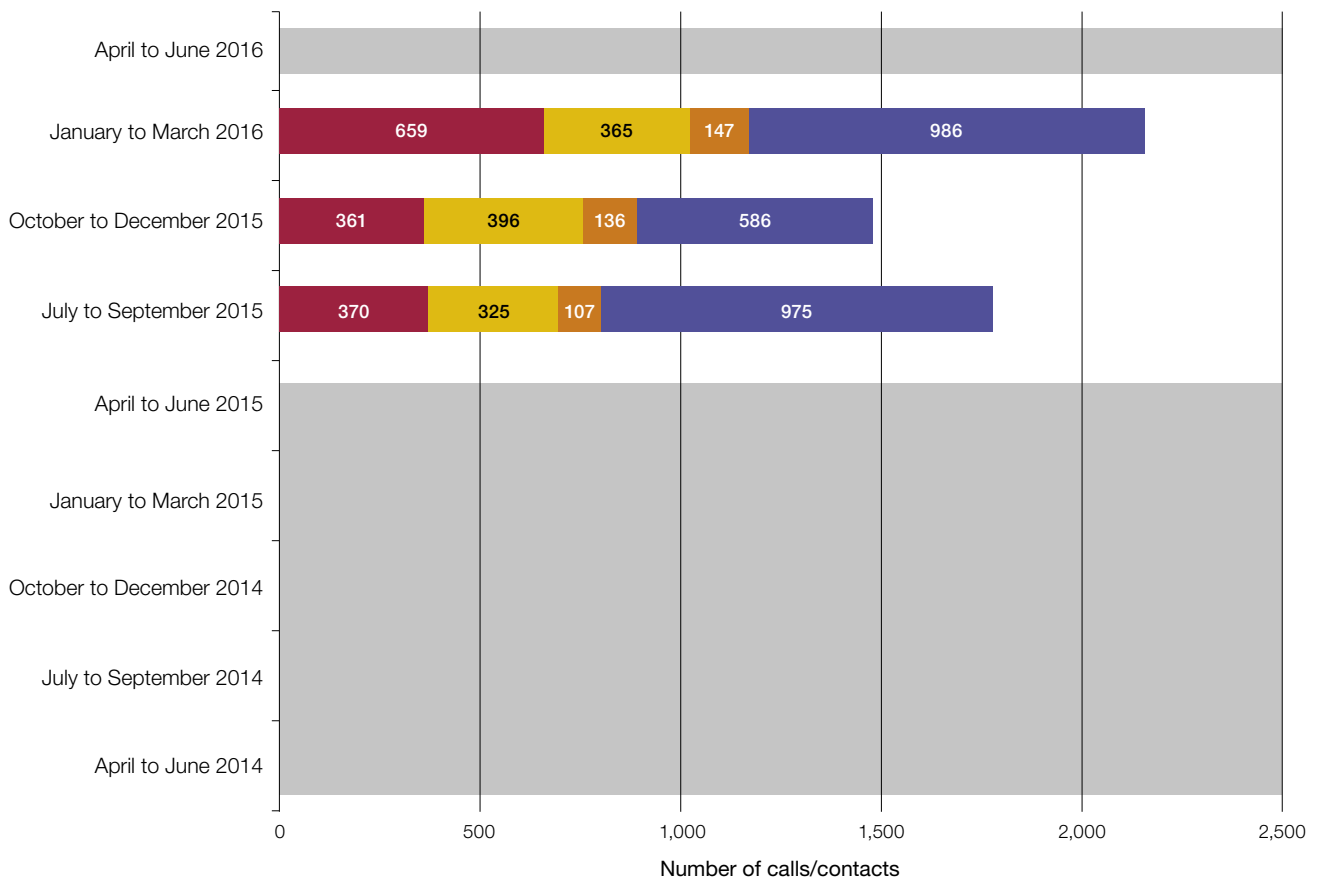
2.21 The Government Internal Audit Agency (GIAA) reported on the whole of the Home Office’s grant monitoring mechanisms in March 2015, and found a number of weaknesses, resulting in a low assurance rating for the department’s grant management process. Broken Rainbow was included in a sample of grants reviewed. The audit identified issues with the Home Office’s management of this grant, including:

- the late processing of the grant agreement (and subsequent late payments);
- the grant holding unit not actively monitoring how the grant was used beyond requesting and receiving the monitoring returns;
- the purpose of funding not being sufficiently clear; and
- the grant holding unit being unaware of its responsibilities and authorities regarding grant management.

Figure 8

Records held by the Home Office on the helpline’s performance, 2014 to 2016

Nearly half of all recorded contacts were via the Broken Rainbow office, online chat or helpline emails



- Number of calls answered by a person
- Number of calls outside of operating hours and diverted to answer machine
- Number of calls not answered, engaged or diverted to answer machine during helpline hours
- Helpline contacts via Broken Rainbow office, online chat, or email support
- No data

Notes

- 1 We asked the Home Office to send us performance monitoring data from April 2014. Grey rows represent periods for which the Home Office does not hold any data.
- 2 Broken Rainbow told us that this data was submitted, but we were not able to verify this through emails as the computer systems had been wiped.

Source: National Audit Office analysis

2.22 In respect of Broken Rainbow, the audit report concluded that there was a:

“lack of clarity around whether the grant funding is intended to support helpline costs or ... support the charity’s associated activities of increasing awareness, training and encouraging the development of LGBT DV [domestic violence]-specific support services across the UK.

Whilst Broken Rainbow was able to demonstrate compliance with the terms and conditions of the grant agreement, [the need for] some improvement in the robustness of its controls was identified.”

2.23 The GIAA made three recommendations to the Home Office in its report. The one most relevant to Broken Rainbow was to “ensure that a supporting ‘second line’ assurance process is in place to proactively monitor the effectiveness of the grants regime across the Home Office”.¹² This was categorised as a ‘high importance’ recommendation. The Home Office told us that following this recommendation, it has revised and reissued its guidance on grant monitoring in August 2016. We asked the Home Office to send us the grant agreements covering the last three years of their funding to Broken Rainbow. The 2015-16 agreement was signed a month after the publication of the GIAA report but did not reflect any of the report’s findings. The Home Office told us that this was because the agreement was set up prior to receiving the GIAA report.

2.24 The grant agreement for 2016-17 contained significant omissions. The Home Office sent us two versions of this. The first version had the specific details of the Broken Rainbow grant completed, but it had not been signed either by the Home Office or by Broken Rainbow. It contained minor differences to the 2014-15 and 2015-16 grant agreements. The second version was almost a completely blank template, which had been signed by the grant recipient. It did not contain any details about Broken Rainbow. The template did include a requirement for an agreed business plan with key performance indicators and timescales, and a joint risk and issue register, suggesting that the Home Office was tightening up its monitoring processes. The Home Office did not receive any information or monitoring data covering 1 April 2016 onwards, as the charity closed before this information was due. The Home Office told us it had initially sent the unsigned version to Broken Rainbow in error. The template version was then sent to Broken Rainbow, which is why this is the only version that has been signed. It is not clear why the template version was not completed by the Home Office before being sent to Broken Rainbow.

¹² The GIAA helps to ensure that government and the wider public sector effectively manage risk. It uses the three lines of defence model to help identify and explain the different sources of assurance within an organisation, and the contributions they make. The first line is operational, where assurance comes from those responsible for delivering specific objectives or operations. The second line of defence is associated with the oversight of management activity, where assurance comes from how well work is being carried out in line with set expectations and policy or regulatory considerations. The third line relates to independent and more objective assurance, which comes from the work of internal audit.

Better monitoring by other funders

2.25 Broken Rainbow provided much more detailed monitoring information to other funding bodies, despite receiving less money from them than it did from the Home Office. For example, London Councils funded Broken Rainbow's helpline to assist callers from London. From 2013-14, it provided funding of between £14,000 and £19,000 a year. London Councils required Broken Rainbow to:

- provide information on the demographic characteristics of callers to the LGBT domestic violence helpline, including ethnicity, gender identity and age; and
- collect information on the appropriateness of the information provided by helpline staff, and whether it met users' needs.

2.26 Broken Rainbow also had to deliver against quarterly targets on the number of LGBT people who:

- received emotional and practical support via the specialist LGBT domestic violence telephone and email support service;
- reported an increase in their knowledge of rights, entitlements and options;
- accessed the specialist telephone and email support, resulting in an increased knowledge about how to make safe decisions; and
- had increased their awareness of the support available.

2.27 London Councils told us it monitors financial as well as performance information. This level of monitoring gave London Councils much more information about how its grant money was being spent than the information collected by the Home Office.

Charity Commission

2.28 The Charity Commission (the Commission) is the registrar and regulator of charities in England and Wales. It is an independent, non-ministerial government department, wholly funded by and accountable to Parliament. It has five statutory duties (**Figure 9** overleaf).

Figure 9

The Charity Commission's statutory duties

The Commission's duties:

- Increase public trust and confidence in charities.
- Promote awareness and understanding of the operation of the public benefit requirement.
- Promote compliance by charity trustees with their legal obligations in exercising control and management of their charities.
- Promote the effective use of charitable resources.
- Enhance the accountability of charities to donors, beneficiaries and the general public.

Source: Charities Act 2011, section 14

2.29 The Commission does not have the capacity or capability to proactively monitor every charity on its register. It has 285 staff (full-time equivalent) and a budget of £21.2 million. In 2015-16, there were 165,334 charities on its register and it regulated £70.9 billion of charity income.

Monitoring and intervention

2.30 The Commission's functions include investigating misconduct and mismanagement in charities and taking remedial action in connection with this. Its specific powers include:

- information gathering powers to obtain information or require named individuals to meet them to answer questions;
- temporary powers to protect charity property while the Commission continues its inquiries; and
- remedial powers to implement long-term solutions to problems identified by an inquiry.

2.31 The Commission may open a statutory inquiry where there are serious concerns about abuse in a charity. It cannot impinge on the trustees' freedom to oversee the charity unless it can show serious failings. The Commission takes a risk-based approach to identifying, monitoring, and engaging with charities it has concerns about. It can take actions from concluding the trustees have matters in hand to opening a statutory inquiry. It told us that it uses a case risk tool to determine the level of risk presented by a charity.

Figure 10 shows the financial issues assessed by the tool.

Figure 10**The Charity Commission's case risk tool: financial issues**

Examples of financial issues that could warrant further investigation by the Charity Commission:

- Poor financial controls.
- Loss or misuse of charitable funds for an improper purpose.
- Financial mismanagement.
- Failure to submit accounts/annual returns.
- Irregular fundraising activity.

Source: Charity Commission

2.32 In August 2015, a Broken Rainbow employee complained to the Commission about cost-cutting measures and the excessive spending of charitable funds. The Commission assessed the case as low-risk, to be followed up when resources allowed. In January 2016, the Commission revisited the Broken Rainbow case. It found that only two of the seven trustees had registered with Companies House as directors of the company – all trustees should be registered as directors. It also inspected the charity's governing document, which suggested that the organisation may not have been exclusively charitable, in breach of charities legislation. Some employees and trustees of Broken Rainbow told us they contacted the Charity Commission in early 2016 with concerns about Broken Rainbow, but received no response. The Charity Commission told us that it has no record of this contact.

Errors in the Register of Charities

2.33 The Charity Commission's Register of Charities is the primary source of publicly available information about registered charities. The website contains information about charities' aims, their operational status, and financial information. We found errors in the information about Broken Rainbow:

- Broken Rainbow was listed as an active charity until November 2016, when, following our inquiries, it was updated to show the charity as being insolvent. Companies House listed the charity as entering insolvency in July 2016.
- There were errors about the information received: Broken Rainbow's 2014-15 accounts are shown on the register as being submitted in June 2015. The Charity Commission has confirmed to us that it had not in fact received these accounts, although they were submitted to Companies House.

2.34 The Charity Commission told us that it does not have the power to fine charities which submit late or poor-quality accounts; it does not have the resources to review every set of accounts it receives; and it is required by law to publish the information submitted by charities.

Companies House

2.35 Companies House incorporates and dissolves limited companies, registers the information companies are legally required to supply, and makes that information available to the public. It also has the power to remove companies from its public register.¹³ It is sponsored by the Department for Business, Energy & Industrial Strategy.

2.36 As a registered company and a charity, Broken Rainbow was required by law to provide Companies House with certain information, including notifying it of changes to its trustees (who are also directors of the company), and submitting its annual accounts and returns on a timely basis. Companies House received 2.7 million sets of accounts in 2015-16. While it does not have the capacity or capability to review in depth every set of accounts it receives, it will reject accounts that fail to meet the minimum examination requirements.

2.37 Broken Rainbow did not comply with its legal obligation to register directors of the organisation at Companies House. The people acting as directors and trustees are listed in the annual accounts. In earlier years we found that most people listed in the accounts were registered with Companies House: in 2012-13 everyone listed as a director was registered as one. In 2013-14, seven of the nine people listed as directors were not registered with Companies House, including the person who signed off the accounts as co-chair of Broken Rainbow. Between December 2015 and April 2016, the only person registered as a director was the CEO, although she was not in fact acting as a trustee at that point because it would have been a conflict of interest. There were a number of other people acting as directors who told us that they had given the necessary registration information to the former CEO, but it had not been submitted.

2.38 In the year before Broken Rainbow went into liquidation, Companies House actively monitored the charity's compliance with its requirements, and issued warnings and penalties relating to the late submissions of accounts and annual returns. These include:

- July 2015 – Companies House initiated prosecution action against two Broken Rainbow trustees following the late submission of the charity's 2013-14 annual return. In October 2015 it issued a court summons;
- January 2016 – Companies House issued a dissolution warning to Broken Rainbow and its directors, threatening the charity with closure. This was related to the late submission of its 2014-15 accounts. The former CEO argues she was not aware of the warning because Companies House sent correspondence to an old business address. Other trustees dispute this, and claim she withheld this information from the board; and
- March 2016 – Companies House published a public notice of its intention to close Broken Rainbow within three months if it did not supply accounts for 2014-15. The former CEO told us that she was not aware of this. The 2014-15 accounts were submitted to Companies House in May 2016.

¹³ This removal is sometimes referred to as a 'strike off'. When a company is struck off, its assets may be seized and its staff may have their employment terminated without notice.

HMRC had not notified the Charity Commission that Broken Rainbow had tax outstanding

2.39 HM Revenue & Customs (HMRC) is responsible for administering the tax system, including managing and reducing risks to the collection of tax revenue. It has a number of specific responsibilities with regard to charities, including responsibility for:

- tax reliefs provided to encourage giving to charities;
- the tax treatment of charities themselves; and
- working with HM Treasury, the development of charity tax policy and the technical aspects of the applicable reliefs and exemptions.

2.40 HMRC's charities team has a Memorandum of Understanding with the Charity Commission to facilitate the sharing of information. The latest memorandum was signed by both agencies in 2013 and sets out a number of specific information exchanges between the two bodies. Our 2015 report on the Charity Commission found that although the Commission exchanged more information with HMRC than with any other organisation, in some cases in the past neither the Commission nor HMRC shared all the information they could have done as specified in the memorandum.¹⁴

2.41 Broken Rainbow was required to make PAYE and National Insurance payments on the salaries of its staff, and to collect and transfer National Insurance and income tax payments from its staff to HMRC. Broken Rainbow could also claim Gift Aid and tax relief back from HMRC. It was never registered for VAT. When Broken Rainbow went into liquidation, it owed HMRC £32,000 in PAYE and National Insurance contributions. HMRC later increased this amount to £34,403. HMRC did not notify the Charity Commission of the circumstances surrounding Broken Rainbow's outstanding tax debts.

¹⁴ Comptroller and Auditor General, *Follow-up on the Charity Commission*, Session 2014-15, HC 908, National Audit Office, January 2015.

Part Three

Comparisons with Kids Company and managing the risks of grant funding to small charities

3.1 This part considers:

- the differences and similarities between Kids Company and Broken Rainbow; and
- lessons for public bodies awarding grants to small charities and recent work by government to improve grant-giving.

Comparisons with Kids Company

3.2 Some published articles and commentary about Broken Rainbow's demise have referred to the charity as the 'new Kids Company'. In October 2015, we published an investigation into the closure of the charity Kids Company, which had been funded by the government for at least 15 years.¹⁵ Broken Rainbow operated on a far smaller scale than Kids Company, which had received at least £42 million in government grants. We noted similarities and differences between the two charities.

Lobbying by charities and their supporters

3.3 Our report on Kids Company noted a pattern of lobbying and media coverage by the charity to secure further government funding. We noted Broken Rainbow had also adopted this approach:

- In January 2015, Broken Rainbow issued a press release announcing that the charity was 'broke' and on the brink of closure. Media articles to this effect then followed. In February an MP lobbied the Home Office to renew its funding commitment to the charity.
- In February and March 2016, media reports again cited financial pressures on the charity, saying it was on the verge of closure due to government cuts. Another MP then lobbied the Home Office to renew its funding to the charity.

3.4 The lobbying did not affect the Home Office's decision in principle to award funding for a further year, as this had already been agreed internally in January 2016.

¹⁵ Comptroller and Auditor General, *Investigation: the government's funding of Kids Company*, Session 2015-16, HC 556, National Audit Office, October 2015.

Weak financial and performance monitoring

3.5 Both charities had been under considerable financial stress for a number of years. For Kids Company, the government had been aware of this and taken steps to seek to address it. In our work on Kids Company, we set out the government’s ambition to secure its longer-term financial sustainability and reduce its dependence on central government grants (paragraph 1.8). For Broken Rainbow, the Home Office was not aware that Companies House had issued notice of its intention to close Broken Rainbow when it agreed a grant payment for 2016-17. Publicly available information showed that the charity’s reserves had fallen by 97% in three years (paragraph 1.9).

3.6 In both cases, government departments received very limited performance information about the use made of public money given to these charities. In its report on the government’s funding of Kids Company, the Committee of Public Accounts found that there “was insufficient scrutiny of what Kids Company was delivering for taxpayers’ money. Until 2013, the government relied heavily on Kids Company’s own assessments of its performance.”¹⁶ We would expect government departments to take a proportionate approach to monitoring arrangements, so we would not expect as much oversight of grants to Broken Rainbow as of grants to Kids Company, which received far more money. However, the Home Office did not have even the very limited information required on its monitoring forms, which in any case fell short of the requirements set out by the grant agreement.

Transition of services

3.7 We observed differences in the continuation of services following the closures of Kids Company and Broken Rainbow. Our report on Kids Company noted that the charity closed on 5 August 2015, and over the following fortnight the Department for Education and the Cabinet Office arranged to have Kids Company’s clients referred to local authority services. There was a smooth and uninterrupted transition for service users of the Broken Rainbow helpline, as it moved between providers without a gap in service.

Managing provider failure

3.8 We have previously set out some good practice principles for managing the failure of an organisation that provides services or goods to or on behalf of government.¹⁷ The Home Office’s arrangements for Broken Rainbow applied the principles in a number of respects, but did not do so around proportionate and appropriate monitoring arrangements so as to detect failure and early warnings of it. Although the Home Office has since revised its financial monitoring arrangements, these do not cover monitoring the financial health of providers, which can provide early warning of impending failure.

¹⁶ HC Committee of Public Accounts, *The Government’s funding of Kids Company*, Eighth Report of Session 2015-16, HC 504, November 2015.

¹⁷ Comptroller and Auditor General, *Principles Paper: Managing provider failure*, Session 2015-16, HC 89, National Audit Office, July 2015.

Changes to government's management of grants

3.9 In December 2016, the Cabinet Office's Grants Efficiency Programme launched its Government Grant Minimum Standards (**Figure 11**). The Grants Efficiency Programme aims to improve the effectiveness of government grants and strengthen guidance, training and best practice in relation to government grant-giving and the monitoring and evaluation of grant awards. In 2014, we reported that the programme was gaining momentum, although there was still more to be done.¹⁸ The standards seek to ensure that government grants are properly agreed and spent. They incorporate recommendations from the Committee of Public Accounts' and the Committee of Public Administration and Constitutional Affairs' inquiries into the collapse of Kids Company.

3.10 Following a critical internal audit report in March 2015 (paragraph 2.22 and 2.23) and the collapse of Broken Rainbow, the Home Office updated its internal guidance on grant monitoring and control in August 2016. It has also sought to implement the standards for managing grants six months ahead of the mandatory deadline.

3.11 The Cabinet Office standards for grant management (Figure 11) were not in place over the period during which the Home Office made grant payments to Broken Rainbow. If these standards had been applied to Broken Rainbow, it would have had to supply better monitoring information to give the Home Office confidence that its money was being spent as intended. The standards do not directly address monitoring the financial health of the provider – for example, to identify the collapse of a charity's reserves – however this could be covered as part of due diligence work that the standards require (Standard 7). They also do not explicitly consider the benefit of seeking to gain a full picture of a grant recipient's financial health by making use of information held, or made publicly available, by other parts of the public sector. Changes in charity accounting regulations mean that accounts covering the period starting 1 January 2016 will have to explicitly consider whether the charity is a 'going concern', so accounts could provide a useful source of evidence about a charity's financial health.

3.12 We have only examined one grant to one charity, so it is not possible for us to draw any wider conclusions about whether the failures to comply with established processes, in terms of monitoring the grant and regulating the charity, are widespread or whether this is a one-off. However, through this work we have identified a number of risks to grant-making to small charities – risks that do not appear to be addressed by the current regime, but which could potentially be mitigated without significant extra cost. The observations below are intended to help departments manage the particular risks of making grant payments to charities with an income of less than £1 million, and to make the best use of their limited resources for monitoring these grants.

¹⁸ Comptroller and Auditor General, *Government grant services*, Session 2014-15, HC 472, National Audit Office, July 2014.

Figure 11**Government Grants Minimum Standards**

The grant standards seek to promote effective grant applications across all government departments

Standard 1: named responsible officer for each grant

All government grants require a named senior responsible owner with clearly defined responsibilities throughout lifetime of grant.

Standard 2: grant approvals process

Departments will ensure they have a robust grants approval process to approve spend above £100,000, and that details of all current grant schemes and awards are available on the Government Grants Information System (GGIS).

Standard 3: new grants advice panel

New government grants, including those that are high-risk, novel and contentious, as well as those undergoing a step-change in scope or funding, should be considered for submission to the New Grants Advice Panel for scrutiny and advice from subject experts.

Standard 4: the business case

A robust business case, proportionate to the level of expenditure and risk, must be developed for all government grants. This will be scrutinised and approved in stages, as part of the grants approval process, in line with the guidance in *Managing Public Money*.

Standard 5: competition for grant funding

Government grants should be competed by default; exceptions may be approved where competition would not be appropriate. Detailed supporting evidence for any direct award decision must be provided in the approved business case.

Standard 6: robust grant agreements

All government grants must be awarded through robust grant agreements, proportionate to the value of the grant and which reflect the minimum standards for government grants, in line with guidance in *Managing Public Money*. All government grant agreements will include terms of eligible expenditure.

Standard 7: due diligence and fraud risk assessment

All government grants will be subject to timely and proportionate due diligence and fraud risk assessment.

Standard 8: defining outputs

All government grants will have outputs agreed and longer-term outcomes defined, wherever possible, to enable active performance management, including regular reviews and adjustments where deemed necessary.

Standard 9: annual reviews

All government grants will be reviewed annually at a minimum with a focus on financial reconciliation, taking into account delivery across the period, resulting in a decision to continue, discontinue or amend funding.

Standard 10: mandatory training for grant makers

All those involved in the development and administration of grants must undertake core training in grant management best practice.

Note

1 These standards were not in place at the time of the Broken Rainbow grants.

Ensuring value for money

3.13 There are limited formal governance and public financial reporting requirements for charities with an income of less than £1 million and very little proactive monitoring of whether charities comply with them. While this reduces the regulatory burden on charities, it means that departments receive very limited assurance about how a charity has spent public money. The Charity Commission told us that small charities may struggle to put in place the mechanisms needed to absorb high-value grant payments. With many of these payments being under the £1 million threshold departments should consider what extra action is needed to secure value for public money. This is particularly important as the government committed in the Autumn Statement 2016 to provide £102 million of fines from criminal activity in the financial sector (the LIBOR fines) to support charities and other good causes over the next four years. Financial monitoring arrangements should be risk-based, proportionate (particularly given the pressure of central government resources) and evidence-based. A one-size-fits-all approach is unlikely to work.

Monitoring grants and performance

3.14 Following the closure of Kids Company, the Committee of Public Accounts recommended that the government “should improve the way it monitors and evaluates the performance of grant-funded organisations including looking at the balance between self-reporting and external evaluation”.¹⁹ Broken Rainbow provided better information to other funders than it did to the Home Office (paragraphs 2.26 to 2.28). While it is important for departments to be mindful of the monitoring burden they place on small charities, it could be useful to ask to see copies of the monitoring provided to other funders.

3.15 We have observed instances where important information about Broken Rainbow was publicly available but was missed by the bodies involved owing to a lack of capacity or capability to investigate (paragraph 1.23). While manually checking information about every supported charity would be onerous and resource-intensive, there may be scope for organisations to do more with automatic alerts or web-scraping techniques, through which data can be automatically gathered from websites. This could include, for example, the registers published by Companies House or the Charity Commission and could help grant funders to stay informed of developments on a timely basis.

¹⁹ See footnote 16.

Appendix One

Our audit approach

Scope

1 This report looked into the funding and governance of the former charity Broken Rainbow. It covers:

- the funding, financial management and collapse of Broken Rainbow (Part One);
- the oversight of Broken Rainbow and its interactions with government (Part Two); and
- comparisons with Kids Company, and observations on the risks of grant payments to small charities (Part Three).

Methods

2 In examining these issues, we drew on a variety of evidence sources. We interviewed key individuals from:

- the **Home Office** to establish its oversight of the charity and its management of the grants;
- the **Government Internal Audit Agency** to understand its review of the Home Office's grant management;
- the **Charity Commission** to establish its regulatory role and subsequent investigation into Broken Rainbow following the charity's collapse;
- **Companies House** to discuss its role as a registrar of Broken Rainbow and its correspondence with the charity;
- **Broken Rainbow's board of trustees** and **former employees** to discuss their roles at the charity and, where applicable, their oversight of the charity's finances and general performance;
- the LGBT charity **Galop** to understand the transition of the national LGBT domestic violence helpline to it from Broken Rainbow and the costs incurred by this; and
- the **insolvency practitioner** handling the liquidation of Broken Rainbow to understand the scope of their investigation.

- 3 We have also spoken to the **former chief executive officer** of Broken Rainbow.
- 4 We reviewed a range of documents and other types of evidence to further establish our evidence base, including:
 - **quarterly performance returns** as sent to the Home Office from Broken Rainbow and Galop;
 - **quarterly records of expenditure** sent to the Home Office by Broken Rainbow;
 - **grant agreements and letters** between the Home Office and Broken Rainbow covering the 2014-15, 2015-16 and 2016-17 financial years;
 - a **Government Internal Audit Agency report** into the Home Office's grant management;
 - the **Memorandum of Understanding** between HM Revenue & Customs and the Charity Commission specifying conditions for the sharing of information between the two departments;
 - evidence from **HM Revenue & Customs** to understand the legal framework within which it can share information about its clients with other bodies;
 - **publicly available information** about Broken Rainbow and its finances, including information on the Charity Commission and Companies House websites, press releases and media articles;
 - **charity records** provided by trustees, former employees and the former CEO. Broken Rainbow filed for insolvency in June 2016 and its remaining assets are now held by its insolvency practitioner. The insolvency practitioner informed us that the charity's records were deleted remotely once they took possession of the charity's assets. While we have not been able to extract Broken Rainbow's records directly from its systems we have received a number of documents from individuals resembling charity records. We have included these documents in our evidence base if they are within the scope of our report and we have been able to verify their authenticity against other sources of evidence; and
 - we have also received evidence from **Companies House, Broken Rainbow's insolvency practitioner, London Councils** and the **Insolvency Service**.
- 5 We have conducted financial analysis of:
 - Broken Rainbow's **annual accounts** and **bank statements** in order to make observations about the financial management of the charity.

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