Highlights from September 25th Forum meeting

What are the essential updates for Treasurers on Audit and Risk?

Audit and Risk was the focus of our September Forum meeting.

The key areas of discussion were the recently updated Charity Code of Governance, the Financial Reporting Council's guidance in relation to the audit of charities, when to opt for Independent Examinations rather than audits, as well as research highlighting the top risks facing charities.

Our guest speakers were James Cross and Sandra De Lord from Kingston Smith, Alan Rawling from the Charity Commission and Kevin Thomas from Ecclesiastical who also sits on the board of the Charity's Special Interest Group (SIG) at The Institute of Risk Management.

An audit update from Kingston Smith

James Cross started by providing an audit update.

He reminded members that the Charity Commission has issued Update Bulletin 1 and that the FRSSE SORP has been officially withdrawn for smaller charities from 1st January 2016.

Also, larger charities with £500,000 or more income must prepare statements of cash flows and provide additional SORP disclosures. He added that the threshold for Audit and consolidation is organisations with of £1m plus.

James also referenced other key updates members should note. These included the Accounting Regulations 2008, which affect charities in England and Wales (not Scotland), the Charity Commission's (CC) 32 updated guidance on Independent examinations and the considerable number of new financial statement disclosures – including fundraising policies (CC20), FRS 102, amongst others. He said details of these can be found on the Charity Commission's website.

The updated Code of Governance

Next on the agenda was the updated Charity Code of Governance - its third rendition in 12 years. This most recent overhaul has received input from a steering group of sector specialists including AVECO, NCVO and others and reflects the challenges faced by the sector over the past two years.

The updated Code is not enforced by the regulator and the rule is not ‘comply or explain’ but ‘apply or explain.’ It also includes separate recommendations for smaller and larger charities.

The Code focuses on seven principles of good governance. These are: leadership; integrity; decision making, risk and control; board effectiveness; diversity; openness and accountability; all underpinning organisational purpose. Many of these principles are drivers of trust and confidence, and can help to demonstrate to beneficiaries, funders and donors that a charity is trust-worthy.

The Code encourages charities to use these principles to shape their governance and to take each principle as a starting point, explain its rationale, apply them and analyse the outcomes and document their impact in their annual report.

A ‘deep dive’ into Section 4

Section 4 of the Code focuses on decision making, risk and control and Kingston Smith’s Sandra De Lord focused on the requirements for small charities and the challenges these might entail.

The key recommended principle is:

“*The board makes sure that its decision-making processes are informed, rigorous and timely, and that effective delegation, control and risk-assessment, and management systems are set up and monitored.”*

The rationale behind this is:

“The board is ultimately responsible for the decisions and actions of the charity but it cannot and should not do everything. The board may be required by statute or the charity’s governing document to make certain decisions but, beyond this, it needs to decide which other matters it will make decisions about and which it can and will delegate. Trustees delegate authority but not ultimate responsibility, so the board needs to implement suitable financial and related controls and reporting arrangements to make sure it oversees these delegated matters. Trustees must also identify and assess risks and opportunities for the organisation and decide how best to deal with them, including assessing whether they are manageable or worth taking.

The key outcomes are:

1. The board is clear that its main focus is on strategy, performance and assurance, rather than operational matters, and reflects this in what it delegates.
2. The board has a sound decision-making and monitoring framework which helps the organisation deliver its charitable purposes. It is aware of the range of financial and non-financial risks it needs to monitor and manage.
3. The board promotes a culture of sound management of resources but also understands that being over-cautious and risk averse can itself be a risk and hinder innovation.
4. Where aspects of the board's role are delegated to committees, staff, volunteers or contractors, the board keeps responsibility and oversight.

Sandra highlighted areas that would be challenging for smaller charities – all of which are documented in Kingston Smith's presentation slides. However, here are a couple of examples:

What are the challenging principles for smaller charities? The section numbers refer to those within the Code.

4.5.1 The board regularly reviews which matters are reserved to the board and which can be delegated. It collectively exercises the powers of delegation to committees or individual trustees, or staff and volunteers if the charity has them.

The challenge here is that small charity might only have one or two trustees and no committees so how can it delegate? Also, if it is delegating, how are these delegations to be documented and agreed? When are they going to be reviewed? All of this has major time and resource implications for small charities.

4.5.2 The board describes its 'delegations' framework in a document which provides sufficient detail and clear boundaries that the delegations can be clearly understood and carried out.

Again, this would be challenging for a small charity who might need to create a delegation framework and monitor whether the details included in the framework happen in practice.

Sandra recommended that smaller charities start with a simple organisation chart, with clearly defined roles and responsibilities and that they also need a clear understanding of what reporting was needed too.

4.5.5 The board regularly checks the charity's key policies and procedures to ensure make sure that they still support, and are adequate for, the delivery of the charity's aims. This includes: policies and procedures dealing with board strategies, functions and responsibilities, finances (including reserves), service or quality standards; where needed, good employment practices and encouraging and using volunteers; key areas of activity such as fundraising and data protection.

Here the key challenge for smaller charities would be keeping up to date with the many key policy and procedure changes.

Sandra quoted Donald Rumsfeld who said, “expect the unknown unknowns” – think about what might be around the corner about to hit you.

Another recommendation was for trustees to keep up to date with the what is going on in the press and also to ensure they access any guidance that is out there and available for free - this could include policy updates from the Commission or tools such as the governance tool kit offered by Kingston Smith.

4.7.1 The board retains overall responsibility for risk management and discusses and decides the level of risk it is prepared to accept for specific and combined risks.

Managing risk is another potentially difficult area for small charities. How do smaller charities ensure they have the right appetite for risk and where is this on the scale? How can they ensure risk management encompasses all the key risk areas? What could come out of the blue? Do the trustees have the right level of sector knowledge? Have they considered how they would respond to emerging risks such as cybercrime and data protection? Again, Kingston Smith referenced its Charity Risk Toolkit as a helpful resource for smaller charities.

Other challenging areas outlined for charities in section 4 were issues around ensuring charities have the right Chair to lead them, having the ideal size board of between 5 and 12 trustees (no more), setting the right terms of appointment, reporting on remuneration and ensuring the recruitment of a diverse range of trustees – again all issues that can prove challenging for smaller organisations.

What’s in the Code for larger charities?

5.8.2 (larger code) - The board reviews its own performance and that of individual trustees, including the chair. This happens every year, with an external evaluation every three years. Such evaluation typically considers the board’s balance of skills, experience and knowledge, its diversity in the widest sense, how the board works together and other factors relevant to its effectiveness.

Larger code also has expanded areas on impact reporting and governance reporting.

2.What are the top risks facing UK charities?

Our next session was led by Kevin Thomas from Ecclesiastical Insurance who is also at the Institute of Risk Management and involved with the Charities Special Interest Group (SIG).

Kevin explained that the group aims to demystify risk management for charities and help them become more robust and better able to deal with and bounce back from shocks.

In 2015 the SIG launched a ‘Getting Started’ campaign offering guidance, presentations, videos and newsletters to help its members understand their risks.

This was followed in 2016 with a ‘Getting better’ campaign, which laid out a framework to help charities improve their risk assessment.

This year it conducted research looking in detail at the risks facing charities. The full details of the research are included in the accompanying slides.

Key findings of the research

Many diverse risks were highlighted in the research. These included fundraising, information governance, cyber-crime, safeguarding, health and safety and security as well as the loss of public confidence, trustee governance, fraud, financial sustainability, ageing population and changing dynamics in terms of giving.

However, five risks were clearly identified by most respondents:

1. Financial sustainability – with risks around the duty of care for staff and volunteers
2. Financial sustainability in terms of volunteer management
3. Fundraising - data protection issues and issues and risks around employee retention and quality
4. Health, safety and security
5. Organisational resilience and continuity

Kevin said that no one would be surprised to see financial stability at number one. The competition between charities, the reliance on local authority contracts, the commissioning process, pressure for funds, reduced public spending and competition for funds are all issues affecting financial stability.

But what can charities do?

Kevin advised that charities needed to diversity their portfolios, focus on their core mission and specialisms amongst other advice and be careful which contracts they take.

He also acknowledged the new data protection laws and the forthcoming GDPR were big challenges charities were having to get to grips with and major risks associated with getting it wrong.

He said that different divisions within charities should work closely together to ensure a joined-up approach to fundraising which will help with compliance. He added that now is the time to diversity income streams and end the over reliance on single revenue streams.

He added that health and safety and security risks can be reduced with good training, check lists, controls, risk registers and by encouraging a top down values culture that permeates an organisation.

In terms of improving organisational resilience he said that if you get a shock you want to be able to recover from it. In such situations, he advised people take time out and spend time thinking and working through ‘what if ‘scenarios to devise strategies and tactics if things go wrong.

3. Independent examination of Accounts for examiners CC32 –new irections and guidance

Lastly, Alan Rawling from the Charity Commission provided insight into the updated directions and guidance on independent examinations for charities (CC32) which was published on 4th September.

He explained the drivers behind the new directions and guidance were:

- The independent examination framework has not had a major review since the Charities Act 2006

- Examiners (and auditors) are our first line of defence against mismanagement in charities.

- The doubling of the income audit threshold from 31 March 2015 has brought more, larger, charities within the scope of examination. There was also an updated list of matters of material significance reportable to the regulator came into force on 1 May 2017

Which organisations need to have an independent examination?

- 62% of charities are not required to have any external scrutiny of their accounts (income less than £25,000)
- 6% of charities must have an audit of their accounts (income £1 million or £250,000 and gross assets £3.26 million)
- 32% of charities may opt for an independent examination of their accounts instead of an audit (income £25,000 but below the audit threshold)

So, what is new in the Directions and Guidance?

The original 10 Directions remain (detailed in the presentation slides) and three new ones have added.

There are three new Directions, covering the independence of the examiner, related party disclosures and the trustees' consideration of the charity's financial circumstances. These are detailed in the accompanying slides.

Section 4: there is guidance for examiners of small charity group accounts (we will accept them if the guidance is followed)

Sections 5 & 6: the guidance on reporting matters of material significance and relevant matters to the UK regulators has been updated (new duties to report 'qualified' examiner's reports and concerns over conflicts of interest and related party disclosures)

Alan finished by providing some advice on how to ensure an examination goes well. He recommended that boards:

- Read CC32, to understand what is involved in an examination and the information that the examiner will need

- Agree with the examiner who will prepare the set of accounts. The examiner may assist, but the trustees must ‘own’ and approve the trustees’ annual report and accounts
- Agree a timetable for preparing the trustees’ annual report and accounts and for the examination itself
- Make the accounting records and key documents available to the examiner and check that they are up to date
- Ensure that trustees and any key staff are available to answer questions

Alan closed his session by saying the Charity Commission will shortly be undertaking a new consultation to bring CC31 Independent Examination of Accounts: guidelines for trustees up to date. He invited HTF members to send their contributions and ideas on how it can be improved and HTF’s CEO Denise Fellows offered to co-ordinate this on behalf of the members.