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Kids Company - The lessons no trustee can afford to ignore

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In early February 2016, the House of Commons Public Administration and Constitutional Affairs Committee (the Committee) published its report into the collapse of the charity Kids Company. This important report contains recommendations and lessons that no one who is a trustee of a charity can afford to ignore.

Whilst being a charity trustee should be a rewarding and exciting experience, the position of trusteeship is one of the most onerous responsibilities an individual can take on. In its publication, The Essential Trustee (CC3), the Charity Commission makes clear: "to be a trustee requires time, understanding and effort" and "good intentions aren't enough to fulfil your responsibilities". These are sentiments echoed in the conclusions of the Committee's reports.

The Collapse of Kids Company

Background

Kids Company was founded in 1996 by Camilla Batmanghelidjh with the aim of providing practical, emotional and educational support to vulnerable children and young people. Over the course of its existence it received government grants in excess of £42 million but its demand-led operating model meant that financially it was always on a "knife-edge". The charity closed on 5 August 2015, following the launch of a Metropolitan Police investigation into allegations of sexual abuse at the charity. These allegations emerged on the same day that the Government released a grant of £3 million to the charity intended to enable an emergency restructure. The police investigation has subsequently been closed, having found no evidence to support the allegations of abuse. However, the allegations meant that potential funders and donors disappeared and this, given the charity's already precarious financial position led, ultimately, to its collapse.

Governance - findings and lessons

Risk management

Kids Company was founded on the premise that no child should be turned away – it was "demand led" with the ability for children to refer themselves to the charity for help. Inevitably, this led to a continuing risk that there would be a significant gap between the charity's resources and its ability to deliver on its commitments to its beneficiaries. The Committee found that the charity's trustees failed to address this risk, relying instead on wishful thinking and false optimism. Whilst many good charities and companies are founded on a vision based on idealism, to be successful in the longer term, it is essential that such idealism is balanced with a sense of being grounded in reality.

Financial reserves

In the case of Kids Company, its demand-led operating model meant that its financial reserves were always very low. The Committee found that the charity's trustees failed to take action to address the charity's long standing weak financial position. Their financial management was described in the Committee's report as "negligent" – its reserve policy was woefully inadequate with no long term commitment to build reserves. The aim of "working with Government to identify sustainable and long term funding" ranked only seventh out of the charity's ten priorities for 2014. The trustees had ignored warnings from the charity's auditors and a warning by HMRC that the charity's model was not viable. The Committee found the trustees of Kids Company in doing this had failed in their duty of care towards the charity's clients, employees and donors.

The lesson: Charities need to have a clear and considered reserves policy setting out their ideal level of free reserves and then monitor the actual reserves against that policy, agreeing on the actions needed to bring the two in line with one another. Those in particular that employ staff and work with vulnerable beneficiaries or have other long term commitments, need to prioritise the building of financial reserves and set their reserves policy at a level that will ensure resources will be sufficient to meet commitments. Charities need to avoid setting their policies for reserves at a lower than realistic level simply to try and attract funding from donors and donors, especially grant funders, should question the prudence and responsible approach of those charity trustees which appear not to have financially viable operating models. It is hoped that grant funders will carry out full and proper due diligence and supply those charities that will provide high quality services and outcomes with which the funder may then be linked indirectly.

Reliance on auditors

The charity's trustees placed over reliance on the unqualified audit reports issued by the auditors. It was noted by the Committee that its inquiry served as a reminder to all who use charity accounts that a set of audited accounts do not provide assurance that charitable funds are being used wisely or that the charity is well run.

The auditors' post audit reports did contain significant warnings to the charity about the precariousness of its demand-led model and the dependency of the charity on the success of future fundraising and grant applications. The Committee believed that the meaning of such warnings should have been clear to the CEO and trustees and have led to a change to the reserves policy, contingency planning for insolvency and substantial downsizing years before the final crisis.

The lesson: It is important that those charged with governance take the opportunity to talk to the charity's auditor at least once a year at a meeting at which the audit findings are presented and to discuss any recommendations coming from the audit and management's response to them. Ideally, an opportunity should be created at some point in such a meeting whereby the trustees and the auditor may have a discussion without members of the executive team present.

Challenging the Chief Executive

The Committee also criticised the lack of challenge by trustees into the number of clients the charity was claiming to have supported. The fact that the robustness or basis of such statistics was never questioned resulted in the trustees being either ignorant of the exaggerated figures for the charity's caseload or simply accepted them as they assisted fundraising.

The lesson: A key responsibility of trustees is to challenge and ask questions of those responsible for the day to day work of the charity – its Chief Executive and the executive team.

Taking note of reports from regulators

Other than Kids Company's early years provision (The Tree House), the charity's education programmes were not subject to statutory inspection. The Department for Education commissioned Ofsted to inspect the charity's Bristol facilities on two occasions and in both instances Ofsted expressed concerns. The charity's trustees were either unaware of these concerns or they simply failed to act upon them. Both scenarios suggest serious failings in governance. If the information was withheld it suggests a significant lack of trust or communication between the trustees and executive team and if it were not acted upon at best it demonstrates a clear lack of understanding for the seriousness of the regulator's concerns. The Committee believes that there is a strong case for the statutory regulation of charities which have safeguarding responsibilities for children or vulnerable adults and has recommended that Government consider how this might be brought about as quickly as possible.

The lesson: Communication between a charity's executive team and its trustees must be such that the trustees are informed of all inspections and receive draft reports. The trustees must consider the content of such reports and be able to contribute to responses in the development of actions arising. Thereafter, the trustees should expect to receive updates from the executive team on progress against such action plans.

Trustee skills and experience

None of the charity's trustees had any background in youth services and as a consequence there was an over reliance on research reports that supported the charity's methods and model rather than considering whether the model was working. The Committee heard that the charity "was not good at measuring its outcomes and the impact it was having on society". There was found to be a lack of robust evaluation of the impact and outcomes of the charity. As a result there is little evidence to show on what basis the trustees satisfied themselves of the appropriateness of support given to clients and the value for money offered by the high resource model. This approach left the trustees unable to defend the reputation of the charity, a prime obligation of good governance and leadership for any organisation.

The lesson: A charity's board needs to ensure it has a breadth of skills and experience. In addition to ensuring that key areas of expertise such as accounting and finance, legal knowledge, a working knowledge of human resources, etc. are covered. It is essential that there are trustees with a detailed understanding of the specific sector in which the charity works and of its activities. Only then can questions be asked that are relevant and able to tease out what real impact the charity's work is having on its beneficiaries and on society more generally i.e. its outcomes.

The application of expenditure

The charity was found to have spent considerable sums on providing luxury items to particular individual clients which diverted charitable funds from other projects or programmes that had the potential to provide longer term and more effective support to a wider group of young people. The Committee asked why the trustees did not examine the extent of the lavish expenditure questioning whether it was appropriate and a proper use of charitable funds. Despite the charity's known cash flow problems, including difficulties in meeting its payroll and related payments to HMRC, the authorisation of such payments by the charity's chief executive went unchallenged by the trustees. Whilst this would, in part, have been due to their lack of experience of youth services it was considered extraordinary nevertheless.

The lesson: Charity trustees must understand the charity's financial position and be prepared to challenge whether expenditure is being applied in furtherance of the charity's objectives, whether it is targeted in the most appropriate areas and demonstrates value for money. This aspect includes the review of budgets ensuring that they reflect the charity's overall strategy, the monitoring of actual results against budget, taking decisions to address cash flow concerns and linking the financial results to the charity's outcomes.

The handling of complaints including safeguarding issues

The Committee found that there was a serious failure on the part of the trustees to ensure the existence and observance of appropriate processes for handling allegations relating to the safeguarding of vulnerable young people. The Committee found that the charity's handling of an allegation about a very serious failure of safeguarding was "inadequate and irresponsible". An initial investigation of the allegation had been carried out by someone who was not deemed to be objective by the individual making the allegation and the subsequent report contained information about the informant that had not been shared during the investigation and which was used to judge them as unreliable.

The lesson: A key responsibility of charity trustees is to protect their charity's reputation. Complaints about the charity's services, its work or those who work or volunteer for it need to be followed up on a timely basis, investigated and responded to. Those charities working with children and/or vulnerable adults need to always be alert to the charity's safeguarding policies and investigate immediately any allegations of failures. Investigations must be seen to be independent, robust and fair with all procedures followed properly.

Founders syndrome

Ms Batmanghelidjh, the founder of Kids Company, has been described as an "emblematic figure" who possessed extraordinary fundraising capabilities. It was said that she was "very much in control of what went on. The ethos, the way in which things were run, the general comportment of the organisation." The Committee heard that there was no evidence that the trustees were involved in a decision to turn down a philanthropist's offer of significant financial and human resource at a time when the charity desperately needed the money. The fact that Ms Batmanghelidjh cited a mere intuition of the potential donor's supposed lack of emotional authenticity as a justification for blocking an exploration of a new partnership at a time of extreme financial difficulty for the charity, underlines how unaccountable and dominant trustees had allowed her to become and how far she was able to insist on maintaining personal control.

The lesson: Whilst "founder's syndrome" can be a risk for some charities, the trustees should always make decisions solely in the charity's best interests and not allow their judgement to be swayed by personal prejudices or dominant personalities.

Over familiarisation

The Committee noted also the fact that both the charity's CEO and Chair of trustees had both been in office for at least 12 years and stated that this was not conducive to the Chair being able to question the CEO. There was said to be a clear link between the failure to correct serious weaknesses in the organisation and the failure to refresh its leadership.

The lesson: Whilst a good working relationship between a Chair of trustees and a charity's Chief Executive is crucial to the sound governance of the charity, it is important that the relationship does not become too "cosy". Both individuals should be aware at all times of their role and the reporting mechanisms. Ideally, the Chair of trustees should have a "job description", part of which should be to hold the Chief Executive to account, carrying out their performance review and setting objectives and priorities.

Governance - summary

A charity the size and complexity of Kids Company needed a board of trustees that demonstrated leadership, judgement and a willingness to challenge assumptions. There was a lack of a trustee with experience of youth services. The vision and fundraising capabilities that Ms Batmanghelidjh demonstrated led to the trustees having false confidence about other aspects of the organisation. They allowed themselves to be swayed by personal prejudice and a dominant personality meaning that they were unable to be objective about the appropriateness of the demand led model, the existence of her substantial discretionary spending powers, the effectiveness of internal controls and the quality of clinical judgements and safeguarding procedures.

The Chair of trustees denied failures in financial management and denied there were any questions about the charity's financial resilience until 2014. The Committee found this an inaccurate and alarming interpretation given the charity's historic hand-to-mouth existence, its continual failure to build up reserves, significant periods on the brink of insolvency and its inability to meet its obligations to HMRC. Together with his fellow trustees he was unwilling to exercise sufficient control and as such they had all failed in their proper function as trustees.

Others subjected to criticism

The trustees were not the only group who were singled out for criticism or two. The Committee was critical of the charity's auditors, the Charity Commission and Whitehall.

Auditors

The auditors were found not to have been robust enough in their warnings about the charity's financial position and it was found surprising that they did not consider their duty to alert the Charity Commission to the extremely high risk of failure in the charity.

The auditors were found to have been overly confident in the charity's internal controls which influenced the sampling process and the level of scrutiny to which the charity was subjected and to have misplaced confidence in the charity's management.

Charity Commission

The Committee found it remarkable that so few people found it appropriate to complain to the Charity Commission about Kids Company, despite donors and others expressing concerns for many years. This highlights the Charity Commission's failure to make people aware of the ability to make complaints which would have prompted investigation. The Committee stated that the Commission must do more to make the public aware that they can and should take their concerns about a charity to the Charity Commission. In addition, the Commission should investigate any adverse media reports about a charity and encourage journalists to make formal complaints to the Commission.

The Charity Commission was found to have only had substantive discussions with the charity about its precarious financial position when the charity's finances reached crisis point. It had relied too much on government engagement with an organisation as evidence of a charity's good governance or effectiveness.

The Committee welcomed the proposed tightening of the Charity Commission's powers as part of the Charities (Protection and Social Investment) Bill. This gave the Commission the power to disqualify a person from being a trustee under certain conditions; if the person is unfit to be a trustee or if it is in the public interest in order to protect public trust and confidence in charities.

The Committee stated that the Charity Commission must have the resources and powers to advise and investigate charities at an earlier stage and to support charities through restructures and downsizing. In addition, the Committee stated that the Commission must have resources to enable it to interrogate charity accounts – particularly those of charities with a large number of employees or a vulnerable client base. The Committee recommends that the Treasury and Cabinet Office address the future funding of the Charity Commission so that it is able to carry out its functions in a way that the Government, charities and the public expect.

Whitehall

The Committee stated that if Government decides to use special powers to grant funding it should provide a transparent case for its decision. It stated also that ministers should not allow charity representatives to exploit their access to Government in a way that may be unethical.

There must be no suggestion that individual ministers have funds under their personal control and the Committee noted that it should be for relevant departments to control grants, not the Cabinet Office or another department that does not have direct responsibility for the sector in which the charity operates.

The Committee made a strong recommendation that the Government should undertake a fundamental review of how it makes direct and non-competitive grants to the voluntary sector and improve the way in which it monitors and evaluates the performance of grant funded organisations.

Conclusion

Those of us who work with or in the charity sector do so because it is something we believe in passionately. The charity and voluntary sector is highly important to the country – not just because of its economic and financial contribution or because of the number of people that work within it but because, in making society a genuinely better place, it has a positive impact on all our lives. The collapse of charities in circumstances such as those surrounding Kids Company carries with it the risk of damaging the reputation of the whole sector and hence of denting the public's trust and confidence. We cannot afford to let this happen and, as a consequence, it is essential that the lessons are learned by all and that the recommendations in the report of the Public Administration and Constitutional Affairs Committee are seen to have been acted upon.

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