

**DSC response to Charity Commission policy  
paper**

# **Official warnings to charities and trustees**

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## 1. Background

The Charities (Protection and Social Investment) Act was passed in March 2016 after several years of consultation, draft legislation and parliamentary scrutiny, particularly in the House of Lords. Much of the Act is uncontroversial, and closes a number of loopholes which the Charity Commission has said will help it deal with difficult enforcement cases. However, **a number of the powers, particularly under Sections 1, 9 and 10 of the Act, are highly problematic** in DSC's view and that of many established and respected charity lawyers.

Section 1 of the Act gives the Charity Commission a new power to issue official warnings to charities and charity trustees, when it considers there has been a breach of trust or duty, or other misconduct or mismanagement. The power is intended to give the Commission another regulatory tool in between a full statutory inquiry (where the Commission can direct the charity's trustees to act or cease acting, and can even remove them entirely), and a simple letter outlining best practice, guidance or remedial action (which trustees might not be bound to heed). The power is intended to be used for lower-level problems as a more proportionate approach than a statutory inquiry.

During the passage of the Act, DSC and others argued that this new power was flawed in a number of ways, and a number of amendments were unsuccessfully proposed. There are no guarantees that it would be used only to deal mainly with lower level problems; a warning could damage a charity's reputation unfairly if made incorrectly or on faulty evidence (for example, any PR damage resulting from a warning made in error could not be easily or entirely undone); there is no right of appeal to the Charity Tribunal; and the period of notice to allow trustees to respond is insufficient.

Partly in answer to these concerns, during the passage of the Act Section 1 was amended by the Government to allow the Commission to vary or withdraw a warning, and the Minister stated that normally there would be a 14 day notice period for warnings, allowing trustees to make representations to the Commission. Crucially however, warnings cannot be appealed and they will be published. There is also no guarantee that the 14 day notice period will be followed – in fact in the policy paper the commission says there will be circumstances in which it is not appropriate to provide any notice.

## 2. Responses to questions in Commission's consultation paper on official warnings

DSC's responses to specific questions about the use of the new power presented in consultation documents by the Charity Commission are provided below. The format of the sections and questions (in italics) is reproduced, followed by DSC's response.

## 2.1 General views and comments

*Having read the draft guidance, do you have any views or comments on how the commission proposes to use official warnings?*

Yes. The guidance clearly outlines when the commission can issue an official warning and who the Commission can issue an official warning to. It says that warnings are unlikely to be issued for minor breaches or where risk is minimal, and explains the circumstances under which a warning might be used.

DSC has already made its broader concerns about this new power known throughout the passage of the Act. Where this guidance is concerned, one issue which remains unclear is the question of 'mismanagement' resulting in 'a charity's reputation being harmed', and this being potential grounds for a warning.

Trustees do have a duty to protect their charity's reputation, but this is not always within their control. Further, questions of whether there has been reputational damage, whether trustees could have prevented it, and whether it actually matters to the fulfilment of the charity's objects or its ability to serve its beneficiaries are not objective questions – they depend on subjective interpretation and may be disputed.

There is a risk, given the number of recent negative media headlines about charities (many of which have been clearly biased or factually incorrect) and the Commission's current aggressive posture towards the sector in general, that in future warnings will be issued on the back of negative media coverage without sufficient balance or basis in fact. The warning power must not become a 'power to pillory', but must be used in the proportionate way that it has been intended.

For example, if a charity is involved in campaigning which is within the law, but potentially controversial, and this results in negative comment from some sections of the press, does this constitute reputational damage and hence 'mismanagement' giving grounds for the commission to intervene and issue an official warning?

The power to issue warning must also not become the go-to option because the Commission lacks the time, resources or willingness to conduct a fair investigation into the issues. While it is a halfway power between a letter and a statutory inquiry, it should not be seen as 'the easier option' by the Commission and a means of achieving 'enforcement on the cheap'.

*Do you have any views or comments on action the commission might take following an official warning?*

Not at this time.

## 2.2 How the commission will use this new power – principles and examples

*Do you have any comments on the factors that the commission will take account of and examples of when it might issue an official warning, as explained in the draft guidance?*

Not at this time.

*Are there particular circumstances in which you think the commission should issue an official warning?*

We are unable to provide any at this time.

*Should charities that repeatedly or persistently default on statutory accounting and reporting requirements automatically be issued with official warnings?*

Yes. Providing timely and correct annual accounts and reports is fundamentally important to the system of charity regulation in this country. It is a critical obligation of charities to do this to demonstrate transparency to the public. Repeated failures to submit reports and accounts for example, should incur a warning or even more robust regulatory action by the commission. However, the commission must take a proportionate approach and recognise that it may make administrative errors, so the phrase ‘repeatedly or persistently’ is key – there must be a clear pattern to justify an automatic warning, rather than a one-off problem. It is also important that ‘automatic’ is not taken to mean that a notice period is not required before the warning is published. It is important that trustees have time and opportunity to make representations.

## **2.3 Notice and representations**

*The commission proposes that 14 days should be the normal minimum notice period for an official warning. Do you agree, or do you think notice should normally be shorter or longer than this?*

The normal minimum notice period should be more than 14 days to be proportionate for the vast majority of charities, which are small and predominantly run by voluntary trustees. There should be a notice period of at least one month.

This is because trustees must have sufficient time to a) receive notice of the warning, b) communicate it to each other c) establish the facts of the matter d) be quorate to discuss and agree any response. Small charities may not be in a position to convene their board of trustees quickly, and may not receive communications from the commission in a timely manner.

*Do you have any comments on the commission’s proposed approach to considering representations on official warnings?*

Yes – the length of the notice period is critically tied to the ability to effectively make representations and prevent any unwarranted reputational damage. If the commission is

incorrect, or the charity has complied with previous advice and the commission was unaware of that for whatever reason, this requires time to establish. Once the warning is issued (and published) any ensuing reputational damage to the charity will be very difficult to remedy after the fact (notwithstanding a withdrawal or variation of the warning by the commission).

## **2.4 Publishing official warnings**

*The draft guidance explains the approach the commission proposes to take on publishing official warnings, based on public interest considerations.*

*Do you agree with the approach set out in the guidance?*

Partly – however there is insufficient explanation about how warnings will be published; in particular how they will appear on the charity's record on the register. The circumstances and reasons for any warning need to be explained, as there will be gradations of severity for different circumstances; for example if the warning was about a specific trustee or the charity as a whole. A 'red flag' by itself on the register will achieve little except deterring the public from involvement with the charity.

The time period of 'two years' for including a warning in the register is arbitrary. If the charity has fully resolved the problem for which the warning was issued, the red flag should be removed in a timely fashion. This might be two years in the case of failure to submit reports and accounts, but it might be two weeks in other circumstances. In fact, in cases where the charity is notified of the Commission's intention to issue a warning and the charity has rectified the problem immediately, it does not seem necessary for the warning to be published at all. It must be noted that continuing to apply a 'red flag' to a charity after they have rectified a problem would be misleading to the public as it suggests there is a problem where there actually is none.

How will the commission make these judgments, and how will it keep the decision to include a 'red flag' under review? If the issue has been resolved, how will a charity be able to effectively press the commission to remove the flag in a timely manner, given the many pressures on the commission's resources?

It is unclear how the warning will be published where it is issued against an individual trustee.

*Do you agree that the commission should usually publish warnings on its website for two years (unless a warning is withdrawn before then)?*

No – see above.

*Do you agree that the commission should usually highlight published warnings on a charity's page in the central register?*

Yes – but subject to the considerations discussed above. Any warning (and the length of time it is present) needs to be proportionate, explained, and current.

## **2.5 Other comments**

The guidance is generally clear and gives the context for how the commission will use the new power. However there are a number of questions which the commission still needs to address, in particular:

- How warnings will be used in the context of 'mismanagement' and 'damage to reputation';
- The insufficiency of 14 days as a notice period – one month is needed as a minimum;
- How warnings will be published on the register (and how they will be removed).
- Whether past warnings will be used against a charity in future compliance cases.

The final section of the discussion paper points out that official warnings cannot be appealed to the Charity Tribunal but that the Commission's subsequent action can be. This was discussed and debated during the Act's passage through parliament. However it is true that trustees could seek redress through the courts or seek a judicial review if they wished to.

## **3. About DSC**

The Directory of Social Change has a vision of an independent voluntary sector at the heart of social change. We believe that the activities of charities and other voluntary organisations are crucial to the health of our society.

Through our publications, courses and conferences, we come in contact with thousands of organisations each year. The majority are small to medium-sized, rely on volunteers and are constantly struggling to maintain and improve the services they provide.

We are not a membership body. Our public commentary and the policy positions we take are based on clear principles, and are informed by the contact we have with these organisations. We also undertake campaigns on issues that affect them or which evolve out of our research.

We view our role as that of a 'concerned citizen', acting as a champion on behalf of the voluntary sector in its widest sense. We ask critical questions, challenge the prevailing view, and try to promote debate on issues we consider to be important.

DSC has a long-standing interest in charity law and the Charity Commission.

#### 4. DSC's principle of Responsible Regulation

DSC believes that voluntary activity should be regulated responsibly. Some regulation is necessary to safeguard and maintain the interests of the general public, the beneficiary, and of the organisations and individuals being regulated. However, it should have a demonstrable benefit and should aim to empower and strengthen voluntary activity rather than control it unnecessarily. We believe that:

- a) Regulation should be **proportionate** – it must strike a balance between perceived risk and intended benefit. It should recognise the diversity of voluntary sector activity and be developed and applied in a proportionate way.
- b) Regulation should be **appropriate** – it must be informed by the characteristics, capacity, and needs of the organisations and individuals that are being regulated. Insofar as is possible it should be focussed, rather than acting as a blunt instrument that has unintended effects.
- c) Regulation should be **enabling** – it should seek to empower rather than control voluntary activity. The reasons for the regulation and the regulation itself must be properly understood by those institutions which are applying it. It should be accessible and intelligible to those being regulated. It should seek as far as possible to encourage self-regulation rather than focus simply on enforcement.