REGULATION AND ACCOUNTABILITY OF NORTHERN IRELAND’S CHARITY SECTOR

The Importance of Regulation, Accountability and Trust

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1. Definition, Size and Regulation

In both the United Kingdom (UK) and the Republic of Ireland (RoI), an organisation is considered to be a charity if its purposes are deemed to be ‘charitable’ and those purposes are for the ‘public benefit’ (with the law in each jurisdiction specifying how such factors are determined). For example, to be a charity in Northern Ireland (NI), an organisation must have purposes which fall under one of 12 listed in the Charities Act (NI) 2008. These purposes include the prevention or relief of poverty, the advancement of amateur sport, animal welfare, education, health (including saving lives), human rights and religion.

The charity sectors in the UK and RoI are vast and growing segments of economic activity with substantial assets at their disposal. Their activities are pervasive, often highly visible and can include fundraising, grant making and trading. In the UK, there are over 200,000 registered charities with an estimated total annual income approaching £80 billion. In NI alone, there are approximately 10,000. The UK charity sector employs over 600,000 people, up 25% over the last decade, and the public is increasingly engaged in voluntary activities, with 45% of the public volunteering at least once a year and 29% at least once a month. In RoI, although it is more difficult to get accurate estimates of numbers and economic significance (partly because of a regulatory framework more in its infancy), it is estimated that there are over 8,000 charities, which are a subset of a larger not-for-profit (NFP) sector of 12,000 organisations with an annual income of approximately €6 billion (approximately £5.3 billion). Here, the NFP sector employs more than 100,000 people and has over 560,000 volunteers.

Under the 2006 Charities Act, the Charity Commission in England and Wales has been charged with the responsibility of: (i) enhancing charity accountability to donors, beneficiaries and the public; (ii) increasing public trust and confidence; and (iii) promoting the effective use of charitable funds in that jurisdiction. In Scotland and NI, the Office of the Scottish Charity Regulator (OSCR) and the Charity Commission for Northern Ireland (CCNI) fulfil similar roles. In RoI, the Department of Justice, Law Reform and Equality is responsible for charity regulation, with the Charities Regulatory Authority (CRA) being established in October 2014.
With reference to NI specifically, CCNI is a non-departmental public body, established by Royal Assent in March 2009, to deliver the legislative requirements of the Charities Act (NI) 2008. It is responsible for ensuring NI has a dynamic and well-governed charities sector in which the public can have confidence. As the independent regulator of NI charities, CCNI has a crucial role to play in enabling charities to meet modern expectations and obligations.

2. A Changing Sector
Regardless of the size they may have, charities play a significant and vital role in society, often serving and helping those who are most disadvantaged, marginalised or helpless. This is a sector that is changing, or perhaps, more correctly, it is a sector that is being changed by the external pressures that it faces. For example, pressures on funding and increasing demands on services have intensified. These, often triggered by the recent financial crisis and subsequent programmes of austerity with respect to public spending, have created a ‘perfect storm’ for charities, whereby they try to do more with less. Such has necessitated, among other things, major changes in strategies for seeking and using precious funds; although the ethical stance of certain charities in this regard is not always viewed as of the highest standard.

Furthermore, the expansion of the charity sector has frequently been openly endorsed by government, sometimes based on policy objectives related to a perceived ‘appropriate’ balance of government and non-government activities. The financial constraints and crises of the last few years have encouraged government to engage more with the charity sector (not always in the most considered and controlled manner) in relation to services previously provided by government. Indeed, the withdrawal of certain public-sector services has often put pressure on charities to respond to increasing beneficiary needs, including the delivery of public services to tackle social exclusion.

3. Accountability, Transparency and Trust
Charities comprise a sector where the fact and perception of accountability, transparency and trust are important; very different from the private and public sectors in terms of its motivation, activities, resource availability and contribution to the public good. Moreover, it is a sector where public trust and confidence are crucial as a basis for ensuring its health and growth. The growth in the size and influence of the sector, combined with a number of highly publicised governance and fundraising scandals, has led to increased visibility and public scrutiny in the UK and RoI. Indeed, there have been calls for increased sector scrutiny for many years; with the need for charities to discharge accountability, operate transparently and act ethically being widely articulated.

Scandals, however isolated, have the potential to inflict considerable damage. For example, in the UK in 2015, there was the collapse of Kids Company amid allegations of financial mismanagement; and the much-publicised suicide of the 92-year-old poppy seller Olive Cooke (believed to have received almost 3,000 charity mailings in a single year). Similarly, in RoI, the Irish Hospice Foundation, for example, claimed that scandals in 2013 and 2014, involving the now reconstituted Central Remedial Clinic and Rehab, resulted in a 50% drop in donations to the hospice’s annual Christmas appeal.

A number of studies of charity activity have identified the UK and RoI as particularly generous nations and ones where charitable activity is pervasive. For example, the World Giving Index identifies the UK as the most generous country in Europe, followed by RoI. Consequently, since a considerable amount of charitable work is supported by the public in the UK and RoI (either directly through donations and/or through voluntary activities, or indirectly through taxes), it is critical that there are appropriate systems in place, not only to ensure that public money is not misappropriated, but also to sustain the health and longevity of the sector and the groups that charities seek to serve.

4. Importance of Good Accounting and Reporting
While scandals, such as those mentioned above, are isolated, their impact is massive since the sector’s strength comes from the value society places on the social capital it generates. A key argument is that good accounting and reporting underpins good accountability, good accountability supports the building of trust, and trust is essential to the continuing health of the sector (including access to funding). Conversely, poor accounting and reporting undermines accountability, undermined accountability damages trust, and damaged trust weakens the sector (making it more difficult to secure funding).
The conventional view of accounting is that it is a purposive activity, directed towards a specified end, which is meeting stakeholders’ information needs. Accountability can be regarded as being answerable for one’s conduct and responsibilities; a concept that becomes more pertinent when faced with a changing external environment (e.g. due to funding pressures and high-profile scandals). While accountability is wider than accounting (no matter how widely accounting is defined), good accounting and reporting is a key aspect of a good accountability system. In the context of charities, accountability is often assessed in terms of a charity’s response to its stakeholders’ information needs, part of which can be met through the provision of performance information in annual reports.

Accountability can be viewed in terms of a principal-agent relationship whereby a principal transfers to an agent, resources and expectations regarding the transfer. For charities, the principal could be a donor/funder (a key stakeholder in a charity setting) who transfers resources (without any direct economic benefit to themselves) to an agent (the charity). With such a transfer, come expectations (often not specifically detailed in contractual terms) on the part of the donor (principal) that: the resources will be used to further the charity’s objectives (typically expressed in terms of supporting beneficiary needs); and information will be provided as to what a charity has done or plans to do (possibly in terms of activities and spending). Accountability is discharged (or an account given) as such information is communicated (through a variety of mechanisms and channels) to the donor (principal) regarding this. On this basis, the principal (donor) holds the agent (to account) by responding to such information through action (e.g. continuing to provide funds or ceasing to provide funds) or communication (e.g. by congratulating or censoring the charity).

Following recent scandals, of various hues and in different jurisdictional settings, some charity regulators have recognised the potential damage this can have and responded by adjusting regulatory and control processes. Such changes reflect shifting expectations regarding accountability, transparency and trust (albeit accepting that these terms are capable of different interpretations) and a trend towards strategic regulation. Whether such is required, or whether it reflects moves towards a ‘big-brother-type’ audit society, is debatable. However, it does suggest, at a minimum, a move towards greater engagement with a variety of stakeholders (e.g. beneficiaries, donors, regulators and the public).

5. The Charities Statement of Recommended Practice

Despite the importance of good accounting and reporting to the charity sector, the framework in the UK and RoI in the 1970s and 1980s was extremely weak: only England and Wales had a charity regulator, charity law was diverse and there was little focus on accounting and reporting. While charities were obliged to keep proper books of account and prepare financial statements, frequently such statements did not have to show a ‘true and fair view’ and were not required to be audited. In practice, the application of accounting standards was commonly ignored (even when charities were incorporated as limited companies) by both preparers and auditors of financial statements. Overall, there was little pressure to improve charity reporting from legislation, accounting standards or an effective regulatory body, with wider reporting (such as that relating to governance and performance) rarely being on the agenda.

This changed considerably in the UK in the 1980s. Research by Bird and Morgan-Jones revealed a sector where non-compliance with accounting standards and archaic accounting treatments were prevalent, frequently with the effect of understating surpluses and assets, or overstating losses and liabilities. This research is widely regarded as a ‘wake-up call’ for the sector and, since then, considerable efforts have been made to improve the quality and consistency of charity accounting and reporting. A vital aspect of this has been the development (in 1988), and periodic ‘refreshing’ (in 1995, 2000, 2005 and 2014), of a charities Statement of Recommended Practice (SORP); one that, over time, has become mandatory for most large UK charities (including those in NI) and best practice for RoI charities. During this process of evolution, the charities SORP has developed virtually beyond recognition:

- becoming an ‘accounting and reporting’ SORP rather than purely an ‘accounting’ SORP;
- becoming mandatory for large UK charities and best practice for RoI charities;
- so that charity accounts are very different from commercial accounts;
- with increasing emphasis on the importance of reporting ‘performance’; and
- significantly reducing the discretion of the preparing accountant.

When considering accountability, two key questions emerge: (i) to whom is a charity accountable?; and (ii) what form should that account take? Arguably, donors (or funders) are a primary upward stakeholder group to whom an
account is owed (they provide funding to a charity, often receiving no direct economic benefit in return); without their support charitable activity will cease. In terms of the form of the account, while financial accountability (through audited financial statements) is important (e.g. to indicate: that the money raised has been used appropriately; that the charity has ‘lived within its means’; and the level of resources available for future service provision), it is unlikely to be adequate by itself. More recently, the debate has focused on the importance of charities reporting their performance or impact\textsuperscript{5}. Indeed, the importance of this has been recognised in the latest SORP which explicitly encourages charities to report impact in the Trustees’ Annual Report (TAR).

As charities do not have a profit objective, their performance can be viewed in terms of a production model which includes inputs, processes, outputs and results/outcomes/impact. While these terms do not have standardised definitions, the following may aid understanding. Inputs are the resources used in providing a service (e.g. expenditure incurred or number of staff) and processes represent the activities undertaken (e.g. number of visits made or number of projects funded), with outputs being the actual goods or services produced (e.g. number of children fed or number of projects completed). Finally, results (or outcome/impact) are concerned with the effect of an organisation’s activities on beneficiaries (e.g. change in the level of education or overall level of satisfaction with the services provided). Given this ‘production’ process, two key criteria for judging performance are efficiency (the ratio of output to input) and effectiveness (the relationship between an organisation’s output and its objectives). An example of an efficiency measure for a charity is the cost (input) per child fed (output), or the number of cases handled (output) per employee (input). A measure of effectiveness is the number of children fed versus the planned, or the increase in adult literacy in a particular area versus the planned as a result of a particular intervention.

While the need to develop performance measures is well founded, there are considerable difficulties in designing systems to capture such information. For example, mission and objectives are often so loose that they inhibit useful measures being developed. In addition, defining objectives in terms of activities, rather than quality or impact, can be problematic since more activity (and expense) does not necessarily mean greater impact. Furthermore, aligning high- and low-level performance measures is challenging due to multiple (frequently competing) organisational goals, multiple stakeholder influences, unclear input-output relationships and benefits arising over time. Moreover, whilst accepting that setting objectives is critical to performance measurement, unless care is taken, the process can degenerate into a formal ceremony that does little to improve efficiency and effectiveness.

6. Our Research

Drawing on recently published research\textsuperscript{6}, this presentation explores the importance of charity regulation and accountability mechanisms in building trust. While all forms of data reaching the public domain can be considered part of the accountability discharge function, and whilst acknowledging the importance of traditional financial statements, our research focuses on performance reporting by large charities in the UK and RoI.

Classifying charities in terms of what they (primarily) do and who they (primarily) help, the following five categories of activities were developed: (i) Medical/Health/Sickness; (ii) Medical Research; (iii) Overseas Aid/Famine Relief; (iv) Animal Welfare; and (v) Wider Social Objects (Children/Poverty/Social Welfare). Then, to identify the performance information made available publicly to charity stakeholders, 25 large UK and 25 large RoI charities (based upon total income) were selected from the above categories and their most recent annual reports and annual reviews (if one was published) were obtained from their website. Of the 50 charities selected, each published an annual report and 20 (UK – 16; RoI – 4) prepared a separate annual review.

Based upon the sector-wide debate presented above, it is argued that charities should explain their (a) objectives and review the (b) activities undertaken in pursuit of those objectives. Furthermore, as argued previously, performance may be measured in terms of a production model, with this information including an analysis of organisational (c) inputs, (d) outputs, (e) impact, (f) efficiency and (g) effectiveness. Complementary (h) future target information and (i) lessons learned are potentially useful to stakeholders in assessing both direction of travel in terms of performance reporting and the challenges faced. On this basis, a checklist was developed to capture disclosures under these nine headings. The extent of the disclosure (or non-disclosure) of these nine key performance information types was viewed as indicative of the extent to which performance accountability was discharged (or not discharged) by a charity.
7. Our Findings

Performance accountability disclosures address the impact of an organisation on society. By considering performance disclosures in more formal TARs and, less formal, annual reviews, our research reflects on the current state of charity performance reporting in the UK and RoI. Before discussing performance information disclosure, it is worth noting that this research found evidence of very limited use of annual reviews as a communication channel by RoI charities. Only 16% (four) of the RoI charities surveyed published such a document, compared with 64% (16) of the UK charities. Annual reviews, compared with annual reports: (i) are normally shorter publications that include some annual report information in a condensed form; (ii) are written in less formal language; and (iii) often include a higher proportion of stories, photographs and diagrams. Indeed, annual reviews have been found to be more engaged with by stakeholders than TARs. Thus, given their lack of utilisation in the RoI, this suggests a weaker accountability architecture.

Overall, the average percentage of UK and RoI charities providing performance-accountability disclosures in both their TARs and annual reviews was low. The overall average disclosure rate of the nine information types used in this analysis was merely 50%. Moreover, with respect to the seven information items which focus more on the ‘calculation’ of performance (items (c)-(i)), the percentage of charities disclosing this information was even lower (TARs – 36%; annual reviews – 35%). Given the importance of performance-accountability disclosures, and even allowing for difficulties in measuring and reporting performance, the results suggest weak performance accountability. For example, a significant proportion of charities reported no information on effectiveness and efficiency, two crucial criteria for judging performance. Such shortcomings can undermine trust and confidence in the sector, and damage reputation, which, ultimately, could impact on funding flows.

Comparing the disclosure of performance-accountability information in UK and RoI TARs, a higher percentage of UK charities disclosed eight of the nine items. Only item (b) (activities carried out) had higher disclosure for RoI charities; although disclosure of this was extensive for all charities. Moreover, a higher percentage of UK charities provided each of the performance information items (c)-(i) compared with RoI charities.

In relation to performance-accountability disclosures in UK and RoI annual reviews, the results were closer, with UK charities having higher average disclosure rates for five of the nine items. However, given the limited use of annual reviews in the RoI (only four of the 25 RoI charities produced such a document), caution is needed when drawing conclusions; although the results do indicate greater use of performance reporting in the UK.

Taken as a whole, these results make a persuasive case (related to concepts of accountability, legitimacy and trust) for greater endeavour by individual charities and sector-wide bodies in the development and use of more substantial charity performance measurement and reporting systems as a basis for meeting stakeholders’ information needs.

8. Relevance for Northern Ireland Policy and Practice

In conclusion, a key theme of this presentation is that good performance accountability helps build trust and legitimacy, both of which are essential to the continuing health of the sector. Conversely, poor performance accountability may damage trust and legitimacy and thus weaken the sector. The research findings may reflect a greater presence and push for performance reporting in the UK (e.g. from the Charity Commission in England and Wales, Inspiring Impact, New Philanthropy Capital and the National Council for Voluntary Organisations) leading to greater engagement by UK charities in such discussions. However, due to a less-regulated RoI sector (at least until recently), such pressures may not have been present there to the same extent. Thus, from an accountability and transparency perspective, the results intimate that having a mandatory reporting system (and an active regulator) increases the likelihood of disclosure and the likelihood of greater performance accountability.

Therefore, with respect to NI, this suggests that CCNI (which is a nascent regulator) has a critical role to play in encouraging/requiring better performance accountability (and better performance focus) by NI charities; indeed, it is argued that such is vital to the continued health and growth of the NI charity sector, as well as to its effectiveness. However, given the very obvious financial constraints facing the NI public sector (and the wider UK public sector as a whole), and the current impasse regarding the establishment of a functioning Executive, a major risk is that
adequate resourcing (financially and legislatively) to enable CCNI to steer the sector in such a direction may not be made available.

Finally, to encourage the development and use of performance information, it would seem appropriate that charity-specific guidance should be developed (or the development should be supported/encouraged) by those concerned with the administration and control of the sector (e.g. CCNI or sector support groups such as the Northern Ireland Council for Voluntary Action). Indeed, given charities’ expertise, focus and limited resource base, to expect individual charities to develop meaningful and extensive performance reporting systems without guidance (including regulatory guidance) is perhaps too optimistic.


xii SORPs are recommendations on accounting practice for specialised industries or sectors which supplement other legal and regulatory requirements. Large UK charities must comply with the extant charity SORP, with compliance in RoI being considered best practice. At this time (December 2017), the extant charity SORP is the ‘FRS 102 Charities SORP’ published by the Charity Commission and OSCR in 2014.
