

Written evidence submitted by Nick Burton

Written Evidence to DCMS Select Committee on Charities Commission

Critical exempt charities should be regulated by the Charities Commission

Summary

- The government has failed to appoint a principal regulator for Charitable Mutual Societies, as exempt charities, and the FCA's performance as their registrar is very unsatisfactory.
- The DCMS Select Committee should examine the transfer of Charitable Mutual Societies to the normal regulatory regime of the Charity Commission as registered charities to resolve both issues.
- It is understood that it is not within the DCMS Select Committee to do more than propose the change and that it will require at least secondary legislation to implement it.
- The Committee should ask the Charity Commission to consider accepting a less than 0.64% increase in their workload to regulate an additional approximately 1000 charities, given the following serious issues:
- The FCA is allowing Charitable Mutual Societies an exemption from a full audit that Exempt charities are not permitted under the Charities Act Section 160.
- Neither of the recent Oxfam or the President's Club scandals would have come to light under the current FCA regime as it has no powers to investigate or appoint inspectors without a request from members. They had also both passed the single annual check the FCA conducts as they had submitted their accounts on time.
- The FCA cannot monitor or enforce the distinct charitable provisions of the Co-operative and Community Benefit Society Act 2014 as it has failed to separately identify Charitable Mutual Societies within its registrar.
- The culture of the FCA is to believe and behave as if mutual societies are fully regulated banks with approved individuals working for them, and therefore deserve to be protected from disclosure of their casework. In practice this enables societies to hide malpractice and bullying with the FCA's explicit complicity.
- The FCA states that they are following a risk based approach to Charitable Mutual Societies when they cannot produce a list of the most important risks, or what the trends in risks are. Nor are they taking any steps to mitigate risks.

Background

1. I was a trustee and volunteer at a Charitable Mutual Society who was so appalled at the refusal of support by the FCA that I conducted a broader investigation into how it fulfils its obligations under the Co-operative and Community Benefit Society Act 2014. The statements below are taken from FCA responses to either me or to an FOI request or a letter from the Charities Commission. It is of note that the FCA was unable or unwilling to provide a single piece of information in response to FOI requests.
2. Charitable Mutual Societies are Exempt Charities under the 2011 Charities Act. It is of note that the total value of exempt charities is greater than that of registered charities. The government has failed to appoint a principal regulator for them, as intended in 2009 review of charities. The FCA was confirmed as their registrar, but not their regulator, under the Co-operative and Community Benefits Societies Act 2014. However the actual practice of this

role has led to several omissions in the oversight of charitable mutual societies and a higher and unquantified risk of undiscovered failure.

3. My investigations have revealed a number of serious issues in even the limited role of the FCA as registrar, as well as the increased risks due to the continuing lack of the regulator.
4. It is understood that it is not within the DCMS Select Committee to do more than propose the appointment of a principal regulator and that it will require at least secondary legislation to implement it. The Treasury Select Committee is considering these matters as part of either their next six-monthly review meeting of the FCA or the examination of the new FCA CEO, but they obviously have many other matters to consider. I have also written to the Charities Minister, Baroness Barran, but have not yet had a response. Your imminent interview with the CEO and Chairman of the Charities Commission offer a timely opportunity to gain their perspective on the possibility of meeting the government's long delayed obligation to appoint a principal regulator for Charitable Mutual Societies, as well as mitigating the poor performance of the FCA as registrar.
5. The biggest issue is probably the attitude and culture of the FCA. The recent comment by the Treasury Select Committee Chairman, following their session with Andrew Bailey sums it up "The Treasury Committee ... has also raised a number of serious concerns regarding the performance of the FCA ... Many of these concerns – specifically around culture, transparency and insufficient speed of action – will remain a key focus for the committee."
6. Neither of the recent Oxfam or the President's Club scandals could have been resolved under the current FCA regime as it has no powers to investigate of itself or appoint inspectors without a request from members. This is laid down in the Sections 105 to 108 of the 2014 Act. The various provisions require either 10 or 10% of members to request the FCA to act and the members are required to state they would be prepared to bear the cost of the inspectors. Why would members underwrite the cost of a potentially hostile investigation prompted by a whistle blower or media coverage? The FCA has also been reluctant to use what powers it has by refusing a related request to order a special meeting (equivalent to an EGM) on the grounds that a dispute is in progress. Their previous CEO stated in an annual public meeting response that very few meetings had been ordered in the last 150 years, seemingly unaware of how much corporate governance standards have changed in the last 15 years let alone 150! The two charities concerned would also have both passed the single annual check the FCA conducts as they had submitted their accounts on time.
7. I am particularly concerned about the FCA's enthusiasm to apply rules and processes based on being a regulator when it is not the regulator, but rather the registrar, for charitable mutual societies. So it uses the former function to cover up its inaction on the latter role. It cannot even recognise the requirement to treat charitable mutual societies differently as it maintains no list of them and does not record their charitable status in the Mutual Society Register. This is yet another example of a poorly function inadequate public register that has been the subject of the FCA Complaints Commissioner's regular adverse comment for several years. Thus it views an approach from a society member as a complaint about a bank. The FCA can reasonably say that it does not need to share the bank's response with the complainant because it has a massive tool kit to monitor and licence the bank and the individuals within it and knows, or ought to know, the background and quality of the bank's response. It also monitors and insists on the publication of complaints that the bank receives.
8. For a charitable mutual society it has virtually no background information. Its sole information would appear to be literally an annual box ticking exercise, however

there appears to be only one box – has the society submitted its annual accounts? Not whether the accounts are correct, been audited or examined or meet the 2014 Act, just submitted. But it still hides behind the “regulator’s cover” to disguise its unwillingness to check information given to it by the management of a charitable mutual society and subsequent lack of action. Almost every communication that I have received from the FCA has referred to its role as a regulator when it meant registrar indicating that this problem is widespread throughout the organisation.

9. I have also received a letter from the Head of Accountancy Services, Investigation Monitoring and Enforcement Directorate at the Charity Commission confirming that there is no statutory basis for the more limited independent examination, rather than formal audit, of exempt charities. This is based on the explicit provision in Section 160 of the Charities Act that: *Nothing in sections 144 to 155 (audit or examination of accounts) applies to an exempt charity.* Within these sections Section 145 includes the option for independent examination for smaller charities. This serious misapplication of the law could have affected hundreds of charities over several years.
10. Another serious concern is the failure of the FCA to maintain a register of Charitable Mutual Societies, or annotate their status on its mutual societies’ register so that neither they nor anyone else can monitor the different oversight regime required under Section 12 and clause 84 of the 2014 Act.
11. The FCA has also stated that it is following a risk based approach when the evidence is that it is not monitoring serious risks, taking any steps to mitigate them or monitoring any of their trends. Their response to an FOI request stated “we do not hold any recorded information setting out the major (or top 5) risks or current trends identified for charitable mutual societies.” Even more significantly if there is no information held on the top 5 risks or their trends what is the value of a risk model or does it even in practice exist or is used in any consequential way? Their stated policy in the FCA Handbook is:

EG 19.2.301/03/2016RP

“The [FCA's](#) enforcement activities in respect of registrant-only societies focus on prosecuting societies that fail to submit annual returns. As registrant-only societies are not subject to the [rules](#) imposed by the [Act](#) and by the [FCA Handbook](#), the requirement that they submit annual returns provides an important check that the interests and investments of members, potential members, creditors and other interested parties are being safeguarded. The power to prosecute registrant-only societies who fail to meet this requirement is therefore an important tool and one which the [FCA](#) is committed to using in appropriate cases.”

12. The evidence in the previous sections strongly suggests that it is not monitoring even the more obvious risks. For example the recent Charity Commission sample showed that nearly half of the submitted accounts were unsatisfactory and many led to the auditors being reported to their professional body. Or is “a risk-based approach” simply fashionable words used to mislead the public, legislators and those monitoring the FCA’s performance that there is some rationality in the process followed?
13. Risk Management is what it says it is - much more than simply collecting and analysing the risks. But that is a critical first part of the process. There is no evidence that any monitoring of risks, other than non-submission of the annual return is taking place.
14. If there is a consensus that the FCA should be acting as the principal regulator for charitable mutual societies it is probably already required to do so as it is required to enforce all legislation applicable to mutual societies under The Financial Services Act 2012 (Mutual Societies) Order 2013 Schedule 1 para 5(1)(a). This would include the Charities Act 2011 which includes items specific to Exempt Charities as described in the Charities Commission

CC23 guidance. However my experience so far is that the FCA will no doubt claim that it will need court action to force it, as a public body, to follow legislation. It follows that if it is unwilling to follow this legislation it is even more important to identify a principal regulator who does want to do the job.

15. Another issue is the abrogation of responsibility to deal with disputes by claiming that the courts will deal with them. Its predecessor as the Chief Registrar of Friendly Societies did have this responsibility. In practice this policy appears to have been a total failure as no court cases have occurred since the practice was changed.
16. Finally there is the total lack of support for whistle-blowers and deliberate attempts to suppress their concerns. Again the compares poorly with the Charities Commission's recent initiatives in this area recognising the complete absence of legal protection for volunteer whistle-blowers.
17. I can of course provide further detail as necessary. These are serious concerns for you to look into as I believe there is great potential for harm to be occurring to many trustees and volunteers within charitable mutual societies. Given that resolution is only possible via a £5000 plus legal bill I am sure many have walked away.
18. I believe it would add value to the delivery of public benefit by charitable organisations if you were to raise the possibility of appointing the Charities Commission as the principal regulator for Charitable Mutual Societies with the CEO and Chairman when you meet them.

March 2020