

COMPLIANCE

# Inquiry Report

## Crescent Relief (London)

Registered Charity Number 1087724



# A statement of the results of an Inquiry into Crescent Relief (London) (registered charity number 1087724).

Published on 29 September 2011.

## The Charity

1. Crescent Relief (London) ('the Charity') was registered as a charity on 27 July 2001. It is governed by a memorandum and articles of association incorporated on 5 October 2000, and amended by special resolutions dated 13 June 2001 and 7 July 2001.
2. Its objects are '*the relief of persons suffering from financial hardship, sickness, or distress or who are otherwise in need, in particular refugees and displaced persons from Azad Kashmir and Pakistan and those persons who have fallen victims to natural and manmade disasters, and the advancement of education of such persons.*'
3. The Charity's main activities included emergency relief and reconstruction work in Pakistan following the 2005 earthquake and the construction of, and ongoing support to, an orphanage in Indonesia following the 2004 Tsunami.
4. The Charity's income and expenditure<sup>1</sup> for the last six years was:

Financial Year End	Income (£)	Expenditure (£)
31 October 2005	353,457	201,657
31 October 2006	236,711	195,914
31 October 2007	16,184	6,960
31 October 2008	12,997	6,284
31 October 2009	5,969	779
31 October 2010	4,976	4,328

5. The Charity raises funds by issuing mail shot appeals during Ramadan, and also from time to time following disasters when it hopes to undertake emergency response work. A number of donors chose to support the Charity on a more regular basis by setting up monthly standing orders.
6. Following the opening of the Commission's Inquiry in August 2006 (see below paragraph 8), the trustees decided to end all proactive fundraising whilst the investigation was ongoing. This had a significant impact on the Charity's income.

<sup>1</sup> These figures are taken from the Charity's accounts which were submitted to the Commission and do not reflect all of the Charity's expenditure in Pakistan (see paragraph 51).

## Source of concern

7. The Commission became aware of allegations linking the Charity with a conspiracy to commit terrorist offences on aeroplanes departing from the UK. The allegations were reported in both the UK and international media<sup>2</sup>. The criminal investigation conducted by the Police, Operation Overt, examined this issue and looked at the Charity as part of its wider investigation.

## Commission Inquiry

8. Due to the serious nature of the concerns raised about the Charity and individuals connected with it, and the Commission's responsibility to safeguard charitable funds, and public confidence in charity, on 22 August 2006 the Commission opened a statutory inquiry under section 8 of the Charities Act 1993 ('the Act').
9. It is the responsibility of law enforcement agencies, not the Commission, to investigate alleged criminal offences. Where a charity and/or its trustees are implicated in such cases, the Commission's role is to assess whether the issues being investigated and evidence arising in those separate criminal investigations may indicate misconduct or mismanagement in the administration of the charity and/or it raises concerns about the individuals' involvement with a charity, as trustee or otherwise. Where there is a regulatory interest for the Commission, it assesses whether it needs to act, using its own powers and jurisdiction, to ensure that trustees meet their legal obligations and duties and to protect charity property.

## Issues

10. The Inquiry examined the following issues:

**Issue 1: Whether funds of the Charity, or funds raised on its behalf, had been used unlawfully**

**Issue 2: Financial management of the Charity and the supervision of overseas activities**

**Issue 3: Governance of the Charity**

<sup>2</sup> For an example of the media reporting see [http://news.sky.com/skynews/Home/British-Request-Over-Terror-Suspect/Article/20060841232277?DCMP=News-search-sslc&lid=ARTICLE\\_1232277\\_British%20Request%20Over%20Terror%20Suspect&lpos=Home](http://news.sky.com/skynews/Home/British-Request-Over-Terror-Suspect/Article/20060841232277?DCMP=News-search-sslc&lid=ARTICLE_1232277_British%20Request%20Over%20Terror%20Suspect&lpos=Home)

## Timescale of Inquiry

11. The Inquiry was opened on 22 August 2006 and the Commission's substantive investigations concluded on 16 June 2011. The Inquiry closed on 29 September 2011 with the publication of this report.
12. The Inquiry was prolonged so as to:
  - avoid prejudicing the criminal investigation, Operation Overt, which had connections to the Charity, and this taking precedence over the Commission's civil investigation<sup>3</sup>. By 6 May 2008 the Police had concluded their enquires;
  - the trustees' inability to access all of the Charity's records as a result of the seizure of those records by the Police; and
  - the time taken to obtain evidence from Indonesia and Pakistan.

## Findings

13. The Inquiry found that all of the Charity's activities were conducted overseas, the vast majority in either Kashmir or Indonesia<sup>4</sup>. It is vital that charities which operate there, and in other high risk areas, have adequate safeguards in place to manage the risks of undertaking humanitarian work in such regions.
14. In reaching its findings the Inquiry did however also note the importance of the efficient provision of humanitarian aid to hard-to-reach communities in times of crisis. The Inquiry took into account in its investigation:
  - the Charity's particular size and income level;
  - that the Charity often needed to act quickly to respond to a disaster situation;
  - the practical challenges<sup>5</sup> the Charity faced as a result of working internationally, and in particularly remote and volatile regions;and tailored its investigation and advice accordingly.

### **Issue 1: Whether funds of the Charity, or funds raised on its behalf, had been used unlawfully**

15. As a result of the criminal case, Operation Overt<sup>6</sup>, no individuals connected to the Charity were convicted of terrorist offences.
16. From the information examined by the Inquiry the Commission found no evidence that the trustees had diverted charitable funds for unlawful or non-charitable purposes. However, the Commission found that the trustees were unable to verify satisfactorily the end use of funds in both Indonesia and Pakistan (see further *Issue 2* and *Issue 3*).

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<sup>3</sup> No criminal charges were brought against any of the Charity's trustees as a result of the criminal investigation.

<sup>4</sup> The Foreign and Commonwealth Office, in its published travel advice by country, states that there is currently a high threat from terrorism throughout both Indonesia and Pakistan - <http://www.fco.gov.uk/en/travel-and-living-abroad/travel-advice-by-country/>

<sup>5</sup> For example language, literacy and the absence of banking facilities.

<sup>6</sup> <http://www.bbc.co.uk/news/10455915>

17. The Inquiry found that such shortfalls in properly controlling, monitoring and documenting the use of charitable funds (in this case by third parties overseas) prevented the Charity's trustees from being able to demonstrate that those funds had been used legitimately and properly and in furtherance of the Charity's purposes. This had also risked the Charity's funds being misappropriated without the trustees' knowledge.

## **Issue 2: Financial management of the Charity and the supervision of overseas activities**

### **Due diligence and monitoring:**

18. To meet their legal duty to protect charity assets with the necessary care, and properly to assess risk, trustees must carry out appropriate due diligence on those individuals and organisations that the charity receives donations from, gives money to, or closely works with, following this up by monitoring and evaluating work.

19. The Inquiry appreciated that collaborative working can be an effective way to maximise the impact of charitable work, especially in an emergency response situation, including, where properly managed, work with non-charitable organisations. Working in collaboration does not, however, relieve trustees of their legal duties and responsibilities towards their charity. Trustees have ultimate responsibility for running a charity, its finances and property. They must always act to protect property owned by their charity and ensure its finances are used appropriately, prudently and in accordance with its charitable purposes.

20. Where charities give money to partners and beneficiaries, especially large amounts of money or in high risk situations, making sure that adequate monitoring takes place is crucial. This means verifying that charity funds or property reach their proper destinations and are used as the charity intended.

21. Partners who are funded to implement a project or deliver aid are in a position to abuse these funds unless:

- the charity is sure they are bona fide organisations;
- the charity has evidence that the partner can implement the programme in the way expected; and
- the partner's internal management and financial control systems enable them to identify and report losses or abuses back to the charity.

22. Overseas partners may be subject to control or have affiliations with proscribed organisations, or designated entities, or have weak internal controls which mean that their funds are potentially open to fraudulent claims or theft by others. In light of these types of threat it is vital that trustees take a risk based approach to their relations with their partners.

23. The Inquiry examined the Charity's due diligence and monitoring procedures for its projects in Pakistan and Indonesia. The Inquiry found that the Charity's practices in this regard had not been adequate. The Inquiry did not find that trustees had informed themselves sufficiently to be able to satisfy themselves that they were making the best decisions for the Charity.

## **Pakistan**

24. The Inquiry acknowledges that the trustees had sought to monitor the work undertaken in Pakistan, by making regular visits to the projects there. However, the Inquiry did not consider that the monitoring visits in these circumstances were in themselves enough to ensure that the trustees were fully discharging their duties.
25. When the Inquiry met with the trustees on 20 October 2008 they produced numerous photographs to evidence the monitoring work undertaken by the trustees and the reconstruction work carried out by the Charity in Pakistan.
26. Despite the Police retaining custody of the documents seized from the Charity's premises, the trustees were able to provide the Inquiry with substantial information regarding expenditure in Pakistan. However, the documents did not provide a complete audit trail. Some receipts were missing and a large number of the documents were self-issued receipts, which did not provide objective corroboration of the documented transactions.
27. The financial analysis conducted by the Inquiry established that the self-issued receipts were printed specifically for the use of Crescent Relief in a format that required two signatures per transaction. The Inquiry found that self-issued receipts were often signed by only one person<sup>7</sup>. As a result the financial controls that had been designed to safeguard the Charity's assets were not always implemented. Further, the trustees had not identified that financial controls were not being followed, and as a result were unable to take steps to remedy this. The Inquiry considered this to be evidence of mismanagement in the administration of the Charity.

## **Indonesia**

28. The Inquiry was informed that, following the tsunami in December 2004, the Charity purchased land in Indonesia and financed the building of an orphanage, which they continued to fund once it was operational. All funds had been transferred by the Charity to one individual based in Indonesia<sup>8</sup>. The trustees indicated to the Inquiry that they were content with this individual's performance as a partner to the Charity, and that they would use him again to undertake charitable work on their behalf.
29. The Inquiry was unable to satisfy itself that the trustees could properly verify the end use of the Charity's funds in Indonesia. Financial analysis conducted by the Inquiry found that between May 2005 and May 2006 £83,000 of charitable funds were transferred directly into the bank account of this local partner in Indonesia.
30. The trustees initially informed the Inquiry that they had an agreement with the local partner that he would retain all receipts for the charitable funds that they spent. As the Charity's documents were being held by the Police, the Inquiry on 13 November 2008 asked the trustees to obtain from their local representatives in Indonesia or partners with whom the Charity had worked, any relevant documentation or Charity records in their possession. The trustees then informed the Inquiry that the local partner did not hold any such records.
31. However on 29 April 2009 the Inquiry did receive a submission of documents relating to the Charity's activities in Indonesia. At a meeting on 7 June 2010 the trustee with delegated responsibility for the Charity's activities in Indonesia confirmed that the Charity had received the information in February or March 2009 via post from the local partner.

<sup>7</sup> The Inquiry noted that the receipts were printed in English and not the local language, Urdu.

<sup>8</sup> Prior to selecting this individual, who had experience of working in an Indonesian charitable organisation, the trustees spoke to local elders to satisfy themselves that he was a suitable person to undertake work on behalf of the Charity.

32. No explanation was provided by the trustees as to why they had previously incorrectly informed the Inquiry that the local partner no longer held any documents. The Inquiry was also concerned to note that, from its appearance, some of the supporting documentation may have been tampered with. These factors raised concerns for the Inquiry that the Charity's funds were at risk. It was hard to see how, without contemporaneous access to (and conscientious scrutiny of) documentation evidencing the Charity's expenditure overseas, the trustees could satisfy themselves that the Charity's funds had been properly spent in Indonesia.
33. Despite their reliance on the local partner to act on the Charity's behalf, and their transfer to him of significant sums of Charity money for this purpose, the trustees did not provide the Inquiry with any documentation to evidence the existence a partnership agreement between the Charity and the local partner to formalise the terms of the arrangement between them. Nor were the trustees able to satisfy the Commission that adequate due diligence checks had been undertaken before the partner had been selected.
34. Charity trustees are all equally responsible for the management of their charity. It is acceptable for trustees to delegate aspects of the day to day management of their charity to one trustee, staff or others. However, charity trustees must always retain the ultimate responsibility for running the charity.
35. When delegating tasks it is vital that adequate safeguards are in place. Trustees are under a duty to manage and supervise the activities carried out in the charity's name and should ensure they monitor and oversee the way in which their delegated powers are exercised.
36. The charity's governance arrangements must be able to cope with the nature of its activities and the high risk area in which it operates.
37. The trustees' displayed a lack of collective knowledge regarding charitable work undertaken in Indonesia. During a meeting with the Inquiry, which the trustee with delegated responsibility for the Charity's activities in Indonesia was unable to attend, the remaining four trustees could not answer any questions relating to the Charity's activities in Indonesia. They were also unable to identify the orphanage built and funded by the Charity from a selection of photographs. This raised concerns that the trustees had not been fully involved in monitoring the Charity's activities, and had not been receiving adequate feedback from the trustee with delegated responsibility to enable their informed participation in decision-making relating to this area of the Charity's work.
38. Subsequently the Inquiry did meet with the trustee with delegated responsibility to discuss the Charity's activities in Indonesia. Having taken on this role, and given the other trustees' lack of knowledge on this subject, the Inquiry expected this trustee to have a clear understanding of how the Charity-funded orphanage was run and to have documents to support the Charity's expenditure in Indonesia.
39. This however was found by the Inquiry not to be the case. The Inquiry was informed that the Charity's local partner in Indonesia spoke good English. The documentation that was supplied by the trustees to evidence the expenditure, which they had received from their local partner, was in Indonesian. However, the Inquiry established that nobody on the trustee body was familiar with this language. Although the trustees informed the Inquiry that they had translation support, they did not appear to have used this in relation to the documents that they produced to the Inquiry, and so were unable to understand or explain their contents. It was therefore hard for the Inquiry to see how the trustees could be satisfied that these documents evidenced monitoring by the trustees of Indonesian activities and expenditure.

40. The documents supplied to the Inquiry in support of the Charity's activities in Indonesia consisted of electricity and telephone bills with varying addresses. During the meeting the address for the Charity's local partner was identified, but the trustee was not able to explain how the other address on the invoices, which had been paid by the Charity, related to the Charity's activities in Indonesia.
41. The trustees are ultimately responsible for the charitable activity undertaken by the local partner on the Charity's behalf. It is acknowledged that trustee with delegated responsibility visited the country on three occasions from 2005 to 2006<sup>9</sup>. However, the Inquiry did not consider that visits of that nature had been sufficient for the trustees to discharge their duties. Despite continuing regularly to send the Charity's funds to its partner agency in Indonesia, the Inquiry found that very little effective ongoing monitoring had been conducted, particularly given the trustees could not understand the local language, had no written and enforceable agreement in place with the local partner, and had agreed that the local partner would retain all of the receipts. The Inquiry also found that the trustees were largely dependent on the verbal feedback of the local partner, the very individual who was in receipt of the Charity's funds.

### **Internal financial controls**

42. All charities must have, as a minimum:
  - some form of appropriate internal financial controls in place to ensure that all funds are fully accounted for and are spent in a manner that is consistent with the purpose of the charity. What controls and measures and what is appropriate will depend on the risks and the charity;
  - proper and adequate financial records for both the receipt and use of all funds together with audit trails of decisions made. Records of both domestic and international transactions must be sufficiently detailed to verify that funds have been spent properly as intended and in a manner consistent with the purpose and objectives of the organisation;
  - given careful consideration to what due diligence, monitoring and verification of use of funds they need to carry out to meet their legal duties; and
  - take reasonable and appropriate steps to know who their beneficiaries are, at least in broad terms, carry out appropriate checks where the risks are high and have clear beneficiary criteria which are consistently applied.
43. The Charity works in remote regions where there are language, literacy and banking challenges. Identifying the risks arising from its activities, and managing those risks are important to assist the Charity achieve its strategic aims while avoiding or mitigating any risk posed to its funds. The Inquiry found that the trustees should have given consideration to these risks and managed them accordingly.
44. At a meeting on 20 October 2008 the trustees informed the Inquiry that, although good financial policies existed, none of these had been put in writing. The Inquiry did not consider this to be satisfactory for the Charity, given its income, overseas activities, and delegation by the trustees to employees and third parties to administer the Charity's funds.

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<sup>9</sup> This individual visited Indonesia on two occasions as an agent of the Charity prior to his appointment as a trustee. He was not a trustee at the time when the first two of his three visits were conducted.

45. Even without any formal policy documents, the trustees had a duty to comply with the terms of the Charity's bank mandate and governing document. Article 49 of the Charity's governing document states:

*'Any bank account in which any part of the assets of the charity is deposited shall be operated by the trustees and shall indicate the name of the Charity. All cheques and orders for the payment of money from such account shall be signed by at least two trustees.'*

46. The Inquiry found that the Charity's bank accounts in Pakistan, contrary to this provision in the governing document, were not opened in the name of the Charity, but in the name of '*Charities Union UK Crescent Relief*'; and nor were the bank accounts operated solely by the trustees, as the Charity's co-ordinator in Pakistan (who was not a trustee of the Charity) was named on the bank mandate.

47. In addition, the Inquiry found that to facilitate charitable work between February 2003 and October 2005, prior to opening the bank accounts in Pakistan, the trustees transferred £68,500 of the Charity's funds directly into the Charity's coordinator's personal bank account. This was in breach of the governing document, mixed charitable and non charitable funds, and exposed the Charity's assets to risk. In late 2005 the trustees opened the Charities Union UK Crescent Relief accounts in Pakistan. The Inquiry acknowledges that this action mitigated the risks to the assets, however, the trustees should never have allowed charity funds to be deposited in a bank account not in the name or control of the charity. The coordinator subsequently transferred £2,100 of the Charity's funds from his personal account to these new bank accounts.

48. The Inquiry also found evidence that cheques had been signed by only one person, contrary to the provisions of the Charity's governing document and its bank mandate. During the course of the investigation, the Inquiry was asked by the Charity's trustees to authorise a payment request involving a cheque that contained only one signature<sup>10</sup>. Failure to implement basic financial controls designed to protect the Charity's assets, placed the Charity's funds at risk.

### **Transparency and accountability**

49. In response to concerns that the Charity's assets may be at risk, on 23 August 2006 the Commission used its powers under section 18(1)(iv) of the Act to make two orders to protect charity property (sometimes referred to as '*freezing*' orders). They were put in place over the Charity's bank accounts in England and Wales to prevent payments being made from these accounts without the prior approval of the Commission. At the date of this action, the Inquiry was only aware of the accounts held with banks in the UK. This measure safeguarded charitable assets on a temporary basis whilst concerns were investigated. Legitimate and proper payments could be authorised by the Commission on receipt of appropriate paperwork.

50. The Inquiry's letter of 23 August 2006 informed the trustees that restrictions had been placed on the Charity's accounts held at two different banks in the UK. The letter stated:

*'If the charity has any other accounts that are not detailed in the Orders please contact me immediately with a full breakdown of the account number(s) and sort code(s)'.*

<sup>10</sup> When an explanation was sought, the Inquiry was informed that this was to expedite the payment process as the other signatory was unavailable and that the trustees intended to obtain a second signature before presenting the cheque to the bank. However, by presenting a cheque to the Commission which only contained one signature and without providing an explanation at that time as to why it had only been signed by one individual, the Inquiry was not satisfied that the trustees had followed proper procedures and could not be satisfied that the second signature would be obtained.

51. Having received this letter the trustees did not contact the Inquiry to inform it that the Charity had additional accounts. However, in September 2008 the Inquiry discovered through its investigations that the Charity had two additional bank accounts in Pakistan. Financial analysis conducted by the Inquiry found that the trustees had continued to transact and expend funds from these accounts without the knowledge of the Inquiry, and after the date of the 'freezing' orders.
52. During the Commission's meeting with the Charity on 20 October 2008 the trustees confirmed that they had spent all of the funds held in the accounts in Pakistan. The Inquiry found that this expenditure occurred during a period when the Charity had no formalised internal financial controls, risk management or due diligence policies in place, and when the trustees were aware of the Inquiry, and its interest in the Charity's use of its funds.
53. Had the Inquiry been aware of the existence of these accounts, steps would have been taken to ensure that the trustees could not access those funds without the prior approval of the Commission. By neglecting to tell the Inquiry about the accounts in Pakistan – despite the specific request for this information from the Inquiry – the trustees circumvented the investigation and the safeguards the Commission had put in place by restricting transactions on the Charity's bank accounts in England and Wales. This allowed the trustees to have unrestricted and unsupervised access to charitable funds during the Inquiry – something the actions taken by the Inquiry had expressly sought to prevent.
54. In addition, when the Inquiry met with the Charity's UK accountant in July 2009 he informed the Inquiry that he had no knowledge of the Charity's bank accounts in Pakistan, and as a result these had not been taken into consideration when the Charity's annual accounts had been produced. It was therefore likely that the Charity's annual accounts were not correct.
55. The Inquiry found that the lack of disclosure of these bank accounts by the trustees, despite the Commission's clear interest in and express request for such information, demonstrated a lack of openness and gave the regulator a misleading understanding of the Charity's assets, activities and the trustees' conduct. It was also contrary to their accounting duties and constituted a failure to be properly accountable to donors, beneficiaries and the public.
56. The Inquiry found that by not being open and transparent with the Commission or the Charity's accountant the trustees' were not fulfilling their duties and responsibilities as conscientious charity trustees, and may have exposed the Charity's assets to undue risk.

### **Issue 3: Governance of the Charity**

#### **Expenditure: due consideration**

57. Although by law, all charity trustees are jointly and equally responsible for the management and administration of their charity; the Inquiry found that the Charity's trustees were not exercising proper collaborative and careful decision-making, taking all relevant factors taken into consideration, before funds were expended; and were not able to demonstrate adequate management and control over the Charity's financial affairs generally. As a result the Charity's assets were placed at risk.

58. Evidence of this included:

- the trustees asking the Commission in October 2006 to authorise the payment of a service charge that the Charity was not liable to pay; and
- on 4 January 2010 the Inquiry received a request from the Charity to conduct a trip to Pakistan to establish the cost and work involved in completing a house-building project that had been started but suspended. The initial request did not demonstrate that due consideration had been given by the trustees to potential risks associated with the proposed trip, nor had adequate quotes for costs of the trip been obtained and reviewed. The Inquiry had to work further with the trustees before they were able to demonstrate they had undertaken proper decision-making processes to determine that the proposed expenditure was necessary and expedient in the interests of the Charity.

59. In accordance with the Inquiry's recommendations the trustees did attempt to introduce written policies for the Charity's governance. However, the Inquiry found that these were not adequate (see *New Policies* below). On 16 October 2010, the trustees had adopted a policy document entitled '*Rules of the Board of the Trustees*'. Clause 2.5 of that document states:

*'The Chairman may take whatever measures, following consultation with at least two other Trustees, constitute (in their reasonable opinion) a suitable response to any issue requiring urgent action. Such measures may similarly be taken by a Vice-Chairman or the treasurer, as appropriate. Such actions shall be reported to the Board as soon as reasonably practicable'<sup>11</sup>.*

60. The Commission appreciates that charities working in disaster response may need to act quickly, and may streamline decision-making processes accordingly. The Inquiry was, however, concerned that these new measures could result in significant Charity funds being expended at the instruction of just one trustee, and without full and proper discussion, consideration of alternative options, and agreement amongst the trustee body, obtaining expert advice where appropriate. Further, the trustees had informed the Inquiry that given the urgent nature of their disaster response work, they preferred '*to make emergency specific risk policies on an ad hoc basis*'<sup>12</sup> as opposed to having a risk policy already in place. The Inquiry found that this, in combination with the clause permitting decisions for major expenditure to be taken outside of a considered trustee meeting, was not a system with adequate safeguards, but potentially placed the Charity's assets at unnecessary and unacceptable risk.

### **Governing document and constitution of trustee body**

61. The Inquiry identified instances when the Charity had not been administered by the trustees in accordance with its governing document, and that there was a lack of transparency about the identities of the individual trustees of the Charity.

62. On 23 August 2006 the Commission issued letters to all individuals recorded as being trustees and/or directors of the Charity on the register of charities and/or with Companies House informing them that an Inquiry had been opened into the Charity<sup>13</sup>. Two of those contacted disputed their trusteeship.

<sup>11</sup> This clause appeared to contradict a clause contained in another contemporaneous policy document the *Governing Policies*, which states '*Approval of the Trustees must be obtained for charitable expenditure on any project*'.

<sup>12</sup> The *Governing Policies* document

<sup>13</sup> The Inquiry was also concerned to note differences between the records maintained by Companies House and those of the Commission, given this information had been supplied by the Charity to both Companies House and the Commission. It is an important principle of public accountability that the individuals running a charity are identified.

- 63. One individual contacted the Inquiry to query why we believed them to be a trustee of the Charity. The Inquiry informed the individual that they were listed as a director of the Charity with Companies House. The individual advised that this information was not accurate as the meeting during which they had been appointed had not been quorate, and therefore the appointment was not validly made<sup>14</sup>.
- 64. Another individual informed the Inquiry that they were not a trustee and had no connection to the Charity. Documents viewed by the Inquiry and which had been submitted to Companies House, appeared to be signed by the individual - making them a director, and therefore a trustee, of the Charity. The individual's son later confirmed his view that the signature on the form was that of his father, but the individual himself failed to provide any explicit confirmation of his trusteeship or connection with the Charity.
- 65. Given the confusion surrounding the identity of the trustees, the Inquiry found it difficult to see how, the trustee body were able to ensure that the Charity was being managed in accordance with its governing document, by individuals who were both aware of the responsibilities and duties that it would involve and who were ready and capable of meeting those.
- 66. The Inquiry also noted that section 49 of the Charity's Articles of Association states:  
*'Any bank account in which any part of the assets of the Charity is deposited shall be operated by the trustees and shall indicate the name of the Charity. All cheques and orders for the payment of money from such account shall be signed by at least two trustees.'*
- 67. A bank in Pakistan confirmed to the Inquiry the identity of the signatories on the two accounts held with it by the Charity – one in Pakistan Rupees and one in Pounds Sterling. The Chairman of the Trustee Board was named as a signatory for the Pakistan Rupees account but none of the trustees were named as a signatory for the Pound Sterling account. The Inquiry found that all payments that had been made from both accounts held with the bank in Pakistan had been made in contravention of the express terms of the Charity's governing document; and generally contrary to good practice for appropriate financial controls for charitable funds.

### **New policies**

- 68. On 3 November 2010, the Charity submitted to the Inquiry newly drafted policies and procedures for its governance and administration which had been adopted by the trustees on 16 October 2010. The Inquiry's assessment of these documents identified a number of concerns about the adequacy of the provisions.
- 69. The Inquiry found that the documents were not properly tailored to the specific activities of the Charity. They did not address the difficulties that the Charity has encountered when working in remote regions where there are language, literacy and banking challenges. This is imperative given that the Charity works solely overseas, and that charity trustees must take steps to ensure that their charity complies with the law of England and Wales as well as local requirements where they are working. The policies also did not adequately assess the nature and extent of the risk of the Charity coming into contact with proscribed organisations. This was particularly important for the Charity given the Foreign and Commonwealth Office's assessment that there is currently a high threat from terrorism throughout Indonesia and Pakistan<sup>15</sup>.

<sup>14</sup> This also raised concerns for the Inquiry that proper decision-making procedures were not being followed, in accordance with the Charity's governing document.

<sup>15</sup> The Foreign and Commonwealth Office, in its published travel advice by country, states that there is currently a high threat from terrorism throughout both Indonesia and Pakistan - <http://www.fco.gov.uk/en/travel-and-living-abroad/travel-advice-by-country/>

70. Although the Inquiry appreciated that flexibility and speedy processes are necessary for a charity operating overseas, in remote areas, and in the aftermath of an emergency, the Inquiry found that - even in these circumstances the policies - fell short of minimum requirements. The policy documents did not address due diligence procedures, particularly what the Commission has described in its guidance as the "Know Your Beneficiaries" and the "Know Your Partner" principles<sup>16</sup>. The Charity's relationship with their local partner in Indonesia was an example of the trustees' not adequately applying the 'Know your Partner principles'. The trustees were unable to answer basic questions concerning the work undertaken in Indonesia via this partner, or to explain how invoices provided from this individual were linked to the Charity's activities (see the section on *Due Diligence and Monitoring* above). The absence of a basic system to conduct due diligence about, or to monitor the work of, third party organisations used by the Charity exposed the Charity's assets to the risk of misapplication, and created further risk to charitable assets by unnecessarily exposing the Charity to potential tax liability<sup>17</sup>.

71. The adoption by the Charity trustees of policy documents which did not appear relevant to the Charity (for example a 'Billing Policy') seemed to indicate that the provisions of the documents had been lifted from model documents, and did not suggest particular scrutiny by the trustees, before sign-off. It is acceptable for trustees to use model documents however, when doing so they should be satisfied that the model meets the requirements of their charity. This Inquiry found that the trustees had fallen short of the standards expected in this regard.

72. The policy documents included an *Anti-Fraud and Corruption Policy* which makes reference to terrorist financing:

*'We must ensure that we are not inadvertently used by a terrorist organisation. The authorities are concerned about charities, who are therefore in positions of trust and authority, being used on behalf of the terrorist organisation. Alternatively another concern is that an employee may use the charity's funds to support the terrorist organisation, by for example directing charity funds to a body connected with a terrorist organisation'.*

73. Despite identifying this as a risk (which seemed appropriate for the Charity given the higher-risk areas in which it operates and the nature of the allegations which prompted this Inquiry), the trustees had not established or implemented procedures to address this issue. For example the policies made no reference to checking the names of beneficiaries, employees or partner organisations against the consolidated list of financial sanctions targets, maintained by HM Treasury, or any list maintained by other governments in areas of operation, to help them assess the suitability of potential employees or third parties.

74. On the evidence it had seen, the Inquiry was therefore unable to satisfy itself that the Charity's trustees had adequately discharged their legal duties and responsibilities under charity law to take appropriate steps to prevent abuse of their charity and ensure that they did not commit a criminal offence. The Inquiry found that the Charity trustees had not:

- adequately informed themselves about the nature and extent of the risk of their charity coming into close contact with proscribed organisations;
- obtained up-to-date information about the security situation in their areas of operation and the risks this posed; and
- introduced and recorded appropriate risk assessment procedures.

16 Although it is acknowledged by the Inquiry that the *Governing Policies* do consider the 'Know Your Donor' principle.

17 See paragraph 113 of *Wider Lessons* for further details of the implications of the Finance Act 2010 on charities.

## Conduct of Inquiry

75. Throughout the Inquiry the Commission liaised with other agencies to ensure the conduct of this civil investigation did not prejudice the criminal investigation.
76. The Inquiry examined the finances and management of the Charity. This included establishing who was acting in the management and administration of the Charity. Immediately after the Inquiry was opened in August 2006, the Inquiry contacted individuals listed on the Commission's Register of Charities as the trustees of the Charity. The Inquiry corresponded with the trustees and remained in contact with them - primarily through their legal advisors - throughout the course of the investigation. This included written correspondence, telephone calls and meetings at both the Charity's premises and the Commission's offices.
77. The Inquiry issued orders under section 18(1)(iv) of the Act to two banks which held accounts in the name of the Charity ("the Orders"). This was a temporary and protective measure to 'freeze' those accounts, in order to safeguard funds and ensure they were used only for the purposes of the Charity. During the Inquiry the Commission approved certain payments from these accounts following submissions from the trustees of satisfactory evidence that the expenditure was proper and reasonable.
78. The Orders were reviewed regularly throughout the course of the Inquiry and the trustees were informed of the outcome of each review, and of the procedures to follow should they wish to challenge the Commission's decision-making.
79. On 15 May 2007 a trustee of the Charity requested a review of the decision taken on 18 April 2007 to keep in place the 'freezing' orders made on 23 August 2006, under section 18(1)(iv) of the Act. In accordance with the Commission's Decision Review process, this review was conducted on 2 July 2007 by the then Head of Division. The outcome of the Decision Review was that the Orders should remain in place. The trustee did not seek further review of this decision. The Orders continued to be regularly reviewed every 2 months during the case.
80. The Inquiry obtained information from a range of sources, including material removed from the Charity's premises by the Police. Material was also provided by the trustees, their legal advisors and the Charity's bankers in both Pakistan and England. Where appropriate, this information was obtained by way of an order made by the Commission under section 9 of the Act. On 13 November 2008 a direction made by the Commission under section 8 of the Act was issued to the trustees to obtain information from them relating to the Charity's assets held in bank accounts in Pakistan and documentation relating to the Charity's activities in Indonesia.
81. The team working on the Inquiry liaised with the Commission's International Programme to further its understanding of the operating environment for charities and NGOs in Pakistan and Indonesia.

82. The Inquiry sought to obtain and verify information from individuals in Indonesia and Pakistan. This included corresponding with:

- the accountant responsible for the Charity's accounts in Pakistan;
- the Charity's bank in Pakistan;<sup>18</sup>
- the Charity's former coordinator in Pakistan; and
- the Charity's partner in Indonesia.

83. To further its understanding of the Charity's work in Pakistan the Inquiry:

- contacted four charities who had previously worked with the Charity. This included a funder of the Charity who confirmed that work had been undertaken and that one of their trustees had visited Pakistan and seen evidence of that work; and
- unsuccessfully attempted to contact the Pakistani Earthquake Reconstruction and Rehabilitation Authority, with whom the Charity had engaged with following the 2005 earthquake in Pakistan.

84. To further its understanding of the Charity's work in Indonesia and particularly the costs associated with building and supporting an orphanage there, the Inquiry:

- identified a charity which had also built an orphanage in the same village in Indonesia as the Charity and met with one of its trustees to discuss their experience of conducting this kind of activity in that particular part of Indonesia;
- contacted three large charities who had conducted work in Indonesia to obtain feedback on their experiences and knowledge of operating in that area; and
- unsuccessfully attempted to verify with the suppliers the utility bills provided by the Charity as evidence in support of its work in Indonesia.

85. The Inquiry conducted a financial analysis of the Charity's records.

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<sup>18</sup> In accordance with the Inquiry's request the trustees instructed their bank in Pakistan to comply with the Commission's request for information.

## Conclusions

86. Charities which undertake valuable humanitarian emergency relief work in areas of high risk must ensure that adequate safeguards are in place to protect their assets and reputation so to ensure public trust and confidence in charity more generally.
87. The Inquiry recognised that vital relief work was carried out by the Charity, and acknowledged that what could be expected of the Charity should take into account the nature of its work, its size and income, and the challenges of working overseas - particularly in remote areas of Kashmir and Indonesia. The Inquiry also acknowledged the Foreign and Commonwealth Office's view that there is a high threat from terrorism in both of these regions<sup>19</sup>.
88. In this investigation the Commission concluded:
  - from the information examined by the Inquiry there was no evidence to indicate that the trustees diverted charitable funds for unlawful or non-charitable purposes. However, the Commission further concluded that the trustees were unable to satisfactorily verify the end use of funds in both Indonesia and Pakistan;
  - that the insufficiency of the measures taken to control, monitor and document the use of charitable funds (in this case by third parties overseas) prevented the Charity's trustees from being able to demonstrate that those funds had been used legitimately and properly and in furtherance of the Charity's purposes. It also risked the Charity's funds being misappropriated without the trustees' knowledge;
  - that the trustees' inability to account for funds, and to follow appropriate processes and checks when expending Charity funds, placed the assets of the Charity at risk and amounted to mismanagement on the part of the trustees in the administration of the Charity. Further the trustees' failure to inform their accountant and the Commission about the existence of the Charity's bank accounts in Pakistan (see paragraphs 49-56) amounted to mismanagement and misconduct<sup>20</sup> on their behalf in the administration of the Charity; and
  - having taken into account the factors detailed in paragraph 87, the trustees had fallen short of ensuring that adequate safeguards were in place to protect the Charity's assets and its reputation. However, despite the mismanagement and misconduct identified the trustees were committed to the future good governance of the Charity. If the trustees act to make improvements to policies and processes the risk of the Charity's assets being misappropriated will be reduced. It was therefore concluded that an appropriate approach, proportionate to the risks posed and resources available, was for the Commission to provide advice and guidance to the Charity, and to direct the trustees to carry out a governance review of the administration and management of the Charity and implement the outcome (see *Actions required of the trustees*).

19 <http://www.fco.gov.uk/en/travel-and-living-abroad/travel-advice-by-country/>

20 The Courts have held that co-operation with the Commission should be expected of any 'self-respecting trustee', even in the absence of any statutory obligation. Failure by charity trustees to co-operate with the Commission during the course of an Inquiry, where serious regulatory concerns have been identified, may therefore indicate mismanagement or misconduct in the administration of a charity. "Misconduct" will normally involve some dishonesty, whereas "mismanagement" will not necessarily, but may still be very serious in its consequences.

## Regulatory action taken

89. The Inquiry exchanged information during the investigation, under section 10 of the Act, with the Police and law enforcement agencies.
90. During the Inquiry, the following regulatory action was taken to gather information:
  - on 18 October 2006, 27 July 2007, 15 September 2008, 7 October 2009 and 25 November 2009 the Inquiry issued orders under section 9 of the Act to the Charity's bankers, requesting details of transactions from the Charity's bank accounts; and
  - on 28 September 2007 a direction under section 8 of the Act was issued to an individual the Inquiry believed to be a trustee of the Charity, requesting that the individual confirm whether they had signed a Companies House 288a form regarding their appointment as a director (and therefore a trustee) of the Charity; and
  - on 13 November 2008, directions under section 8 of the Act were issued to the trustees, requesting information about the Charity's assets held in bank accounts in Pakistan and documentation relating to the Charity's activities in Indonesia.
91. The Inquiry took the following regulatory action to temporarily protect the Charity and its property:
  - on 23 August 2006 the Inquiry issued two orders under section 18(1)(iv) of the Act, temporarily 'freezing' the Charity's bank accounts in England and Wales. Both of these orders were discharged on 20 April 2011; and
  - on 25 August 2006 the Commission issued two orders under 18(1)(iv) of the Act, temporarily 'freezing' bank accounts believed to belong to the Charity after the Commission was contacted by the banks holding those accounts. These orders were discharged the same day, as soon as it was identified that the bank accounts did not in fact belong to the Charity.
92. On 20 April 2011 the Commission used its powers under section 19A of the Act to make an Order which directed that the trustees and the Charity implement a number of actions aimed to improve governance, within certain timescales and report to the Commission on progress as specified (see paragraphs *Actions required of the trustees*).

## Impact of Commission intervention

93. In publishing this report the Commission has placed on the public record its findings and conclusions regarding the Charity, and the allegations that had linked the Charity to a conspiracy to commit terrorist offences on aeroplanes departing from the UK.
94. The Inquiry's action in making orders under section 18(1)(iv) of the Act to temporarily 'freeze' the Charity's bank accounts in England and Wales meant that the funds held in these accounts were safeguarded whilst the investigation examined serious allegations that charitable funds may have been used unlawfully.
95. The Commission provided specific regulatory advice and guidance to the trustees, pertinent to their work overseas and in high risk areas to help ensure the trustees meet their legal duties and responsibilities as trustees.

96. The Commission directed the trustees to undertake a governance review and implement the outcomes of that review. This will strengthen the management of the Charity and will address the weaknesses in the Charity's financial controls.

## Resources applied

97. The Commission adopted a multi-disciplinary team working approach on this Inquiry. The team consisted of investigators, lawyers and accountants. Translation costs and the costs of having a transcript produced for one of the trustee meetings were also met by the Commission.

## Actions required of the trustees

98. On 20 April 2011 the Charity and its trustees were directed by Order of the Commission to carry out a governance review of the administration and management of the Charity, and to implement the outcome within three months of the date of the Order.

99. The governance review must ensure that robust governance frameworks and financial controls are in place –supported by policies and procedures appropriate for a charity working both overseas and in high risk areas.

100. Under the terms of the Order the trustees must submit a report to the Commission outlining the activities the Charity has undertaken and how the trustees have ensured the Charity's assets have been, and will continue to be, protected. This report must be submitted no sooner than 11 months and no later than 12 months of the date of the Order.

101. The Commission will monitor the trustees' compliance with the Order.

102. Further action may be required of the trustees depending on the outcome of the governance review and the implementation of the review's outcomes.

## Issues for the wider sector

103. This section identifies issues arising from the Inquiry which may be of interest to the wider sector. This section of the report is framed around the three issues identified at the start of the Inquiry (see paragraph 10).

### Safeguards to mitigate the risk of charitable funds being used unlawfully

104. Proven instances of terrorist involvement in and abuse of charities are extremely rare but are completely unacceptable. It is the responsibility of charity trustees to safeguard their charity from the risk of abuse.

105. The Commission will support trustees to protect their charities from the risk of abuse, including terrorist abuse. It believes that the most effective way for the sector to minimise its exposure to the risk of terrorist abuse is through implementing strong governance arrangements, financial management and partner management. The Commission recognises that this is a difficult area and has produced guidance on designation, and other issues relating to terrorism legislation. For further information see; [http://www.charitycommission.gov.uk/Our\\_regulatory\\_activity/Counter\\_terrorism\\_work/protecting\\_charities\\_landing.aspx](http://www.charitycommission.gov.uk/Our_regulatory_activity/Counter_terrorism_work/protecting_charities_landing.aspx)

106. Trustees must be vigilant to ensure that a charity's premises, assets, staff, volunteers and other resources cannot be used for activities that may, or appear to, support terrorist activities. People and groups can be designated for association with Al-Qaida and the Taliban (UN designations) or because HM Treasury reasonably believes that that person is/or has been involved in terrorist activity or for any other reasons given in the Terrorist Asset-Freezing etc. Act 2010. Some are also designated as part of sanctions against foreign countries, governments, entities or individuals. Given the financial restrictions on the affairs of designated individuals and entities, they may seek to take advantage of charities and their work. Trustees must therefore put in place proper procedures for managing the risks of coming into contact with designated entities, groups or persons, and taking appropriate steps if the situation arises.

107. If trustees, charity employees or volunteers have information about possible terrorist activity they should telephone the Anti-Terrorist Hotline on 0800 789 321. Charity trustees, employees and volunteers are now under a positive legal duty to report their suspicions of terrorist financing offences to the Police. If they do not, they may commit a criminal offence. In addition if a charity is concerned about an immediate threat to life they should contact the Police immediately.

108. Charity trustees must report instances where the charity (including any individual staff, trustees or volunteers) has any known or alleged link to a proscribed organisation or to terrorist or other unlawful activity to the Commission as soon as they are aware of it.

109. Unfortunately, when there are disasters and charities are appealing for funds, some people take advantage of the public's generosity and use a variety of methods to divert donations their way for their own personal gain. Charities may be vulnerable to fraud or other abuse from persons working or volunteering for, or otherwise associated with the charity, perhaps taking advantage of the highly-pressurised environment which can occur in a post-disaster situation to act improperly without detection.

### **Financial management and the supervision of overseas activities**

110. Trustees are under a legal duty to protect charity assets<sup>21</sup>. Having sufficiently rigorous controls not only provides protection for a charity's assets but is also the best defence for the trustees against the charge of failing to protect their charity's assets and funds.

111. A significant aspect of a trustee's legal duty to protect charitable assets with the necessary care means ensuring that where a charity gives money to partners or beneficiaries, or uses partner and delivery agents, or where it funds other projects, charity trustees must conduct appropriate due diligence checks and properly and appropriately monitor the use of the charity's funds, checking both that funds reach their destination and that they are used for the purposes intended.

112. Charity trustees must exercise sufficient control over their charity's financial affairs both in the UK and internationally. As an absolute minimum, they must keep proper and adequate financial records for both the receipt and use of funds and audit trails of decisions. Records of both domestic and international transactions must be sufficiently detailed to show that funds have been spent properly and in a manner consistent with the purpose and objectives of the organisation.

<sup>21</sup> For further guidance see *CC8 - Internal Financial Controls for Charities* which can be viewed on our website at; <http://www.charity-commission.gov.uk/Publications/cc8.aspx>

113. The provisions of the Finance Act 2010, recently enacted, reinforce the trustees' duties when transferring funds to a non-UK body, to take 'such steps as are reasonable' to ensure the funds would be applied for purposes recognised as charitable under English law. This revised legislation makes it clear that such steps have to be reasonable in the view of Her Majesty's Revenue and Custom (HMRC). As a result charities working internationally need to ensure that their practices for assessing grant applications and monitoring donations overseas stand up to scrutiny. Further information on this can be found on HMRC's website.

114. Financial transparency is crucial to help maintain the confidence of the public who give money to charity. Charities' annual reports and accounts are extremely important in helping maintain public confidence in the integrity of charities as well as in charity more generally. It is imperative that they accurately reflect the charity's income and expenditure.

115. Charities setting up disaster funds and spending often large amounts of money quickly, in areas affected by disasters are as much, if not more, at risk of fraud and other financial crime than charities operating in more stable physical and financial environments. They may be operating in countries where the physical and financial infrastructure is affected. They may be starting operations in a new area or working with new partners. They may need to place an unusual reliance on cash transfers or use of financial intermediaries. It may be more challenging for charities to maintain the same standards of transparency and accountability as would apply in the UK, but they must strive to do this.

### **Governance**

116. An effective charity is run by a clearly identified trustee body who are aware of their duties and responsibilities as charity trustees. Holding the position of trustee in name but failing to fulfill the legal duties and responsibilities of a trustee amounts to misconduct and mismanagement in the administration of a charity.

117. Trustees are jointly and equally responsible for the management of their charity. To be effective and to meet their statutory duties as charity trustees they must contribute to the management of the charity and ensure that it is managed in accordance with its governing document and general law. They must also bear in mind their over-riding duty to take decisions that are in the best interests of the charity and when doing so should take all relevant factors into consideration and should keep a record of the discussion.

118. All charities should have appropriately tailored internal policy documents which address the specific risks associated with the kind of activities that are undertaken. Trustees should ensure that these policies are implemented and reviewed at appropriate junctures. A failure to implement internal policy documents could be evidence of mismanagement in the administration of the charity.



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