National Audit Office

Review
by the National Audit Office

Department for Culture, Media & Sport

Due diligence processes for potential donations

JULY 2017

Our vision is to help the nation spend wisely.

Our public audit perspective helps Parliament hold government to account and improve public services.

Contents

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Summary

1 Museums and galleries increasingly rely on philanthropic donations due to the reduced availability of public grant funding. Donations carry unique risks as a source of income and there have been high-profile cases of the damage that can be caused if these risks are not well managed.

2 We have reviewed the systems and policies relevant to donations management that are in place across a number of the museums and galleries sponsored by the Department for Culture, Media & Sport (DCMS). This enabled us to draw together a summary of the issues faced and best-practice examples of how to manage the risks.

3 We have grouped best practice into three thematic areas:

Governance →	Donations policies Trustee oversight
Risk management →	Risk assessment Due diligence and decision-making
Staff and stakeholder management →	Learning and development Managing donor relations

4 Generally, we found that institutions have a good understanding of issues involved in managing donations but the extent to which this had been developed into formal procedures and processes varied. There is, however, scope for museums and galleries to adopt more of the best-practice procedures and to learn from those generally considered to be leaders in the sector.

5 The National Audit Office (NAO) will continue to work with DCMS and its arm's-length bodies to understand the risks and pressures facing the museums and galleries sector and to make use of our unique insight to highlight further key messages that emerge. Please direct any questions on this review to Paul Keane, as Portfolio Director for the DCMS sector, or your audit manager.

Part One

Background to our work

1.1 The Department for Culture, Media & Sport (DCMS) has responsibility for 16 museums and galleries which are non-departmental public bodies and also charities. DCMS provides funding to these bodies directly and also indirectly to other museums and galleries in the wider culture sector via the Lottery distributors – principally Arts Council England and the Heritage Lottery Fund.

1.2 The National Audit Office (NAO), on behalf of the Comptroller & Auditor General, undertakes the statutory audit of 15 of the DCMS-sponsored museums and galleries. Through this audit work we have become aware of the increasing challenges faced by the sector in reducing the reliance on public funding. We frequently see matters relating to financial sustainability on the strategic risk registers of the museums and galleries.

The financial context

1.3 Public funding in the museum and gallery sector has reduced in recent years. Financial sustainability has required the development of strategies for the more efficient use of available resources and structured cost reduction. At the same time, the sector has also been expected to increase its revenue from sources other than public funding.

1.4 The DCMS *Culture White Paper* sets out government's view that there is scope for additional revenue not only from an expansion of the sector's commercial activities, but also an increase in philanthropy and private donations.[1] In recent years, DCMS's museums and galleries have set ambitious targets for fundraising activity and looked to increase recruitment of museum staff with development and fundraising expertise.

Increased reliance on fundraising and philanthropy

In 2012-13 the total of grant-in-aid (GIA) given by DCMS directly to the museums and galleries amounted to £444 million, which was 52% of the sector's total income. This had reduced to £393 million in 2015-16, which represented 45% of the total sector income.

Over the same period, income from legacies, donations and other voluntary sources increased from £147.7 million (17% of total sector income) in 2012-13 to £182 million (21% of total sector income) in 2015-16.

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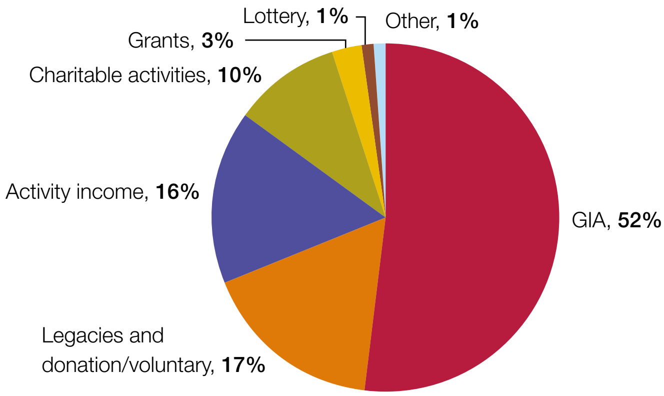
1 Department for Culture, Media & Sport, *The Culture White Paper*, Cm 9128, March 2016. Available at: www.gov.uk/government/uploads/system/uploads/attachment_data/file/510798/DCMS_The_Culture_White_Paper__3_.pdf, p. 50.

1.5 Figures 1 and 2 illustrate the increase in donations, legacies and other voluntary income within the overall mix of income sources within the sector:

Figure 1

Sources of income for museums and galleries 2012-13

Seventeen per cent of income from legacies and donations in 2012-13

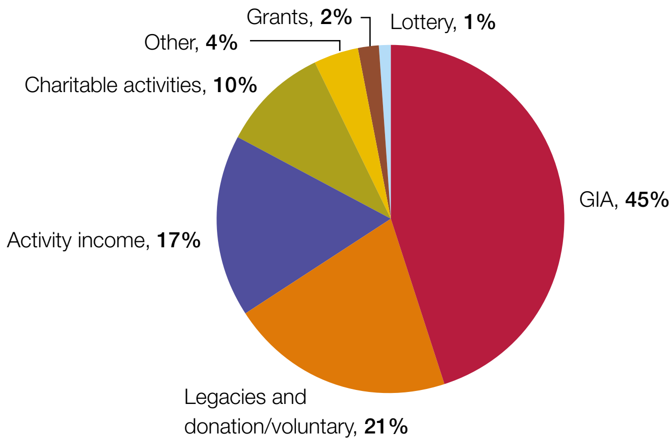


Source: National Audit Office analysis of published annual reports of DCMS-sponsored museums and galleries

Figure 2

Sources of income for museums and galleries 2015-16

Twenty-one per cent of income from legacies and donations in 2015-16



Source: National Audit Office analysis of published annual reports of DCMS-sponsored museums and galleries

Risks associated with income from donations

1.6 Private donations present different risks to other sources of revenue and cannot be managed in the same way as commercial transactions. Transactions are conducted within a less formal legal framework and donors may have motives other than philanthropy, for example to achieve respectability, influence or undisclosed commercial gain. Risks include:

- legal risk – if accepting a donation could breach legislation such as the Proceeds of Crime Act 2002 (for example, where the donor has generated the underlying funds through illegal activity). This could expose a charity to legal or regulatory challenge;
- financial risk – if the donor cannot honour the donation in full or in part. This would be most damaging where the receiving institution was heavily reliant on the anticipated donation to fund key strategic expenditure;
- reputational risk – if accepting the donation creates an association with an individual or entity which is perceived to be inappropriate or unethical by other stakeholders. This would include the perception of the public, employees and other significant donors; and
- dependency risk – if accepting the donation gives the donor an undue level of influence over a charity and its trustees.

1.7 The increased pressure to generate revenue via donations may increase the likelihood that these risks occur if they are not effectively managed. This could have a damaging impact for the charity itself and its trustees, who could be challenged on whether they have met the requirement to act in the charity's best interests.

Increasing public and regulatory focus on fundraising ethics

1.8 High-profile examples have brought public attention to what can go wrong if appropriate governance and management procedures are not in place to mitigate the risks over significant donations. In particular, in 2011 the Woolf Inquiry, which reviewed the relationship between the London School of Economics (LSE) and Libya, found that failures in process had led to the acceptance of donations that otherwise should have been rejected.[2]

2 Lord Woolf, *The Woolf Inquiry – An Enquiry into LSE's links with Libya and the lessons to be learned*, October 2011. Available at: www.woolflse.com/dl/woolf-lse-report.pdf, p 70.

Woolf Inquiry: recommendations for the LSE directly relevant to donations

1 The LSE should have an embedded code dealing with ethics and reputational risk which applies across the institution. The LSE should set up a committee to effectively deal with issues relating to the code.

8 The LSE should adopt an up-to-date policy on donations. That policy should be contained as part of or in a separate document contained within the School's code on ethical and reputational risk.

9 The donations policy should include a procedure for the scrutiny of proposed donations with clear lines of responsibility. Any individual who has responsibilities in relation to gifts should have those identified in writing.

10 The donations policy should identify whether, and in what circumstances, it is appropriate for an individual, centre or department to request a donation on their own initiative. The donations policy should require that the Office of Development and Alumni Relations must be informed of any potential donation.

11 The School should set out written guidance on the appropriate relationship between the LSE and a donor.

1.9 The ethics of fundraising have also come under increased public scrutiny in recent years following negative media coverage of fundraising activities and attention from the Public Administration and Constitutional Affairs Committee.[3] In response, the Government set up the Etherington Review.[4] The Review team published its report in September 2015 and recommended the creation of an independent body to set and regulate fundraising standards among charities and other bodies.

1.10 The Fundraising Regulator was created in 2016 and it launched a Code of Fundraising Practice which outlines the standards expected of all charitable fundraising organisations in the UK.[5] Although this code of conduct for fundraisers does not specify standards of due diligence, it does state that performance of due diligence procedures on potential donations is essential.

Regulation in the DCMS sector

1.11 Of the 16 museums and galleries directly sponsored by DCMS 13 are exempt charities. This means they are not registered with the Charity Commission or directly regulated by it. Under the Charities Act 2011, DCMS was appointed as principal regulator with a requirement to monitor and promote compliance with charity law. Despite this, the Charity Commission's guidance on legal compliance and best practice in fundraising is still relevant to exempt charities.

3 House of Commons Public Administration and Constitutional Affairs Committee, *The 2015 charity fundraising controversy: lessons for trustees, the Charity Commission, and regulators*, HC 432, January 2016. Available at: www.publications.parliament.uk/pa/cm201516/cmselect/cmpubadm/431/431.pdf

4 Sir Stuart Etherington et al, *Regulating Fundraising for the Future – Trust in charities, confidence in fundraising regulation*, September 2015. Available at: www.ncvo.org.uk/images/documents/policy_and_research/giving_and_philanthropy/fundraising-review-report-2015.pdf

5 The Fundraising Regulator, *Code of Fundraising Practice*, July 2016. Available at: www.fundraisingregulator.org.uk/code-of-fundraising-practice/code-of-fundraising-practice/

1.12 In 2016 the Charity Commission updated its guidance on fundraising to reflect the changing regulatory and financial environment. This now includes a guide to trustee duties in respect of fundraising and updated guidance on a range of due diligence activities.[6,7]

1.13 DCMS museums and galleries face the challenge of stimulating increased donations in an environment of increased public and regulatory scrutiny of fundraising activity. Performing appropriate due diligence procedures on potential donations is, therefore, an increasingly important issue for these bodies and one that needs to be managed well. The NAO has sought to review the way in which individual museums and galleries establish and execute due diligence procedures, in order to establish areas of best practice which can be applied across the DCMS sector. This report sets out the findings of our review.

Background – key messages

- The ethics of fundraising are subject to increased public and regulatory scrutiny. DCMS charities should be aware of the Code of Fundraising Practice and may be required to register with the Fundraising Regulator.
- Although most DCMS charities are not registered with the Charity Commission, they should ensure they keep up to date with the Commission's guidance, which is also relevant to exempt charities.

6 The Charity Commission, *Charities fundraising: A guide to trustee duties*, June 2016. Available at: www.gov.uk/government/publications/charities-and-fundraising-cc20

7 The Charity Commission, *Due diligence monitoring and end use of funds*, September 2016. Available at: www.gov.uk/government/publications/charities-due-diligence-checks-and-monitoring-end-use-of-funds

Part Two

Scope of the report and approach

2.1 In January and February 2016, the National Audit Office (NAO) met with individuals responsible for donor due diligence in a broad range of arm's-length bodies:

- **The Geffrye Museum** is in Shoreditch, London and explores the home from 1600 to the present day.
- **The Imperial War Museum** is a family of five museums. It provides for and encourages the study and understanding of the history of modern war and 'wartime experience'.
- **The National Gallery** houses the national collection of paintings in the Western European tradition from the 13th to the 19th centuries. It is located in Trafalgar Square, London.
- **The National Portrait Gallery** houses a collection of portraits of historically important and famous British people. It is located in St. Martin's Place, London.
- **The Natural History Museum** is a museum of natural history and a scientific research centre based primarily in South Kensington, London.
- **The Science Museum Group** is a family of five museums. The principal museum is based in South Kensington, London and exhibits scientific, technological and medical achievements from across the globe.
- **Tate** is a family of four art galleries. It displays the national collection of British art from 1500 to the present day, along with international modern and contemporary art.
- **The Victoria and Albert Museum** is a museum of decorative arts and design, housing a permanent collection in South Kensington, London.

2.2 We are grateful to all those who took the time to assist us in this work.

2.3 Engagement with the bodies listed above took the form of semi-structured interviews and a review of systems, documentation and policies relevant to donor due diligence. Our review focused on the arrangements for donations and gifts and did not cover all other forms of fundraising incomes, such as corporate sponsorship and endowments. We also drew on wider guidance on best practice and other relevant published material.

Key elements of best practice

2.4 Our review identified three thematic areas of best practice for the sector to consider in responding to the risks associated with significant potential donations. The extent to which these are applicable and can be formalised will vary by size of institution, but we believe there are relevant issues for all charities to consider. The three thematic areas we have identified are:

- governance;
- risk management processes; and
- staff and stakeholder management.

Overall findings

2.5 Overall, we found that there was good awareness of the issues and risks related to donations management among the key officials we spoke to and the extent of procedures tended to reflect the level of risk faced by the charity. However, written policies and procedures did not always reflect actual practice, either through being out of date or being insufficiently detailed. There was also a lack of information in the public domain in terms of many of the charities' ethical positions on fundraising and donations.

2.6 We corroborated our findings with the work of our teams responsible for the financial statement audits of the Department for Culture, Media & Sport (DCMS) museums and galleries. Our review did not identify any evidence of a significant inappropriate donation being accepted in the sector or of a breach of money-laundering legislation. This was consistent with the findings of recent audits completed by the NAO's financial audit teams.

Part Three

Governance

3.1 In the context of this review, we have defined governance to mean the framework of policies and monitoring processes established by senior management and the board to oversee due diligence activity. This includes the charity's formal policies on receiving donations and ethical issues, as well as the role of trustees in setting and monitoring the organisation's approach to these matters.

Written donations policies

3.2 In charities which had a clear and structured approach to due diligence, we saw that written donations policies were in place to provide the overarching framework for managing donations risk. In a number of other cases, written policies either did not exist or were under development. The good donations policies we saw set out a clear ethical position in respect of donations along with the principles which would be used to guide decisions taken by a charity on whether to accept or reject them. A clear policy can encourage clarity and consistency of internal decision-making and reduce the risk of accepting donations from inappropriate sources.

3.3 Charities with well-established policies emphasised the benefits of these being publicly available. Public documents clearly setting out the main reasons why donations could be rejected are a useful guide to potential donors. They help build relationships of trust with the donor community and reduce the likelihood that an 'ask' (a request for a donation) will be made which will be clearly inappropriate.

3.4 A freely available policy can also enable stakeholders to understand the thought process behind the acceptance of significant donations. The policy can act as the public face of the charity's ethical position on donations and support the charity's wider communications strategy.

Keeping policies up to date

3.5 We found that there was inconsistency among museums and galleries regarding whether written policies existed and whether they were made available on the institutions' websites (of the 16 Department for Culture, Media & Sport (DCMS) museums and galleries only four had published their policies). Where policies did exist, it was not always clear when the policies had been most recently updated and whether they had been subject to periodic review. There is, therefore, a risk in some cases that the written policies do not reflect the charity's latest ethical position on acceptance of donations, or current best practice in the sector.

Good-practice example – timed cyclical review of policies

It is best practice to show the date of publication on any policy. One charity also showed the date of the next scheduled policy review alongside this, which was three years from the publication date. As part of a broader approach to keeping practices up to date, policy reviews were then built into the agenda of trustee and audit committee meetings as standing items in order that policies which are due to be reviewed are scrutinised and updated on a timely basis.

Core elements of a donations policy

3.6 The best policies that we saw succinctly set out the following:

- the principles that will guide decision-making on donations;
- how the principles will be applied to different types of donation;
- the processes that donors can expect the charity to undertake before the donation is accepted; and
- any prohibited form of donations or donor relationships.

3.7 Development teams we spoke to stressed the importance of the tone of the policy documents as well as their content. Effective policies emphasised that the charity welcomed new donor relationships and provided reassurance that the intrusiveness of acceptance procedures was proportionate to identified risk. Charities are also increasingly aware of the requirements of the Data Processing Act 1988 to process personal data fairly, and effective policies provide transparency about how this will be achieved. Without all of these elements in place, policies may discourage legitimate donors from involving themselves with the charity.

Good-practice example – London School of Economics (LSE)

As part of its response to the Woolf Inquiry, the LSE published a detailed *Donations Acceptance Policy,* which provides a good example of a public-facing policy document:

Available at: www.lse.ac.uk/intranet/LSEServices/Advancement/documents/07-06-16-LSE-Donations-Acceptance-Policy---Final.pdf

This sets out the principles that will govern the acceptance of donations and gifts and links to other relevant LSE policies including the overarching Ethics Code and also the Procedures for the Ethical Screening of Grants and Donations.

3.8 More detailed guidance on preparing a donations policy has been prepared by the Institute of Fundraising:

Available at: www.institute-of-fundraising.org.uk/library/donation-acceptance-and-refusal/donation-acceptance-and-refusal-guidance-for-web-17.07.13.pdf

3.9 The guidance document covers:

- why having a policy is important;
- creating and developing policies/processes – this includes a list of the most relevant legislation and regulation that needs to be taken into account;
- processes – how to gather, use and store information; and
- implementation – how to run the donations processes.

Trustee awareness and involvement

3.10 Trustees have a personal legal responsibility for a charity's management and administration. They are required to act in the best interests of the charity and ensure that appropriate, ethical decisions are made. In this context, it is important that trustees are aware of the charity's approach to fundraising and donor relations. Conscientious trustees will be aware of key policies on accepting donations and often play a role in the decision-making process where issues of high risk are identified.

3.11 We saw good examples where trustees had approved the charity's overarching ethical and donations policies. These complemented other related internal policies, including those on the acceptance of gifts and hospitality and donated assets. A number of museums and galleries we spoke to have a good track record in seeking and receiving trustee approval for their policies.

3.12 We saw a small number of cases where trustees had, via audit committees, sought periodic assurance from their internal auditors over the effective implementation and operation of donations policies. This can be a useful source of reassurance for charities where donations management represents a significant strategic risk. The audit reports we have seen have typically identified areas for improvement, in both the design of policies and procedures and their actual implementation, needed to bring the charity in line with best practice.

3.13 Our conversations with development teams also demonstrated the value they draw from trustee intelligence about the donor community. We were made aware of several cases where a trustee's network of contacts, often in the financial services sector, informed institutional knowledge on potential donors. This proactive engagement with development teams also opened up opportunities to explore possible sources of new donations.

Ethics committees

3.14 At some of the larger charities, an ethics committee had been established, which played an important supporting role in the decision-making process for high-risk donations. These are typically sub-committees of the board of trustees, which focuses on establishing and maintaining proper conduct in matters with an ethical aspect. These larger charities welcomed the input from committees, which provided challenge but also reassurance that contentious or high-risk potential donations had been handled appropriately. Committees also reviewed the charity's donations policy and provided reassurance to the board of trustees that it remained fit for purpose. Committee membership typically included trustees along with co-opted independent members to bring an impartial level of scrutiny to proceedings.

Case study

An established ethics committee

One large charity has a well-established ethics committee whose members include legal experts, business leaders and sector experts. It reviews high-value propositions (more than £100,000 in value) and those which trigger corporate or political risk. The charity's development team provide the output of their research to the committee to enable it to review the case. The committee then reports to the board of trustees with independent, evidence-based conclusions on whether such donations should be accepted. It also reviews the list of ongoing relationships with major donors annually.

Governance – key messages

- Written policies encourage a consistent approach and ethical position in respect of donations management.
- Publication of the policies helps manage stakeholders expectations of the donations process.
- Policies should be reviewed cyclically to keep them up to date.
- Trustees should be aware of due diligence issues and approve the overarching policies.
- Ethics committees can be an effective forum for oversight of donations policies and advising on high-risk decisions on accepting donations.

Part Four

Risk management

4.1 In the context of our review, we have defined risk management as the forecasting and evaluation of risks around accepting potential donations and the internal processes supporting these. Informed risk management is essential in ensuring that the due diligence procedures undertaken by charities are proportionate.

Documented internal procedures

4.2 Well-documented internal procedures help to ensure that risk assessment operates in a consistent manner and is underpinned by an adequate evidence base. In the larger organisations we reviewed, overarching donations policies were typically supported by more detailed process documentation. The detailed guidance set out the expected practical steps for assessing individual donors and the roles and responsibilities of staff involved at all levels.

4.3 Across the museums and galleries sector, we were aware of significant staff turnover in development teams – often markedly higher than in other areas of these organisations. Documented policies and procedures reduce the risks that due diligence procedures are heavily reliant on key individuals' knowledge and understanding.

4.4 The best internal procedures we reviewed set out:

- roles and responsibilities of those involved in the process (including segregation of duties);
- initial risk assessment;
- due diligence procedures; and
- decision-making processes.

Defined roles and responsibilities

4.5 Defined roles and responsibilities give staff clarity on what tasks they need to perform in relation to donations management. They help ensure that the appropriate people carry out appropriate tasks, building accountability into each stage of the process.

4.6 Effective segregation of duties within due diligence procedures mitigates the risk of error or bias in decision-making. Good-practice examples we saw included requirements that:

- an individual carrying out fundraising activities should not perform the research role in terms of gathering and assessing the data on the donor; and
- an individual separate to those performing the fundraising and research gave final approval for the decision to accept or reject a donation.

4.7 This arrangement can be challenging for smaller entities, although we expect there to be sufficient scope for the end-to-end process not to be entirely entrusted to a single individual.

Case study

Segregation of duties in a small charity

In one small charity we visited there was close liaison between the development manager and the finance director on progress in securing large-value donations. Both individuals acknowledged their different responsibilities, but this close working gave the finance director the opportunity to raise matters with trustees or raise concerns directly with the development team before any commitment was made to accept a donation.

Initial risk assessment

4.8 Due diligence processes should be risk-based to ensure that disproportionate time is not spent assessing low-risk donations. A number of bodies set thresholds to determine the level of checks performed on potential donations of varying value. We noted that £10,000 was a common trigger for the introduction of increased due diligence checks in the sector. This amount is consistent with money-laundering regulations that are applied to the sale of goods and services.

4.9 Qualitative factors were also important criteria to determine the level of scrutiny of proposed donations, often prompting a higher degree of due diligence than their value might otherwise require. In the best examples we saw, teams were provided with a clear list of qualitative factors that would indicate a higher-risk case (in addition to considerations by value) and the necessary research process was clearly set out for donations with differing risk profiles.

Common factors which could indicate a higher-risk proposal

- A requirement to repay the donation (in substance a loan).
- A donation in an atypical foreign currency.
- A donation which requires unusual transfer arrangements for the funds to be received by the charity.
- A donation where very specific services need to be provided to secure the donation.
- A requirement to pass on the donation to a specific entity or use for a specific unusual purpose.
- The donor requests anonymity.
- Donations potentially create a relationship in perpetuity.
- Donations are sourced from countries with a problematic international status or regulatory environment.
- Donations are from bodies with which the charity has a significant pre-existing commercial relationship or which could result in financial gain for the donor.
- A donation which could impose a very restrictive course of action on the charity and compromise the independence and effectiveness of the board of trustees.

4.10 In the best-practice examples, the risk factors identified for potential donations were not only those which implied legal risk or issues with the provenance of the donation but also took into consideration whether the source implied any conflict of interest with the entity's charitable objectives.

Best-practice example – Tailored list of 'high risk' industries

Guidance for due diligence researchers typically included examples of sectors of industry which would generically create a high risk of conflict with the organisation's charitable objectives (such as tobacco manufacturers, the arms trade or adult entertainment industries). Potential donors and sponsors from these sectors were automatically classified as high risk (although not necessarily automatically prohibited).

The best examples also included evidence of a more tailored thought process. These drew attention to more specific risk areas such as bodies with an interest in the property market local to the charity or auction houses or other organisations with a potential vested interest in a museum or gallery's curatorial decisions.

Due diligence processes

4.11 Following the initial risk assessment, museums and galleries collate more detailed information to assess whether the possible donation should be accepted. This involved asking key questions about the potential donor, including:

- What business is the donor involved in and associated with? Does this include industries or sectors inconsistent with the charity's purpose?
- Has the donor received unfavourable media attention for their actions?
- Have they been or are they involved in litigation?
- What is the source of the donor's money? Is it legal and is there any risk that it does not exist or will not actually be available to the charity in the future?

4.12 A number of charities noted the difficulty of penetrating complex corporate structures to determine a potential donor's source of wealth and business relationships. Individuals tasked with making a decision based on the evidence gathered by the charity need to consider the completeness and quality of information they have been provided and whether it is sufficient to enable them to make a defensible decision.

4.13 A complicating factor for some charities was where there were unsubstantiated allegations about prospective donors. We recognise that there may be circumstances where allegations are of a nature that they should be taken into account in the decision-making process. This is particularly the case where the decision could have an impact on the perceptions of and relationships with the charity's key stakeholders.

4.14 The best due diligence procedures we saw balanced rigour with efficiency so that the viability of donations was not compromised as a result of unduly onerous requirements. Efficiency was built into the process by identifying and assessing the most critical factors first to increase the likelihood that issues of significance are identified early in the process.

4.15 Best-practice examples also built in efficiency through identification of 'safe' sources whose legitimacy could be reasonably assumed. This included bodies such as well-established charities regulated by the Charity Commission and public sector organisations.

Decision-making procedures

4.16 Robust initial risk assessment and due diligence procedures provide the foundations for informed decision-making. Senior staff are responsible for the approval of higher-risk donations and we support the practice of some charities of referring the highest-risk cases to the board of trustees for final approval. It is important that everyone within the charity understands who has the delegated authority to take decisions based on different circumstances.

4.17 Consistency of the evidence base and decision-making can be aided by due diligence checklists setting out expected steps and sources of evidence to be consulted for different types of donations. This helps provide clarity to individuals on what they need to do and enables a transparent and consistent trail of records to be kept for each decision that is made. This also gives the opportunity for the decision-maker to evidence their review of the underlying research.

Record-keeping and audit trails

4.18 One way of retaining institutional knowledge and enabling staff to learn from it is via documentation of due diligence activities. Best practice requires keeping records of past decisions to act as a source of guidance and an aid to the consistency of decision-making. It is helpful for staff making decisions on donor acceptability to be able to refer back to historic practice, in terms of sources of information used and judgements made. Otherwise learning and experience around due diligence and ethical matters will be overly reliant on key individuals, who may not always be available to the charity.

4.19 Audit trails also enable staff to demonstrate compliance with an organisation's policies and procedures to trustees, regulators and auditors. These can be particularly valuable in the case of a subsequent investigation.

4.20 We recognise the dilemma that organisations face in determining how much information to retain on individuals in their systems. Data protection legislation imposes significant penalties on organisations that do not handle the personal data they hold and control responsibly. A library of intelligence on the donor community can be beneficial, but it is essential that charities hold these in accordance with data protection legislation and recognise that individuals have a legitimate right to know what personal information is held about them.

External resources to support internal processes

4.21 Effective due diligence requires appropriate intelligence to support evidence-based decisions. Common search engines were often a starting point for museums and galleries but many research teams were aware of the risks that online profiles can be manipulated by individuals keen to manage their reputations. Organisations also need to establish whether the sources of data are compliant with data protection legislation. A charity using a non-compliant data source without conducting appropriate due diligence could be subject to enforcement action from the Information Commissioner. Other key sources and providers of information that were most commonly referred to by staff we spoke to were:

- publicly available sanctions lists, which include proscribed individuals and terrorist groups;[8,9]
- Companies House;
- The Electoral Register;
- Lexis Nexis;
- Mint UK;
- Iwave Pro;

8 HM Treasury, *Financial sanctions – Consolidated list of targets*, March 2017 (last update). Available at: www.gov.uk/government/publications/financial-sanctions-consolidated-list-of-targets
9 Home Office, *Proscribed terrorist groups or organisations*, December 2016 (last update). Available at: www.gov.uk/government/uploads/system/uploads/attachment_data/file/538297/20160715-Proscription-website-update.pdf

- Prospecting for Gold;
- World Check (provided by Thomson Reuters);
- Factiva (provided by Dow Jones); and
- Prospect Research UK forum – Yahoo Group open to all researchers in development and fundraising roles with the aim of sharing information.

4.22 Research staff we spoke to felt that there was no single source of reliable and comprehensive information so found that it was necessary to consult multiple sources. This was done to gather as complete a set of information as possible and to then corroborate that information.

4.23 In particularly challenging cases, some charities undertook more intrusive procedures, such as neighbourhood visits, to research the backgrounds of prospective donors. As this is inevitably an expensive option, it appeared to be very rarely used in the Department for Culture, Media & Sport (DCMS) sector, but may be a useful option if the potential benefits outweigh the costs. Where external third parties are used to gather research, this does not absolve the charity and its trustees from their ultimate responsibility for deciding whether or not to accept a donation.

Risk assessment – key messages

- Documented roles and procedures support a consistent, robust and evidence-based donations management process.
- Proper segregation of duties should be incorporated into processes to reduce the risk of bias, error or fraud.
- Risk assessment procedures should incorporate quantitative and qualitative risk factors tailored to a charity's circumstances and ethical policies, so that effort and attention is proportionate to the level of risk.
- Due diligence procedures should encompass a potential donor's reputation and associations along with the provenance and reliability of their funds.
- Decision-making procedures should be tailored, with more senior-level involvement for decisions on higher-risk donations.
- A range of external sources should be used where feasible to gather complete, reliable and corroborated information on a prospective donor.

Part Five

Staff and stakeholder management

5.1 More mature organisations provide ongoing learning and development opportunities for their staff, to facilitate knowledge-sharing on development issues across the broader cultural charities sector. They also recognise where the donations policy and due diligence procedures fit within the broader management of stakeholder relationships. Ideally, due diligence procedures are carried out at an early stage in order to establish whether an ongoing relationship is likely to be beneficial for both parties.

Training for staff and trustees

5.2 Museums and galleries need to ensure that staff with roles in the due diligence process receive adequate training and guidance on the charity's processes and also the legal aspects of fundraising. This includes briefing on key legislation such as the Bribery Act 2010 and Money-laundering Regulations 2007. A number of organisations we spoke to build this training into induction procedures for staff in relevant roles.

5.3 It is also important that anyone with a fundraising role on behalf of a charity, including development teams and trustees, is aware that the due diligence process can be time-consuming. Due diligence and ethical decision-making processes may be compromised if the procedures are expected to be completed unrealistically quickly. Those soliciting donations for the charity should notify research teams responsible for due diligence at the earliest opportunity. As a range of individuals can make first contact with a prospective donor (including executive managers, development team members or trustees), it is essential that the right people at all levels are fully briefed.

Sector networking

5.4 Staff we spoke to at museums and galleries in development roles have undertaken a range of networking and knowledge-sharing opportunities relevant to fundraising and due diligence. This included participation in:

- the Development Directors' Forum (run by the law firm Farrer & Co); and
- Institute of Fundraising special interest groups (including the group relating to fundraising in the culture sector).

5.5 We also saw evidence of knowledge-sharing with other sectors with an established fundraising function, such as the academic sector, and interaction with specialist groups such as the Council for the Advancement and Support of Education (CASE).

5.6 One museum that is planning to expand its development activities also noted the learning it had gained from other areas within the organisation that were already performing due diligence tasks. This included procurement teams, who are often required to perform due diligence reviews of potential suppliers. These teams may have knowledge and insights to share with development teams on approaches to conducting research.

Case study
Lottery Finance Directors' Forum

There is potential for more direct, formal networking within the Department for Culture, Media & Sport (DCMS) museums and galleries sector in the context of the increasing importance of development activities. We have attended meetings of the Finance Directors Forum for the Lottery Distributing Bodies. This group meets regularly and shares insight, best practice and sector developments. There may be scope for a similar forum for heads of museums and galleries development teams.

Written agreements with donors

5.7 A charity's risk management and due diligence procedures should not stop when the decision is made to accept a donation. The charities we spoke to stressed the importance of written agreements with significant donors, setting out the terms of acceptance and, where appropriate, how the funds would be used. Well-drafted agreements mitigate the risk that a donor could pressure an entity to carry out actions which are inconsistent with its charitable objectives. They should also allow the charity to withdraw from the relationship if the donor subsequently acts in a manner which is incongruous with the charity's objectives, harmful to its reputation or is inconsistent with the basis for the original decision to accept the donation.

5.8 Sound legal advice is beneficial in determining whether the terms and conditions of an agreement are appropriately drafted to afford the right level of protection to the charity. Securing this level of protection could, for example, require donors to disclose potential conflicts of interest as they arise.

5.9 Although donations are primarily a matter of philanthropy and are not exchange transactions, it is common for a form of benefit to be provided by the charity to the donor. We would expect these to be specified in the written agreement. Benefits could involve naming rights to an exhibition space or attendance at private events for major donors. In order that this is done fairly and consistently, a number of charities used a written benefits matrix which sets out what could be provided to the donor for different values of donation.

Periodic reviews of relationships

5.10 In the more mature arrangements we saw, teams recognised that, with any ongoing donor relationships, the intelligence used to underpin the original decision should be revisited periodically. These periodic reviews assessed whether circumstances had changed that would impact on the initial decision to accept an individual's donation. This is particularly important where the subsequent behaviours of donors mean that their association is no longer appropriate for the charity.

5.11 For those charities with larger development teams, ongoing checks can consist of a formal annual review of donor relationships. This could be limited to considering whether the charity has gathered any additional relevant intelligence (including from its trustees and their knowledge of the donor community).

Anonymous donors

5.12 There are occasions when charities are required to manage a relationship with an individual donor who wishes to remain anonymous. Typically, we would not expect the acceptance of a donation from an individual who remained anonymous in the strictest sense to be allowable under a donations policy, including when they are being represented by a named and known party. Appropriate levels of due diligence are highly challenging in this scenario.

5.13 However, we saw examples of best practice in the sector where the identity of the individual was restricted to a very small number of named key senior officials who have clear responsibilities under the approval process. In this way the entity can benefit from the donation while fundamentally preserving the individual's anonymity. In these circumstances, it is important that the charity's communications with the donor about the nature of the relationship are honest and unambiguous. The individual must be made aware that their anonymity cannot necessarily be given an absolute guarantee under Freedom of Information legislation.

People and donor relationships – key messages

- Appropriate training and guidance should be provided to staff with key due diligence roles and awareness of these processes shared with other staff and trustees.
- There may be opportunities for development staff to more formally liaise with their sector peers to share best practice and knowledge.
- Donor relationships need to be managed on an ongoing basis, starting with a written agreement and subject to periodic review for changing circumstances.

Appendix One

Museums and galleries sponsored by the Department for Culture, Media & Sport[10]

British Library

British Museum

Geffrye Museum

Horniman Public Museum and Public Park Trust

Imperial War Museum

National Gallery

Natural History Museum

National Museums and Galleries on Merseyside

National Portrait Gallery

Royal Armouries Museum

Royal Museums Greenwich

Science Museum Group

Sir John Soane's Museum

Tate

Victoria and Albert Museum

Wallace Collection

10 Thirteen of the 16 museums and galleries listed are exempt charities under section 3 of the Charities Act 2011, with the Department for Culture, Media & Sport their principal regulator rather than the Charity Commission. The exceptions are the Geffrye Museum, the Horniman Public Museum and the Sir John Soane's Museum.

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