

Governance & Disclosure Practices

Learning Series for Voluntary Organisations, Vol.-II, Issue - VIII, 2013-14

Risk Management in NPOs



A joint initiative of Credibility Alliance & Oxfam India

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* The Advisory support members have contributed to the document, however, the entire content is not necessarily the opinion of the advisory group.



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Risk Management in NPOs

Introduction

- 1.1.1** In the previous issue we discussed about crisis management. All crisis are related with certain amount risk, though it does not imply that if the risk is higher then the crisis would be severe. One may face a severe crisis where the risk is considered to be very low and contrarily a severe crisis where no risk was perceived.
- 1.1.2** A 'crisis' should be distinguished from a 'risk'. A 'risk' is a probability attached to the happening of a crisis or an event. A risk pertaining to a crisis may or may not be under the control of an organisation. For instance, a risk pertaining to a sudden legal change or withdrawal of a donor due to the change in policy of the country, are the types of risk which are difficult to anticipate and control.
- 1.1.3** The perception of risk may not be the most precise indicator of the impending crisis, however risk analysis always helps an organisation to minimize the possible threats to a great extent. A risk analysis, sometimes, can overlap with a crisis analysis because risk has to be analysed in relation to a future event which may or may not result in a crisis. Therefore, risk analysis is a much broader concept and it applies even to such cases which may not result in a crisis.
- 1.1.4** A crisis happens only rarely but risk analysis and management should be done on a continuous basis. For example, a person may purchase insurance policies against accidents and wear seat belts throughout his life, but may not face any accident in his/her entire life. Then the question may arise that the insurance and the precaution were totally wasted as there was no crisis. The risk was always there but the crisis never came.
- 1.1.5** Therefore, risk analysis is something which should inherently and concurrently be embedded in almost all activities, systems and events of an organisation. All

the issues pertaining to risk analysis cannot be generalised and will always remain organisation specific, however, in this issue we are discussing some broad issues and parameter pertaining to risk analysis.

Overall Objective of Risk Analysis

1.2.1 All NPOs should carefully analyse the purpose of risk analysis and what objective it may achieve in the organisation. Some of the assumptions vis-a-vis objectives are short listed as under :

- ◆ Unattended Risk may affect the efficiency and quality of the work and various input processes.
- ◆ Unattended Risk may affect the efficiency and quality of the work and various output processes.
- ◆ Unattended Risk may affect the safety of human resources.
- ◆ Unattended Risk may affect the safety of assets and other resources.
- ◆ Unattended Risk may affect the fund mobilisation and income of the NPO.
- ◆ Unattended Risk may affect the capacity to face catastrophic events.
- ◆ Unattended Risk may affect the capacity to face legal litigation against non compliances and other contingencies.

Legal Risk

1.3.1 All NPOs should carefully analyse the legal risk involved in their activities and interaction with stakeholders. An NPO may face various kinds of legal risk which may range from suspension to dissolution to heavy financial penalties. The Board members and Trustees of an NPO may also be subjected to various kinds of legal risk. Some of the important areas which may involve legal risk are discussed as under :

- ◆ **Legal Risk pertaining to the key documents** : An organisation should carefully study its key document including the Trust deed, Memorandum of Association, Articles of Association, Contract documents, Policy document etc. For instance the Trust deed or Memorandum of Association should empower the NPO to conduct various activity and take major policy decision. A small disabling clause in the Trust deed, Memorandum of Association may endanger the existence and the various licences of an NPO. A clause pertaining to commercial activity or power to invest may

be in violation of the law of the land. Similarly there could be various kinds of risk in the documents we make and use in our day to day functioning.

- ◆ **Legal Risk pertaining to Liability of the Organisation and the Board/Trustees :** An organisation should carefully study the legal risk, it may face in the shape of liability towards external stakeholders due to non compliance or non performance of various organisational responsibilities. Some issues pertaining to legal liabilities are discussed as under :
 - An organisation may face legal liabilities with regard to various staff and consultancy contracts. An organisation should understand the law of land and take proper legal advice in issuing contracts to staff and consultant.
 - An organisation may face legal liabilities with regard to various contracts signed. An organisation should understand the law of land and take proper legal advice before entering into any kind of contract.
 - The Board of Directors or the Trustees may also be subjected to criminal or civil liability if violation of the law is being made with a malafide intention. Contrary to the common belief the Board members or the Trustees may not enjoy immunity of limited liability if any deliberate or malafide action is noticed.
 - An organisation may suffer legal risk for the misconduct or any illegal act of any of its directors or senior member done in representative capacity. For instance, if there is violence in a formal protest or rally organised by an NPO, then the entire Board or the organisation may suffer even if the violation is made by 1 to 2 individuals.
- ◆ **Legal Risk pertaining to terror and money laundering :** An organisation should carefully study the sources and the credential of its funding and donors. Just like banks, which are subjected to KYC (Know Your Customer) norms, the NPOs are also subjected to KYD (Know Your Donor) norms effectively. An NPO may face criminal prosecution if it is found to have received funds from dubious, anonymous or prohibited sources, whether from within the country or abroad.
- ◆ **Legal Risk pertaining to non compliance of law :** An organisation should carefully comply with the requirement of all the statutes applicable to it. An NPO may face various kinds of legal risk ranging from financial liability to criminal liability to cancellation of registration.
- ◆ **Legal Risk pertaining to intellectual property, copyright, patent, trademark etc. :** An organisation should carefully understand the national and international laws pertaining to intellectual property, copyright, patent, trademark etc. It should ensure proper compliance in use of material/intangible assets

belonging to the NPO as well as others. Proper registration and approval should be taken wherever applicable. Some such issues are discussed as under :

- An organisation should ensure that the internet domain & email id's etc. are formally registered and any possibility of loss of right is prevented.
- An organisation should ensure that all its intellectual properties such as (i) books or research materials (ii) logos or trademarks (iii) videos and designs (iv) other development or scientific/social innovations etc. are registered with the appropriate authority.
- Any newsletter or dissemination material should also be properly approved and should be as per the law of the land.

Human Resource Risk

1.4.1 All NPOs should carefully analyse the issue pertaining to all the human resources involved. Apart from the legal risk which have been already discussed above, there are various other risk which may create crisis for an NPO. Some of such additional important areas which may involve human resource risk are discussed as under :

- ◆ An NPO should ensure that all the human resources right from the Board to the grassroots worker are adequate, competent and sustainable. An organisation is always under the threat of human resource turnover and the deficit of appropriate expertise required for each specific position.
- ◆ An NPO should ensure that all the staff are provided with a safe and fair environment to work. It should also ensure that promotions, appraisals, dispute resolution are being done in a very objective, independent and fair manner in order to avoid resentment and legal litigation.
- ◆ An NPO should ensure that all the human resources are provided with insurance and social security support as far as possible. It not only secures and satisfies the employees but also safeguard the organisation against any financial liability in case of a contingency.
- ◆ An NPO should ensure that all the termination and retirement policies are as per the law and transparent.
- ◆ An NPO should verify the credentials & antecedents of all the human resources right from the Board to the grassroots worker. It is also advisable to take a self declaration regarding the social, criminal and civil conduct of past.
- ◆ An NPO should verify the legal eligibility and authenticity of qualification and experience of all the human resources right from the Board to the

grassroot worker. For instance, in case of volunteer from overseas the appropriate visa to work in the country should be verified. In case of staff, a test check of qualifications should be made directly from the various universities or institutions.

Conflict of Interest Risk

1.5.1 There should be a clearly defined policy to ensure that any conflict of interest is properly dealt with. The conflict of interest transactions are most dangerous for an NPO and may create legal threat to its basic existence itself. Therefore, conflict of interest issues are not only ethical issues but may have a serious legal risk attached to them. Some of the transactions/decision which may be regarded as material interest are as under :

- ◆ Appointment of relatives in Board or senior management.
- ◆ Ownership or partial ownership in organisations which are engaged or may seek business or consultancies.
- ◆ Payment of fees and remuneration.
- ◆ Directorship or management position in other NPOs.
- ◆ Providing consultancies in personal capacities.
- ◆ Having commercial interest in any decision or resolution.
- ◆ Having direct or indirect relationship with the donor or donee organisations.
- ◆ When contracts are awarded to relatives of the Board members.

1.5.2 All NPO should check the law of the land regarding the permissibility of various conflict of interest transactions. For instance, in India, any kind of benefit provided to any Trustee or Board member may result in cancellation of registration under the Income Tax Act. The Board of Directors of the Trustees should declare such interests. The interested Trustees and Directors should not participate in the decision making and voting process for that particular resolution. An annual declaration of such interests should be placed in the annual general meeting.

Integrity and Corruption Risk

1.6.1 All NPOs are managed by human beings where all kinds of persons exist. We may find people with very high values and ethics, on the other hand there might be people who are prone to corruption and unethical practices. Therefore, all

organisations need strong systems to negate the possibility of unethical practices. Strong systems can only be built and sustained if there is a mechanism of identifying the various risk pertaining to human integrity and corruption. An NPO may take remedial measures against various risks, once they are properly identified. Certain common processes also may prevent corruption which sometimes look very innocuous. For instance, the possibility of a thief entering a house with hostile pet dogs is lesser than a house without any such protection. To take this example further sometimes just the sign “Beware of Dog” may deter a thief, even if a real dog is not present.

1.6.2 In other words, an organisation should identify the risk and establish tangible as well as subtle systems to negate any integrity loss or corruption. Some of the popular practices which go on to reduce the possibility of integrity loss or corruption are :

- ◆ Joint authorisation or joint signatory in processes.
- ◆ Multiple controls by different people.
- ◆ Use of banking channels for financial transactions.
- ◆ Rotation of senior staff responsibility.
- ◆ Rotation in the Board and leadership.
- ◆ Independence and effectiveness of Audit process etc.

Efficiency Risk

1.7.1 An NPO may be good but still not good enough. Loss in efficiency in various functions is one of the most dangerous risk attached in an organisation’s functioning. The efficiency risk generally goes unnoticed because of the lack of comparable standards of performance. In intellectual and intangible work, it is very difficult to quantify the quality and efficiency of the output. If NPOs don’t remain vigilant then organisational lethargies may set in.

1.7.2 Some large organisations conduct efficiency audits but it is more important to understand the larger principle of efficiency risk and look for organisation specific solutions.

Skills and Expertise Risk

1.8.1 An NPO may face the mismatch of skills and expertise required for the various human resources. All the system and infrastructure will be of no use, if

appropriately qualified/skilled persons are not available with the NPO. The Board of the NPO should analyse the adequacy of the existing skills & expertise and should also assess the risk attached in future regarding the loss of such skills and expertise due to staff turnover or changes in technology or external environment.

Communication and Articulation Risk

- 1.9.1** An NPO should also analyse the risk related with the communication and articulation systems. For instance, in India, any dissemination of public information or current affairs on the website or through print media may result in cancellation of registration under the Foreign Contribution Regulation Act, 2010. Similarly failure to disclose key information including conflict of interest also has considerable legal and other risk. Therefore, all NPOs should carefully study the various documents and reports they produce and analyse the risk, if any. Even the learning materials or the training modules should be carefully studied to ensure that they do not contain any objectionable or sensitive content.

Systems Risk

- 1.10.1** An NPO should also analyse and understand the functioning of all the existing systems. There could be risk pertaining to failure or inadequacy or performance of system. For instance, due to change in technology the existing systems may have to be replaced, which may involve sudden financial expenditure.
- 1.10.2** Integration and compatibility of various systems also is an area which needs to be carefully analysed for plugging any loophole or risk in it. For instance, integration of financial data from field level could be an area of risk.

Governance & Leadership Risk

- 1.11.1** The leadership and governance risk is another area which mostly goes unnoticed. An NPO may fall into the hands of a specific individual or a group of individuals, who may have conflict of interest attached to it. An independent risk analysis of the Board and the leadership processes is necessary to ascertain the quality of governance in an NPO. Even the NPOs which have dynamic leaders may face a

governance and leadership risk if they don't have a contingency plan for any unexpected event resulting in loss of key individuals. Further, undemocratic election processes may also pose considerable risk.

Values and Direction Risk

- 1.12.1** The another important risk in the functioning of an NPO is the possibility of deviating from the original mission and fall in the level of ethics and values. The organisation's Board should carefully analyse the risk involved in various activities which may affect the values and direction of the organisation. For instance, an NPO engaging itself in unrelated projects may lose sight of its own mission and become donor driven.
- 1.12.2** Similarly an NPO should also develop its organisation's culture and value through various practices. It should also study the various existing systems and processes and see the risk involved with regard to the values and mission.

Categorisation of Risk

- 1.13.1** An organisation should categorise the risk in the following categories which will help it in handling the various potential threats in a more informed and competent manner.
- ◆ **Risk which can be avoided** : The first category is the risk which can be avoided. For instance, the risk of financial loss through accident of a vehicle can be avoided by having an insurance policy. Or the risk of data loss can be avoided by having proper backup. The risk which can be avoided are required to be mitigated by taking the appropriate remedial measures.
 - ◆ **Risk which can be distributed** : The second category is the risk which cannot be avoided but can be spread or distributed. For instance, the risk of decrease in resources from a donor can not be avoided but can be handled by reducing the expenditure in a planned manner over various activities so that there is no serious implication on any specific individual or function. The risk which cannot be avoided but can be spread or distributed are required to be mitigated by taking the appropriate remedial measures in advance in a planned manner.
 - ◆ **Risk which can be minimised** : The third category is the risk which cannot be avoided but can be minimised. For instance the risk of failure in cataract operations or road accidents cannot be totally eliminated but with proper

precautions and safe practices such events can be minimised to a great extent. The risk which cannot be avoided but can be minimised are required to be mitigated by improving the quality and systems and also enhancing the efficiency level.

- ◆ **Risk which has to endured** : The fourth category is the risk which cannot be avoided and has to be endured. For instance the risk of under going a legal scrutiny by a government department viz. the Income Tax Department randomly selects organisations for thorough scrutiny of all books and records. In case of such risk the organisation should prepare itself for the eventuality as it cannot be avoided or minimised.
- ◆ **Risk which cannot be anticipated** : The fifth category is the risk which neither can be avoided nor can be anticipated. For instance :
 - The risk of sudden death of the Chief Functionary
 - The risk of sudden withdrawl of donor due to change in country policy
 - The risk of suspension of licences due to court cases

In case of such risk, the organisation should analyse and see whether it is totally dependent on certain persons or circumstances. Taking the above three instances :

- The risk of sudden death of the Chief Functionary can be mitigated by creating a capable pull of senior person.
- The risk of sudden withdrawl of donor due to change in country policy can be mitigated by making the NPO multi funded or diverse in nature.
- The risk of suspension of licences due to court cases can be mitigated by the NPO through strong legal due diligence of all the activity and processes and also by strictly following the law of the land.

About Credibility Alliance

Credibility Alliance (CA) is a consortium of Voluntary Organizations committed towards enhancing Accountability and Transparency in the Voluntary Sector through good Governance. Registered in May 2004 as an independent, not-for-profit Organization, CA emerged as an initiative from within the Sector after an extensive consultative process over a period of two years involving thousands of VOs all over India. As an Organization, CA aspires to build trust among all stakeholders through improving Governance within the Voluntary Sector. As an initiative whose hallmark has been the participatory approach, CA has developed suitable Norms through wide-ranging consultation with and participation of diverse Organizations within the Sector by developing a large membership base.

With the mission 'to build credibility of the Voluntary Sector through creation and promotion of Norms of Good Governance and Public Disclosure', CA's core programme areas comprise of: Accreditation, Capacity Building, Networking and Information Dissemination.

- I. **Accreditation:** Accreditation of Voluntary Organizations refers to the certification of upholding of the quality of an organization, which adheres to the minimum norms or desirable norms set by Credibility Alliance. The main purpose of the Accreditation exercise is to develop a cost effective mechanism of periodic evaluation of VOs in the country.

'Minimum Norms' are the Norms that all VOs should follow. It is mandatory for all the Accredited Members of CA to comply with the Minimum Norms or give an undertaking that they will do so within an year, whereas 'Desirable Norms' are the next level of Norms for good Governance and public disclosure. These are the practices that are at present not mandatory and some Organizations may require time to adopt such practices.

- II. **Capacity Building:** Credibility Alliance focuses on the Capacity Building process to maximize its potential and sustain its work by adopting the existing best practices. CA plans the Capacity Building initiatives for the Voluntary Organizations by identifying and outlining the gaps in the Sector, assessing the needs and finally instituting the programs to address those needs.
- III. **Networking:** Credibility Alliance facilitates interaction between experts in different areas and promotes the sharing of ideas and information between the Voluntary Organizations and the experts. CA helps VOs to seek issue-based information in the Sector that they are working in, which helps in building the professional capacities of VOs through training, thereby enabling them to increase institutional capacities.
- IV. **Information Dissemination:** Credibility Alliance sensitizes, spreads awareness, assists, educates and appraises on the recent developments, responsibilities and other critical issues pertaining to Voluntary Sector by disseminating vital information periodically to all VOs.



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