Fact Sheet: Risk Management for Community Foundations

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Risk comes from not knowing what you`re doing.

Risk is like fire: if controlled, it will help you; if uncontrolled, it will rise up and destroy you.

For community foundations, managing risk is critical to their success because in doing so the foundation will be in a better position to:

- manage reputation and goodwill, which is critical to public perception and success
- reduce exposure to legal and financial liability
- reduce exposure to regulatory fines and penalties
- undertake necessary 'duty of diligence' which is a fundamental role for directors of non-profit corporations
- understand that things can go wrong, and you need to find ways to reduce the impact

Risk management allows organizations to attempt to prepare for the unexpected by minimizing risks and extra costs before they happen. By implementing a risk management plan and considering the various potential risks or events before they occur, an organization can save money and protect their future.

Directors also need to understand their liability relating to risk. If risk is not managed well, their personal reputations could be impacted due to a financial scandal, which sadly we've heard too often about these in the news. Directors also face personal financial liability should payroll remittances or GST/HST remittances not be submitted when due. Should board decisions be made without due consideration of risk and impact on the foundation, there is the potential for lawsuits to be filed against both the organization as well as individual directors.

What can we do to protect ourselves?

- Understand, identify & manage risk,
- Implement strategies to mitigate risks (internal controls),

- Get the right people with the right skills,
- Create robust reporting systems,
- Document roles and responsibilities,
- Create and document policies and procedures and ensure they are followed.

What is risk?

Risk is the chance of something happening that will have an impact on the organization. It is measured in terms of consequences and likelihood. Risk management includes the culture, processes, and structures that are directed towards the effective management of potential opportunities and adverse effects. A risk management process includes the systematic application of management policies, procedures, and practices to the tasks of establishing the context, identifying, analyzing, assessing, managing, monitoring, and communicating risk.

Types of risk and mitigants

Compliance or legislative risk
Risk of fines and other penalties for failure to comply with federal, provincial, or municipal acts and regulations.

Mitigants
- human resource policies that are regularly reviewed for compliance **and** which are reviewed regularly by employees AND which are adhered to
- development of a compliance checklist to ensure annual regulatory reports are filed (signed off by board and staff)
- as part of annual audit, have auditor review accuracy of required content of donation receipts

Financial risk
Risk of fraud, financial failure, or decisions made on inadequate or inaccurate information, which specifically could include:
- running out of unrestricted cash
- occupational (employee) fraud/theft/embezzlement
- inappropriate gifts or income tax receipts
- grants to organizations that are not qualified donees
- not in compliance with donor fund agreements
- low investment returns
- CRA payroll assessment done incorrectly or filed inappropriately
- Losing charitable status

Mitigants

- financial checks and balances with respect to receiving money and paying invoices (i.e. at least two different people involved in each of these processes – Treasurer should not do the bookkeeping),
- ensure financial controls are functioning effectively and reviewed periodically to ensure they are accurate and comprehensive,
- link reserves to business plans; regularly review reserves policy,
- budgets include previous year's figures and notes on variances. Budgets reviewed by at least 2 people before presented to board for approval,
- ensure volunteer and staff have adequate skills base to produce and interpret budgetary and financial reports - consider engaging a volunteer professional accountant as your Treasurer; consider hiring a part-time controller and a bookkeeper with non-profit experience,
- consider providing financial training/orientation for your Board,
- adequate property and general liability insurance.

<u>Governance Risk</u>
Risk of ineffective oversight and poor decision-making

Mitigants

- fair and transparent board recruitment process that aligns skills needed to organization's strategic priorities
- board orientation process and on-going professional development
- regular bylaw review
- securing director's and officer's liability insurance (also covers volunteers)

<u>Strategic and Opportunity Lost Risk</u>
Risk of inappropriate or unrealistic programs and initiatives, the risk involved in not taking advantage of new opportunities and the failure to keep the organization strong and relevant

Mitigants

- a strategic plan that is regularly monitored, reported on and updated and/or revised
- keeping current on trends and opportunities impacting your organization's core business
- when new programs/initiatives are being introduced, board needs to ensure that they align with mission and strategic plan and understand risks involved and how risks will be mitigated

<u>Program or Operational Risk</u>
Risk of poor service delivery, day-to-day crises, and misuse or neglect of human capital, property and other resources.

Mitigants

- human resource policies for staff and volunteers
- structured staff, board and volunteer orientation and training programs
- capital asset maintenance and replacement plan
- clear communication policies and practices
- accessible customer/donor complaint's process
- get professional advice on terms and conditions of contracts
- regular program review and evaluation

<u>Reputation Risk</u>

Risk of losing goodwill status in the community, which impacts the ability to raise funds and attract prospective volunteers (i.e. protecting your brand), which could include:

- inappropriate asset use
- ineffective asset use
- reporting errors to clients/accountants/regulators

Mitigants

- develop risk management practices and policies
- when implementing or changing programs, board and senior staff need to ask the question 'what is the impact on our reputation?'
- develop a code of conduct policy and procedures for volunteers and staff

<u>Information Technology Risk</u>

Risk that the information technologies used in the organization may not be secure and provide dependable service and accurate information that is available when needed. Cybercrime is the top reported economic crime. It's critical to protect donor and employee data and to protect from phishing, which is the fraudulent practice of sending emails purporting to be from reputable companies in order to induce individuals to reveal personal information, such as passwords and credit card numbers.

Mitigants

- regularly update software to the latest versions, including anti-virus and anti-malware software
- use data backups that include off-site or remote storage – <u>**test the backups**</u>
- secure your passwords and use secured computers, servers and wireless networks
- consult with auditor and insurance provider to current best practices
- have an IT or Cybersecurity audit done by a 3rd party on a periodic basis

Climate Change Risk
Risk resulting from climate change effecting natural and human systems and regions. This is a relatively new risk category being factored into business operations.

Mitigants
- implement practices that reduce your organization's carbon footprint
- develop and promote policies and actions that use natural infrastructure to reduce risks associated with floods, storms and droughts
- message that investing in nature can provide cost-effective solutions for both climate change mitigation and adaptation

Process to Manage Risk

There is much literature available on assessing and development a risk management process. Whichever process your foundation uses, there are key questions that must be answered when reviewing risk. These include:
- What could happen that would affect our ability to meet our objectives?
- How likely is it to occur?
- How serious might it be?
- What should we do to reduce the risk?
- How can we be prepared to respond to problems?

When developing your process, you need to determine who is ultimately responsible within your foundation for identifying, assessing and managing risk. This is usually delegated to your senior staff member or, for smaller foundations, could be delegated to the Treasurer or Finance Committee. Regardless, it is critical that whoever is responsible for risk management should have this function included either in their job description or committee terms of reference.

Here is a simple three-step process that your foundation could considering implementing when looking at managing risk.

Step 1 Identify categories of risk most relevant to the work of the foundation based on the types of risk identified earlier in this document.

Step 2 Identify specific risks to your foundation's operations in each risk category

Step 3 Analyze the risk, the likelihood that it could occur and the impact on the organization

Step 4 Determine what your foundation is doing or can do to mitigate the risk

When developing risk mitigants consider these attributes:

- compatible with the foundation's values, objectives and risk tolerance
- realistic in balancing cost and protection
- supported by strong internal processes and reliable partners

The Cure for Risk: Indemnity or Insurance

(note: the following content is an excerpt from a document written by Maureen F. Forester, Vancouver – original content included in Volunteer Vancouver publication)

After you identify potential risks and set up a plan to reduce or prevent these risks, there still may be a sense that more protection is needed. Every organization must consider how it might pay for claims if they arise. In many cases, corporate funds are in adequate. The following are things to consider.

Many organizations indemnify (pay back) board members if they are sued. This means, the organization will cover the expenses that a director or officer incurs to defend an action, or the cost related to a settlement or a judgment of a claim. However, an agreement to indemnify a director is only as good as the financial resources available in an organization. In other words, indemnity may not be sufficient. Also, some statutes limit organizations from providing indemnity and an organization can decide not to indemnify an individual if the cost of litigation would push the organization into bankruptcy.

If you decide to purchase insurance, take the following into consideration.

Unfortunately, insurance policies are often written in language that is difficult to understand. Since an insurance policy is a contract between you and the insurer, it's important that you understand what is being said and your commitments. If you do not meet the obligations set out in the contract, this may affect whether or not you are covered. When looking at insurance, look for four main things:

A. Who is covered?

Ensure that directors, officers and volunteers are covered You may also want to include higher level management staff such as the chief executive officer. Policies will either describe "insured" narrowly or broadly. In some narrow definitions, coverage is limited to current directors and officers of the organization only. Broadly defined policies will include the organization, all past, present and future directors, employees, committee members and volunteers. It is important to name as many people and organizations as possible in the definition of insured. Most litigation

lawyers, when suing, will name all of these persons or organizations, regardless of who is ultimately responsible.

B. What is the definition of claim

Almost all director's and officers' liability insurance is made on a "claims made" basis. This means that insurance must be in place when a claim is made in order for it to be covered. In other words, it doesn't matter when the actual event occurred. For example, if an organization has an insurance policy that lasts for all of 2018 and the organization fired an employee in 2017, if the employee decides to sue the organization in 20188, that claim will be covered. This is not very good for directors since they can be held liable for lawsuits about events that occurred years earlier.

C. What is the definition of wrongful act

The definition of wrongful act is fairly important since most policies limit their coverage only to wrongful acts that result in a claim. Most policies define wrongful act in a long series of paragraphs usually speaking about such things as errors, mistakes, or omissions that occur in the discharge of an officer's or director's duties. Wrongful act also usually includes those "causally connected errors" that are also called inter-related wrongful acts. In most situations, wrongful act will not include criminal activities such as false arrest or such things as libel, slander, infringement of copyright or trademark.

It is important to read the exclusions part of the contract very carefully because some claims that are included in the initial part of a policy are excluded in this section.

D. Policy Limits and deductibles

One of the most obvious parts of a policy is the limit that can be claimed under the policy. Limits are usually described in the dollar amount allowed per claim and the dollar amount allowed annually. So, for example, a $1,000,000/$1,000,000 policy means that any number of claims can be brought in a year, but none can be greater than $1,000,000 and they cannot total more than $1,000,000 in a year.

Other policy limits are related to defense costs. Defense costs are either included within the policy limits or in addition to policy limits. They will either be paid as incurred or paid at the end of the litigation.

Deductibles are the amount of the loss that the insured must pay. In some cases, it must be paid up front when a claim is made. Many insurance policies charge different deductibles for

individuals and organizations. Some insurance companies will pay for the loss and then ask for repayment of the deductible later. In many cases, this clause or term is negotiable in the contract.

D & O Insurance - balancing costs against risk

Not-for-profit directors' and officers' liability insurance typically costs from $1,500 to $50,000 year. The costs are based on the organization's annual revenues and on a risk assessment by the insurer. For not-for-profit organizations, it is important to realize that this cost can be lessened if it is spread out among several organizations. Therefore, it is important to speak to other not-for-profit organizations and perhaps arrange for coverage which covers all of you.

The key question which every organization must ask itself is what is the probability that the board or senior staff will be sued? If it is very high, what is the likely reason and what loss prevention is currently being done? Weigh this risk against the cost of insurance and then decide what amount of insurance you need.

Some buying tips

- Solicit competitive bids every three to five years
- Allow sufficient time for a risk assessment by the insurer
- Locate an insurance advisor with expertise with not-for-profits
- Be extremely careful when filling out the application form (possibility of misstatements)
- Fully disclose the organization's prior losses and provide details on ways in which the organization can avoid future losses
- Negotiate for coverage and pricing
- Make sure that you report any prior incidences that might potentially give rise to a claim
- Ask each insurer to provide information on the insurance carriers' "financial strength"

Risk Management Checklist

The Risk Management Checklist that is included in this document was developed by the Niagara Community Foundation. Their Finance Committee is responsible for developing, implementing and monitoring the Risk Management Plan and Checklist. The Committee works closely with the Executive Director in this area, who annually prepares a report to the Committee, which is forwarded to the Board, reviewing each of the risk exposure areas, the adequacy of the quality of the risk management, determining if the mitigants are operating efficiently and if not, making recommendations for improvements including an implementation plan. The Finance Committee is tasked with ensuring the implementation of this plan.

For issues that arise during the year which are not addressed in this plan or are of a strategic nature, the Executive Director's report to the board includes reference to the issue including any risk to which the foundation could be exposed and a strategy to mitigate the risk.

Risk Exposure	**Risk Category**	**Applicable NCF mitigants to manage risk** **Board responsibility**	**Staff Responsibility**	**Quality of Risk Mgmt. (W – weak; A – adequate)**	**Operating Effectively (Y, N)**
Legislative & Legal	Financial Reputation	Bylaws regularly reviewed Bylaw changes approved by board Human Resource Policy Policy sign-off and review External auditor review Ensure no ineligible directors Ensuring T3010 filed Ensuring payroll remittances are current	Reporting and receipting practices T3010 filing Industry Canada filing Communication with CRA Remittance of payroll tax and GST Workplace safety inspections Monitoring changes in law Staff training and orientation program Minutes kept of all meetings Manage and monitor human resources within policy Ensure directors complete Directors' Eligibility Questionnaire annually		
Fiscal Performance and Financial Reporting	Financial Reputation Operational	Annual financial audits Review annual management letter Finance Committee oversight Investment Committee oversight Finance Policies Ensure adequate insurance coverage	Annual budget and operational plan Preparation of quarterly financial statements Preparation of annual report Annual review of insurance coverage Operating procedures documented		
Management of Volunteers	Reputation Operational Financial	Terms of reference Board orientation HR policies for volunteers	Screening process Reviewing terms of reference on regular basis Reference checks Sign-off on relevant policies		

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Donor Steward ship	Reputationa l Strategic Financial	Donor Rights Policy Privacy Policy Donor Recognition Policy	Appropriate policy implementation Preparation of annual fund statements		
Employ ee Relation s	Operational Financial Reputationa l Strategic	HR Policies Performance Evaluation (for ED)	Screening process Staff job descriptions and related operating procedures Reference checks Sign-off on relevant policies Develop and monitor annual work plans Performance Evaluation Professional development		
Strategi c & Econom ic Risk	Operational Financial Reputationa l Strategic	Strategic Plan Development Monitoring and evaluation of strategic plan Monitoring investment policy Monitoring community & economic trends ED Succession Plan Staff succession Plan	Annual business plan preparation and implementation Monthly investment reports Background research on community and relevant economic trends Knowledge transfer and training programs designed and implemented		
Informat ion Technol ogy	Operational Financial Reputationa l Strategic	Disaster Recovery Policy Human Resource Policy (refers to IT usage) Records Retention Policy	Appropriate policy implementation Records are backed up and key documents are scanned and stored off-site Testing backup on a regular basis Monitoring HR IT policy Disaster recovery plan reviewed annually		