

# Basic Risk Management

From the Nonprofit Risk Management Center - <http://nonprofitrisk.org/>

## 1) Why Risk Management?

**Risk management is a discipline for dealing with uncertainty.** Every nonprofit faces uncertainty and risk. Few, if any, nonprofits operate in risk-free environments. From uncertainty about continued funding, program outcomes and the organization's ability to ensure client safety, managing a range of risks is required for both survival and success. Every nonprofit — including small organizations — can use risk management strategies and tools to protect vital assets.

**The discipline of risk management helps identify, assess and control risks** that may be present in operations, service delivery, staffing, and governance activities.

It is well worth the time to integrate risk management into your operations and there are many good reasons to do so.

- **The threat of litigation is increasing.** Many nonprofits never face a lawsuit, but those that do know that it can be costly and time consuming. Good risk management can reduce these costs or perhaps help you to avoid a lawsuit altogether.
- **The risk of client harm.** Your mission is to help people, not hurt them. Causing harm to a client, however unintentional, undermines your purpose and jeopardizes your mission.
- **For your own safety and security.** Sound risk management will help create a sense of confidence and safety about your operation. In an atmosphere where the threat of unnecessary risk is reduced, a nonprofit can be more creative in providing services to clients and achieving results.

**Risk is** anything that threatens the ability of a nonprofit to accomplish its mission.

**Risk management is** a discipline that enables people and organizations to cope with uncertainty by taking steps to protect its vital assets and resources.

**The risk management process provides a framework for identifying risks and deciding what to do about them.** Of course, just making a laundry list of all possible risks is not enough. It is easy to quickly become overwhelmed by the huge list of risks the organization faces.

**Not all risks are created equal.** Risk management is not just about identifying risks; it is about learning to weigh various risks and making decisions about which risks deserve immediate attention. Risk management is not a task to be completed and shelved. It is a process that, once understood, should be integrated into all aspects of your organization's management.

Let's take a closer look at how this process works.

- **Establish the context** — It's important to begin a risk management program by setting goals and identifying any potential barriers or impediments to the implementation of the program. In the goal setting exercise, ask, "What are we trying to accomplish by integrating risk management into our operations?" Some common goals for nonprofit risk management efforts include: reducing injuries, avoiding costly

claims, preserving the nonprofit's reputation in the community, freeing up resources for mission-critical activities, and ensuring adequate risk financing.

- **Acknowledge and identify risks** — In this tutorial we will categorize risks according to four major categories of nonprofit assets: People, Property, Income and Goodwill. There are many ways to undertake risk identification; the key is using a framework or strategy that allows you to identify all major risks facing your nonprofit. By the end of this tutorial, you will have had the chance to identify the important risks to these critical assets.
- **Evaluate and prioritize risks** — The third step in the process helps you keep things in perspective and establish a list of action items in priority order. The risk of an asteroid crashing into your organization's annual Black Tie Event is remote, so it probably makes more sense to work on a more likely risk - that someone could slip and hurt themselves on a waxed dance floor.
- **Select appropriate risk management strategies and implement your plan** — We'll discuss four risk management techniques that can be used individually or in combination to address virtually every risk facing your nonprofit.
- **Monitor and update the risk management program** — nonprofits are dynamic organizations that constantly face new challenges and opportunities. Risk management techniques and plans should be reviewed periodically to make certain that they remain the most appropriate strategy given the organization's needs and circumstances.

## 2) Four Risk Management Techniques

Four basic risk management techniques are: avoidance, modification, retention, and sharing. Let's take a closer look at each.

**Avoidance** — Whenever an organization cannot offer a service while ensuring a high degree of safety, it should choose avoidance as a risk management technique. Do not offer programs that pose too great a risk. In some cases avoidance is the most appropriate technique because a nonprofit simply doesn't have the financial resources required to fund adequate training, supervision, equipment, or other safety measures. Always ask, "Is there something we could do to deliver this program/conduct this activity safely?" If you answer "yes," risk modification may be the more practical technique.

**Modification** — Modification is simply changing an activity to make it safer for all involved. Policies and procedures are examples of risk modification. An organization concerned about the risk of using unsafe drivers may add DMV record checks to its screening process, or an annual road test for all drivers. An organization concerned about the lack of male and female chaperones for an overnight camping trip may decide to host a day-long hike and picnic instead.

**Retention** — There are two ways to retain risk. The first is by design. A nonprofit may decide that other available techniques aren't suitable and it will therefore retain the risk of harm or loss. Nonprofits make conscious decisions to retain risk every day. For example, when a nonprofit purchases liability insurance and elects a \$1,000 deductible or self-insured retention, it is retaining risk. This can be a rational and appropriate approach to managing risk. Where organizations get into trouble is when risk is retained unintentionally. The unintentional retention of risk can be the result of failing to understand the exclusions of an insurance policy, insufficient understanding of the scope of risk an organization faces or simply because no one has taken the time to consider the risk and how it can be addressed.

**Sharing** — Risk sharing involves sharing risk with another organization through a contract. Two common examples are insurance contracts that require an insurer to pay for claims expenses and losses under certain

circumstances, and service contracts whereby a provider (such as a transportation service or caterer) agrees to perform a service and assume liability for potential harm occurring in the delivery of the service.

### 3) People and Goodwill

We are going to start our examination of risks with the asset categories of People and Goodwill.

**People are the heart and soul of your nonprofit.** They represent the talent, commitment, and community your organization serves. The people assets in your organization include staff, volunteers, clients, board members, and donors.

Each person is a unique individual with a unique set of skills. In a very real sense, each is irreplaceable. **Unlike damage to property or loss of income, injuries sustained by your people may never be fully repaired.**

**Not only are such losses very expensive, they are completely antithetical to all that your organization is trying to accomplish.** Nonprofits are in the business of helping people not hurting them. It is clear then, that people are our most precious assets. Exercise available for this concept – see last page.

**Goodwill is an asset that is difficult, if not impossible, to quantify.** For a nonprofit organization a more descriptive word might be "reputation." Every nonprofit understands that its reputation is key to fundraising, volunteer recruitment, staff retention, and overall good organizational health.

**Damage to a nonprofit's reputation can be devastating,** and many nonprofits with otherwise strong programs would have a hard time recovering from a "hit" to their reputation.

**In many cases, damage to reputation occurs in the wake of a crisis,** such as a scandal involving malfeasance or widely publicized client injury.

**In some cases there may be guilt by association** if a corporate or nonprofit partner comes under fire. Even an incident of tax evasion by a major donor could have repercussions for a nonprofit organization. Exercise available for this concept – see last page.

### 4) Property and Income

People may be your most precious resource, but that doesn't mean that your organization couldn't be devastated by a severe property loss. Imagine what you would do if your organization's computers and accounting records were lost in a fire or if a significant sum of money was embezzled. This section of the tutorial will address the risks of loss associated with your property and income assets.

**Property includes...** buildings, office furniture and fixtures, computers (hardware and software), intellectual property (trademark, logo, copyright, patent, etc.), motor vehicles, other equipment (lawn maintenance equipment, contractors equipment, A-V equipment, laptops, exhibits, etc.) It also includes cash and securities, financial assets and even property borrowed for special events.

**What are some possible property risks?** Property risks come in various forms, including those caused by nature (flood, earthquake, hurricane, forest fires, wind/tornadoes, extreme heat or cold) and others resulting from human intervention (fire, theft, vandalism, collision, carelessness).

Exercise available for this concept – see last page.

**Income** is like a spring of cool water that sustains life, nonprofits require a steady stream of reliable income in order to operate and grow. Common sources of income include donations, grants, government contracts, fees for services, investment income, merchandise sales, loans, proceeds from special events, sponsorship fees, registration/participation fees, membership dues and more.

**Most nonprofit managers have come face to face with an income risk**, such as the loss of grant funding, event proceeds falling shy of projections, contract cancellations and more. A disaster such as a fire or flood can also curtail operations resulting in an interruption of the income stream.

**Consequences of a loss can range from inconvenience to devastation.** While income ups and downs are arguably "par for the course" in the nonprofit world, it's possible to use risk management techniques to reduce the likelihood that a loss of income will destroy an organization.

**Some techniques for reducing income risk include** business interruption insurance, establishing a reserve fund, implementing sound financial controls, and diversifying income sources.

Exercise available for this concept – see last page.

## 5) Putting it all together...

**Once you complete the short exercises at the end of this paper, you will have developed a list of possible risks in four general categories:** People, Property, Income and Goodwill. The last exercise will help you to develop an action plan.

**The first step is to identify your priority risks.** Consider choosing the two most troubling or potentially costly or disrupting risks from each list identified previously. That will give you eight risks in total to focus on. Or choose the top five risks from the combined lists.

**Another approach is to form a task force or committee to review the risks** you've identified and choose priorities as a group. Using a committee is an excellent way to make sure you've covered the bases -- members of the committee may identify risks you missed. In addition, by involving a committee in the risk identification process and selection of priorities, you've taken an important first step in getting key players to buy into the process of risk management.

**Typically, a risk management committee would include key staff, volunteers, and perhaps an insurance professional** like your broker or agent. Your committee should be large enough to include a diversity of views but not so large as to be unwieldy.

Exercise available for this concept – see last page.

*Examples:*

**Priority Risk:** Theft or loss of our donor database

**Strategies:** Review current security strategies with our IT consultant. Increase frequency of tape back-ups to daily. Begin storing tape back-ups off-site immediately.

**Priority Risk:** Loss of income at annual fundraiser due to bad weather or natural disaster.

**Strategies:** Have a backup indoor location in case of rain. Purchase event cancellation insurance.

**Priority Risk:** Risk of injury to participants in recreational events

**Strategies:** Make sure that participants are physically fit. Require appropriate safety equipment for participants. Have emergency medical personnel on hand during event. Acquaint staff and volunteers with emergency procedures.

**Priority Risk:** Risk of embezzlement by volunteers selling tickets at the upcoming 5K run.

**Strategies:** Discuss cash controls and reconciliation procedures with our CPA. Order numbered tickets. Schedule periodic cash pick-ups throughout the day, rather than waiting until the end of the day

## 6) Your Risk Management Program

In the last exercise, you developed a list of priority risks and corresponding lists of strategies to manage those risks. If you've undertaken this effort alone, you've made a great start.

**The next step is to involve others in your efforts.** Remember that an effective risk management program can never be the responsibility of one individual. If you've already engaged a group, task force, or committee in identifying risks and strategies, you're well on your way to implementing a risk management program.

**Keep in mind that many effective strategies for managing risk in a nonprofit may not require any additional expenditures.** Instead, time, attention, and resolve may be all that's needed to increase the safety of vital assets. Give your team a deadline, a date by which you plan to have made significant progress in achieving your risk management goals. Review your progress frequently and set new goals as you achieve the existing ones.

As we have seen, **risk management need not be a complex and bewildering array of technical terms, actuarial tables, or probability statistics.** On the contrary, risk management is, in large part, the application of healthy doses of common sense and sound planning.

Remember that **the simpler the risk management strategy is, the more likely it is that it will be applied.** Yes, there may be items that are not considered in the first iteration of the plan, but at the outset it is more important that your program be comprehensible rather than comprehensive. As you continue to develop and refine your plan, what now seems new and strange will become second nature.

**As time passes, you plan should become more inclusive as you address more risks in order of their priority.** As we stated at the beginning of this tutorial, risk management is a process not a task, therefore

it is important to constantly review what you are doing, celebrate your triumphs, and analyze the reasons behind any setbacks.

We hope this tutorial has been helpful in providing an introduction to the discipline of risk management. **The Nonprofit Risk Management Center can provide additional assistance and support as you work to integrate risk management into the day-to-day operations of your nonprofit.**

## 7) Risk Management Exercises

### *People Asset Exercise:*

1. Identify the "people assets" in your organization.
2. List some of the risks to the people in your organization.

### *Goodwill Asset Exercise:*

1. Describe your nonprofit's reputation in your community (geographic and/or issue/specific).
2. Identify some of the risks to your organization's goodwill assets. What events or crises could shatter the reputation you've built over the years?

### *Property Asset Exercise:*

1. Describe your nonprofit's principal property assets.
2. Identify some of the risks to your property assets.

### *Income Asset Exercise:*

1. List the major categories of income for your nonprofit.
2. Identify the major risks to each income category. What could go wrong?

### *Putting It All Together Exercise:*

1. List the priority risks you've decided to focus on from the lists previously compiled, leaving several lines of space between priorities.
2. Below each risk, list some of the steps or actions your organization can take to minimize the likelihood of the risk materializing, or reduce its negative effect on the organization should the risk materialize.