NPC briefing, February 2013

Eleanor Bentley

On 4 February 2013, NPC and the Clothworkers’ Company held a seminar for trustees wanting to understand more about the risk environment charities currently face and what it means for trustees. Attendees explored why risk management is a crucial part of the trustee role, and learned from other charities’ experiences of managing risk. This report highlights the main themes discussed during the seminar, looking at the key risks for charities and how trustees can assess and mitigate them.

The seminar was chaired by Richard Atterbury, Chair of NPC. The panellists provided four perspectives on the importance of governance in planning for risk:

- **David Membrey** (Deputy Chief Executive, Charity Finance Group) spoke about five main issues that come up when he speaks to his members about risk, and encouraged attendees not to underestimate the risk of not taking an opportunity.

- **Phil Duffy** (Underwriting Consultant, Ecclesiastical) highlighted the need to understand legal liability, for staff as well as trustees, in case things do go wrong; and suggested practical tools to help with risk management.

- **Michele Acton** (Chief Executive, Fight for Sight and Trustee of St John’s Smith Square) argued that trustees are particularly valuable in identifying risks as they can draw on their professional experience and bring external insight.

- **Michael Chuter** (Director of Finance and Resources, National Children’s Bureau) and **David Rimington** (Treasurer, NCB) spoke about the importance of achieving mission as well as financial sustainability, and how the decentralised structure of NCB affects risk management.

**Introduction**

A recent NPC survey found that 90% of charities believe they face a riskier future now than they did at this time last year.¹ Changes to the landscape of the voluntary sector have direct relevance for trustees as, in 2000, it became a requirement for trustees to accept responsibility for risk management by stating in charity accounts that “...the major risks to which the charity is exposed, as identified by the trustees, have been reviewed and systems have been established to mitigate those risks.” Significant challenges include:

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• **Cuts to charity income.** More than a third of respondents to a survey conducted by NPC have experienced cuts to their statutory income in 2011/2012, and, for 12%, these cuts affect more than a fifth of their income.\(^2\)

• **Opening up of public services.** At the same time, new parts of the public sector are being opened up to competition from businesses, charities and social enterprises. This is creating new opportunities for charities to deliver public services. However, it is also increasing competition for contracts that some may have held for years.

• **New funding mechanisms.** Historically, simple block contracts and grants were the norm. However, more complex funding mechanisms are gaining currency, aiming to give better value for money and improve results for services users. As NPC’s survey shows, charities prefer block contracts and grants, and see many risks in the new funding mechanisms, including payment-by-results (PBR) and personal budgets.

• **Increasing numbers of partnerships and collaborations.** Faced by larger contracts and more competition, many charities are opting to enter into partnership with other organisations—including other charities, businesses and public sector organisations. Two main models have emerged: sub-contracting and consortia. These expose charities to the risks of their implementing partners and sub-contractors, over whom they may have little direct control.

> ‘Trustees have ultimate responsibility for assessing, managing and monitoring risk.’
> 
> Michele Acton, St John’s Smith Square

**Five key risks for charities:**

**Opportunity risk**

David Membrey, Charity Finance Group (CFG), emphasised that opportunity risk is not only about the risks related to taking on new projects (eg, financial, reputational); the risk of not doing something should also be borne in mind. He pointed to the newsworthy demise of both HMV and Jessops as warnings of what can happen to organisations that do not take action in a changing environment.

> The crucial point is to manage and understand the risks of a new opportunity, not to avoid it altogether, and to do so early on. As attendees identified in roundtable discussions, this could be achieved by linking it into strategic planning, to understand opportunities and their related risks with reference to where the charity is and where it wants to be.

> What might happen if you don’t change, don’t do something different? You might end up like Blockbuster!

**People risk**

Drawing on his experience with CFG members, David Membrey shared that trustees often struggle to get their heads around people risk, as it feels less tangible than other potential pitfalls. However, skills gaps—at board level and across the organisation as a whole—are a risk, and can be mitigated by ensuring that the organisation has identified the skills needed, noticed any gaps, and fed these findings into recruitment plans. Charities also need to plan for how they would deal with the loss of key staff at short notice, no matter how small the organisation.

\(^2\) ibid.
Risk of fraud

Charities face a risk of fraud, both external and internal. As far as internal fraud is concerned, it is essential that charities have strong systems in place to manage areas open to exploitation, such as petty cash and expenses. With respect to external fraud, charities are often seen as a soft target for scams, and while online fraud is commonly seen as a greater threat, particularly where online banking is concerned, charities need to be just as wary offline. The first step is to find out about the types of fraud: it is easier to control fraud risk if you know what to look for, and can understand your organisation’s particular vulnerabilities. Then, devise procedures to address these and train your staff so they are familiar with fraud risk and how to manage it.

As a problem, fraud is getting worse—it’s a cliché, but a fact.

David Membrey, CFG

Risk appetite

Trustees need to understand their own individual risk appetite, and how it compares to that of other board members and of the executive staff. These can differ, and while variation is often beneficial in ensuring a balanced perspective within the board and between the board and executive staff, it can also cause tensions. It is important to be open about these differences—transparency here provides an important context for decision-making and helps staff to gauge how decisions and opportunities will be received—and to agree a collective appetite for risk as a board.

We also need to recognise that this appetite is not fixed, and will vary even if the board’s composition remains the same. Attitudes to risk will vary over time and in response to the prevailing environment. In the current funding environment, for example, when many charities are struggling to sustain services and financial stability, trustees may feel more risk averse.

Charities are by nature risky things… We mustn’t forget what charities were set up to do—things that other people didn’t want to do.

David Membrey, CFG

Embedding risk

Risk management needs to be linked to everything an organisation does: to its financial strategy, its project action plans, and even to individual staff objectives. However, as trustees pointed out during the discussions, while risk management should be embedded, it should not become too regimented in case organisations miss new and unpredictable risks because they fall outside their past experience. To prevent this, the panellists recommended including all front-line staff in risk management and leveraging the trustees’ external experience, helping to incorporate a broad range of perspectives. Trustees also need to ensure that the organisational culture permits staff to raise risks without fearing that a project will necessarily be cancelled.

Remember the unknown unknowns: the biggest risk may turn out not to have been on the risk register.

Michele Acton, St John’s Smith Square
Case studies from our speakers

The view from a Trustee and Chief Executive

Michele Acton, Trustee of St John’s Smith Square and Chief Executive of Fight for Sight, felt that risk management is an essential part of good decision-making. It helps to ensure that a charity has an informed and timely strategy, maximises impact and avoids reputational and financial damage. Board involvement is particularly important, given the trustees’ legal responsibility for the charity’s performance and their role in scrutinising and challenging executive staff decisions. For Michele, risk management is a key area in which trustees can add value by drawing on their external experience from their professional lives.

She shared the risk management framework used in the organisations with which she is involved, using specific examples from her time as a trustee to illustrate the role the board plays:

1. Identify different types of risk and rate their probability and their impact.
2. Devise strategies to reduce this risk, both in likelihood and in impact.
3. Consider the retained risk after management—is it acceptable?
4. Monitor the risk on an ongoing basis and re-assess periodically whether further measures need to be taken.

The view from a charity supporting children and young people

David Rimington, Treasurer at NCB, emphasised that being a trustee is not just about financial sustainability, but about ensuring that funds are used to achieve organisational mission. He spoke about the two main risks he sees there: failure to effectively achieve its mission, and financial loss. NCB finds it difficult to measure its progress, as much of its work is in improving policy and practice, and has found the current government to be more willing to support frontline organisations. As a result, NCB has had to take more of a commercial focus in the current funding environment.

David also spoke about the personal challenges he faced in transferring his financial background to the charity sector, as differences in the accounts and the way they are reported can be confusing at first. The lumpy nature of charity income makes it more difficult to assess financial performance on a month-to-month basis, while annual accounts do not necessarily show how effective an organisation is in achieving its mission. His key thoughts on managing risk were to ensure that management and leadership are strong, and to insist on clear strategic planning, detailed business planning and budgeting, and regular progress reports on all of these to the board.

Michael Chuter, NCB’s Director of Finance and Resources, explained how its structure affects its risk profile. NCB is composed of many smaller organisations, making it legally responsible for organisations over which it may have only loose control. Its area of work means that reputational risk is a high priority. Individual projects can also have variable risk impacts for the different organisational tiers: the risks relating to certain projects may be large for members but small for NCB as a whole, while for others, the opposite may be true.

Michael explained that, at NCB, risk is assessed under three primary headings: corporate, which are risks that any organisation must manage; reputational, focusing on those specific to organisations working in the field of vulnerability; and proportionate risks, relative to the size of the activity. These are monitored regularly by both SMT and trustees, and crucially, each identified risk is ‘owned’ by an individual responsible for its oversight. To prevent information overload, NCB uses a scoring system to ‘filter’ risk management up the organisational hierarchy, with minor areas of concern managed at project level and more significant risks reviewed by trustees.

Risk management is not risk avoidance.

David Rimington & Michael Chuter, NCB
Discussions with our attendees

How can you assess opportunity risks?

It is important to look at opportunity risks early on, ideally during strategic planning, as knowing where you are and where you want to go will help to identify which opportunities should not be missed. Many trustees felt that they did not look at opportunity risk enough in their organisations, particularly the risk of not doing something.

At the same time, our attendees argued that staff and trustees need to feel able to refuse new opportunities, despite the sense of anxiety created by the current funding climate. This is especially important given the shift away from grants towards contracts and payment-by-results and the greater financial risk these types of opportunity create.

How to manage people risks—tips from our attendees:

• Bear the skills mix in mind when recruiting new staff.
• Remember the risks of people staying too long, as well as not long enough, when considering retention.
• Maintain robust systems for managing and monitoring staff—permanent and voluntary, part-time and full-time—to ensure that information is being shared within the organisation.
• Ensure that contracts have enough flexibility to permit restructuring where needed.
• Always plan for succession: it is important however small the organisation, and not just for senior staff.

How can you plan for the risk of fraud?

Trustees proposed a six-step plan to mitigate fraud risk for charities:

1. Identify your organisation’s vulnerabilities.
2. Tap into received wisdom within the governing body by consulting the relevant sub-committees (eg, finance, audit).
3. Devise organisational procedures to assess risk. It is important that these are proportional to the charity’s size—a large, complex organisation will need a sophisticated risk management process, but this may not be appropriate for a small charity.
4. Use these processes to assess and manage risk.
5. Engage all staff in the process, as this will help them to be aware of organisational vulnerabilities and incorporate their front-line experience into risk planning.
6. Conduct spot checks to ensure that risk management procedures are being used.

How do you assess appetite for risk?

Risk appetite is similar to the skills mix, in terms of the value of having a representative board, but it can be difficult to measure attitudes towards certain types of risk. For example, the preferred level of reserves may offer an insight into attitudes to financial risk, but in other areas (eg, attitudes to reputational risk) it may be harder to summarise and quantify. Trustees proposed a ‘traffic light’ system as one solution, and suggested including an exercise on risk during inductions to help trustees understand their own appetite for risk and how it compares to other board members. Managing differences of opinion on risk appetite is like managing any other conflict, and it needs to be collectively agreed.
How do you ensure that risk management is embedded within your organisation?

Suggestions from our attendees:

- Use the risk register regularly—not just once a year, and not just to keep auditors happy.
- Involve staff across the organisation in risk management processes. Incorporating risk planning into away days is one way to do this.
- Incorporate risk assessment into strategic planning. For example, devise different strategic opportunities with different risks, and choose those that match the organisation’s risk appetite.

How can you manage reputational risk?

When assessing reputational risk, it is important to remember your internal audience, and how staff relate to the organisation, as well as your external audience. Consider both aspects when planning for reputational risk, and have an organisation-wide strategy in place for how to respond to reputational damage.

The rise of social media and 24-hour news has made reputation an increasing concern for some charities: bad coverage spreads much faster, and it can be difficult to move on when information is cached and easily accessible through a quick web search. Given this, it is essential to collaborate with your communications team on how to manage and respond to reputational risk. It should be incorporated into your charity’s communications strategy and, where projects are high-profile or especially risky (for example, projects working with vulnerable children), in the communication plans for individual projects too.

Final thought

*The trustees’ role is not to eliminate risk: sometimes the biggest risk is not taking a risk.*

Michele Acton, St John’s Smith Square
Tips for trustees

Trustees have a critical role to play in ensuring their charity is identifying and managing its risks effectively.

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<tr>
<th>Tips for charities</th>
<th>Questions trustees could ask</th>
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<tbody>
<tr>
<td>‘Understand your liability in law.’ (Phil Duffy, Ecclesiastical)</td>
<td>• What legal structure does my organisation have, and what does this mean for liability?</td>
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<td>Check:</td>
<td>• Do all trustees, staff and volunteers understand the organisation’s corporate liability and their own personal liability?</td>
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<td>• the charity’s governing documents;</td>
<td>• How can we ensure this knowledge is embedded throughout our organisation? Eg, can we include it in job descriptions, training, targets?</td>
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<td>• Charity Commission guidance;</td>
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<td>• local and national government regulations; and</td>
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<td>• EU regulation.</td>
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<td>‘Remember the unknown unknowns: the biggest risk may turn out not to have been on the risk register, so keep assessing and monitoring.’ (Michele Acton, St John’s Smith Square)</td>
<td>• Have we considered future events as well as risks we’ve faced in the past?</td>
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<td>• Do we need to meet without risk registers occasionally to help us think beyond risks we have already identified?</td>
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<td>‘Use the tools available to you:’ (Phil Duffy, Ecclesiastical)</td>
<td>• Are we getting all the information we need to understand the risks we face?</td>
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<td>• Undertake regular health and safety assessments.</td>
<td>• What additional information do we need, and how can we get it?</td>
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<td>Conduct basic checks on a frequent basis as well as scheduled, thorough assessments.</td>
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<td>• Keep accurate records, as these are essential if a claim is made against you.</td>
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<td>• If an incident occurs, this is the time to begin insurance procedures, don’t wait until a claim is made.</td>
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<td>‘It’s important to agree the risk appetite among the trustee body.’ (David Membrey, CFG)</td>
<td>• What is my personal appetite for risk?</td>
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<td>• How does it differ from that of other trustees, and of the executive staff?</td>
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<td>• Has it changed?</td>
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<td>• Is it appropriate in the current environment?</td>
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<td>‘Consider seeking guidance from an insurer that is a charity specialist.’ (Phil Duffy, Ecclesiastical)</td>
<td>• Do our third party contractors have adequate insurance?</td>
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<td>• Do we have professional indemnity insurance?</td>
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<td>• Will my charity meet my liability as a trustee, or do I need personal insurance?</td>
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<td>‘All charities should be managing risk, whatever their size.’ (David Membrey, CFG)</td>
<td>• Who is responsible?</td>
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<td>• Is our system appropriate for an organisation of our size?</td>
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