Strategic Planning, Risk and Oversight for Not-for-Profit Organizations

Beth Deazeley
CMA Ontario
Deryck Williams
Grant Thornton LLP
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Agenda

• Strategic Planning for Not-for-Profits
  – role of the board in developing & approving strategy and plans
• Operational & Capital Planning
  – aligning the resources
• Board Oversight of Risk
  – oversight of strategic & enterprise risk
• Monitoring and Learning
Not-for-Profit Organizations (NPO's) may be:

- unincorporated,
- federally or provincially incorporated under a variety of statutes or
- may be trusts
NPO's may be segmented into:

- the largest subset, charities,
- and all other NPO's
- social enterprises occur in both – they are still evolving
Role of the Board in an NPO

Why the Board is so important:
• the "third sector" (after business & government) contributes 8% of Canadian GDP
• 13 million Canadians volunteer in NPO's
• 2 million are employed by NPO's
• thriving business + sound government + healthy third sector = a great place to live

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Types of Charities

- 86,000 registered in Canada
  - religious organizations
  - public & international charities
  - private foundations
  - public foundations
  - arts organizations
  - universities
  - hospitals
Types of NPO's

- > 100,000 in Canada
  - member & professional associations
  - amateur sport organizations
  - private clubs, certain private schools
  - youth, benevolent programs
  - non-profit housing, lobby groups
  - certain gov't funded public service organizations
## Risk Characteristics of NPO's

<table>
<thead>
<tr>
<th>Size</th>
<th>Board</th>
<th>Risk Considerations</th>
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<tbody>
<tr>
<td>Small, limited or no</td>
<td>volunteers fulfill both board and management roles</td>
<td>lack of segregation of duties, informal risk assessment, difficult accountability</td>
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<td></td>
<td></td>
<td>structure, poor decision documentation</td>
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<tr>
<td>Medium, a few staff</td>
<td>operations managed by an E.D. Board involved in operational decisions</td>
<td>board/mgmt conflict over roles, informal risk assessment, segregation of duties</td>
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<td></td>
<td></td>
<td>weak, insufficient board skills</td>
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<td>Large, expert management</td>
<td>board is policy &amp; strategy, management fully responsible</td>
<td>Longer time cycle for decisions, board controlled by staff, good segregation of</td>
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<tr>
<td></td>
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<td>duties and risk assessment</td>
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Developing NPO Strategy

- **Small NPO:** strategy done by the board, is often limited to non-existent
- **Medium NPO:** done by board and executive director, often disconnected to operations
- **Large NPO:** facilitated, in-depth analysis completed by staff, may not connect to operations
Best Practices in Developing Strategy in Charities

• Charities:
  – are created because an urgent and important need is not being adequately addressed
  – core purpose is to make change happen

"Theory of Change" (TOC) is the best practice strategy development logic model
What is a Theory of Change

• How we think change will happen
  – eg Bill & Melinda Gates Foundation
  – Theory of Change: homelessness in Washington State could be solved by creating more transitional housing

HOMELESS  THEORY OF CHANGE  HOUSED
A Theory of Change

- Gates Foundation TOC to end homelessness:
  - efficiently built 1,400 new transitional homes
  - measured homelessness before and after
  - outcome was increased homelessness!
The Theory of Change

Study, measure and test causal links:

**Problem Statement** - what problem do we want to address?*

**Program Goal(s)** - what changes are we hoping to create?

<table>
<thead>
<tr>
<th>Inputs</th>
<th>Activities</th>
<th>Outputs</th>
<th>Outcomes</th>
<th>Impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Funding - Staffing - Resources</td>
<td>- Programs &amp; processes</td>
<td>- Direct results - Products - Quantities</td>
<td>- End-user changes in behaviour</td>
<td>- Changes in community, society</td>
</tr>
</tbody>
</table>

Work backwards from goals to intermediate outcomes clarifying logic & assumptions

*based on B. Slater, Schulich School of Business

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A Theory of Change

• Gates Foundation developed a much deeper TOC:
  • “Ending family homelessness required a systematic coordinated approach to help a broad range of support systems and housing providers work together in mutually reinforcing ways”

(Read more at www.gatesfoundation.org)
Best Practices in Developing Strategy in Charities

• elucidate purpose through a clear, measurable, theory of change
  – organize inputs & activities to result in outcomes and impacts that achieve the changes
  – test and refine the logic chain
  – communicate the strategy, logic chain, outcomes and impacts
  – do not confuse outputs & outcomes
Best Practice Strategy in Charities

• characteristics of charities with a strong TOC:

  – recognition of a continuum of change and their place on it
  – partnering with other organizations across the continuum
  – continual research/learning: in measurement; in what other organizations are doing; in academic progress; in solutions
Best Practices in Developing Strategy in NPO's

- NPO's:
  - usually have a clearly defined membership
  - are originally created for a specific purpose but often evolve to include others
  - frequently experience disagreement within membership over "change"
  - often have disagreement on measures
Best Practices in Developing Strategy in NPO's

• a best practice model is Balanced Scorecard, adapted for NPO's
  – literature and experience is extensive (Kaplan & Norton, 1996) (Niven, 2006)
  – not a fad, here to stay
Why is BSC so Effective

1. "Chunking":
   - information can be best processed and maintained in memory when divided into meaningful subsets
   - Scorecards typically contain 4 categories of up to 4 to 7 measures
   - presented on a single page, we can grasp the information
   - it is a brilliant communication tool
Why is BSC so Effective

2. Non-Financial Measures:
   – NPO's imperatively understand their status through non-financial measures
   – yet their highest quality, detailed and consistent information is financial
   – by definition, BSC provides a means of "balancing" important financial and non-financial measures
Why is BSC so Effective

3. Broad Balancing of Measures:
   – can balance short and long term measures
   – balance competing concerns – eg. new vs old members, member needs vs employee morale etc.
   – balance hindsight measures with future focused measures
   – accommodates RISK measures
Why is BSC so Effective

3. Linkages:
   - can link vision/mission to objectives, measures, targets and initiatives
   - forces clear specification of strategic objectives
   - helps managers understand critical success factors and develop key performance indicators and value drivers
When Does BSC Fail

- the mission/vision and objectives may be poor
- measures may be too difficult to develop or deliver
- targets may keep changing
- organization is large & complex
- implementation is shallow: a "dashboard" is not a BSC
Recap: Role of the Board in Developing Strategy

• the board approves all strategy, and the methodology for its development
  – in small organizations, it will "do it all"
  – in medium organizations, the Executive Director will partner with the Board
  – in large organizations there should be a facilitator, and heavy staff support – but the Board remains responsible
Mechanics of Strategy Development

1. a retreat, in which the group completes a SWOT analysis, (strengths, weaknesses, opportunities, threats)

2. *then*, start the Scorecard or Theory of Change
   – first time with BSC or TOC will require a *second* retreat, after investigation and preparation, in order to prepare first Scorecard or TOC logic model
Mechanics of Strategy Development

- *the most common problem with strategy documents, is lack of connection to execution*
- the two models (BSC & TOC) provide a means of systematically ensuring strategy is executed
- consequently the "extra" step (first time) of a second retreat is critical
Role of the Board in Approving Plans & Budgets

with strategy clarified into Scorecard objectives for an NPO, or into TOC inputs, activities and outcomes for a Charity, management now has clear direction
Alignment of Strategy with Plans & Budgets

- alignment is achieved by using BSC or TOC to establish short and long-term strategic targets that represent the desired objectives or outcomes
- the targets are expressed as measures
- the operational and capital plans are activities designed to achieve the targets
Role of the Board in Approving Plans & Budgets

- plans are developed by management to achieve the approved objectives or outcomes, each of which is measured
- the purpose of board due diligence is to assess the quality of the plans in meeting the objectives and outcomes
Role of the Board in Approving Plans & Budgets

- budgets, both capital and operating, are driven from the plans
- the purpose of board due diligence is to assess the quality of the budgets in supporting the planned objectives and outcomes
Questions to Ask When Reviewing Budgets

- Is the budget aligned with the strategic plan?
  Expenses:
  - Have sufficient resources been allocated to support key objectives?
  - Are the majority of resources directed towards core activities v. non-core or project activities?
Questions to Ask When Reviewing Budgets

• Is the budget aligned with the strategic plan:
  Revenues:
  – How stable are the funding sources supporting key objectives?
  – Are there restrictions on how revenues are used?
  – Do revenues provide core funding in addition to project funding?
Questions to Ask When Reviewing Budgets

- How much risk is inherent in the budget?
  - What is the intended outcome (break-even / surplus / deficit)
  - What assumptions were used?
  - How conservative is the budget?
  - How stable are major funding sources?
  - How efficient is the organization (admin & fundraising costs)?
Questions to Ask When Reviewing Budgets

• How much risk is inherent in the budget?
  – How much of a financial ‘cushion’ do we have?
  – Does the budget support long term financial health as well as short-term objectives?
Timing of Budgets

• When should budgets be prepared?
  – Following or in conjunction with the operational plan
  – Before the fiscal period in question

• When (if ever) should budgets be revisited?
  – Revised budget v. mid-year forecast
Board Oversight of Risk

• Risk Management v. Risk Oversight
  – role of the board may vary with the size, complexity & resources of the organization
  – directors should be able to satisfy themselves that effective risk management processes are in place and functioning properly
  – board is directly responsible for strategic & leadership risk
Framework for Board Oversight of Risk*

1) Establish context
   • Understand current conditions in which the organization operates

2) Identify risks
   • Document material threats to the organization’s achievement of its objectives

*Framework for Board Oversight of Enterprise Risk, J. Caldwell, CPA Canada
Framework for Board Oversight of Risk

3) Analyze consequences
   • Quantify the impact of the risk and likelihood of occurrence

4) Analyze interconnectivities and compounding effects
   • Aggregate risks and understand relationships, interdependencies, and the compounding effect of simultaneous occurrences
5) Re-analyze consequences
   • Re-calibrate and, if possible, create probability distributions of outcomes of interrelated risks

6) Prioritize
   • Rank risks in order of importance, blending severity with likelihood of occurrence and potential for mitigation
Framework for Board Oversight of Risk

7) Assess Risk Capacity, Tolerance and Risk Appetite
   • Determine the entity’s capability, tolerance and appetite for potential consequences of risk

8) Choose Response Strategy
   • Develop plans to avoid, reduce or control, share or insure, accept, or exploit risks
9) Monitor

- Continually measure and monitor the risk environment and the performance of the risk management strategies
Risk Identification

Some key risk areas:

- **compliance**: Non-compliance with laws and regulations
- **reputational**: may include social media, privacy, litigation
- **information technology**: Data availability, data security
- **financial**: Liquidity, capital availability, investment, theft
Risk Identification

- **external**: economic conditions, structural change, competition, natural disasters
- **governance**: failure to have an appropriate governance structure or skills
- **operational and program**: Service quality, capacity constraints
- **strategic**: failure to implement strategy, ineffective or no strategy
## Analyze Consequences & Connectivity

<table>
<thead>
<tr>
<th>Risk</th>
<th>Likelihood</th>
<th>Impact</th>
<th>Interconnectivity</th>
<th>Clockspeed</th>
<th>Overall risk</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low investment returns</td>
<td>Moderate</td>
<td>High</td>
<td>Low</td>
<td>Moderate</td>
<td>Moderate</td>
</tr>
<tr>
<td>Injuries to participants in sports programs</td>
<td>High</td>
<td>Moderate</td>
<td>Low</td>
<td>Low</td>
<td>Moderate</td>
</tr>
<tr>
<td>Abuse of vulnerable individuals by staff and volunteers</td>
<td>Moderate</td>
<td>High</td>
<td>High</td>
<td>High</td>
<td>High</td>
</tr>
<tr>
<td>Loss of information systems and information</td>
<td>Moderate</td>
<td>High</td>
<td>High</td>
<td>Moderate</td>
<td>Moderate</td>
</tr>
</tbody>
</table>

Chartered Accountants of Canada, 20 Questions Directors of Not-For-Profit Organizations Should Ask About Risk
Risk Capacity / Appetite / Tolerance /

• **risk capacity:** the amount of risk that an entity is able to support in pursuit of its mission

• **risk appetite:** the desired level of risk that an entity is willing to take in pursuit of its mission*

• **risk tolerance:** the acceptable variation in outcomes related to specific performance measures linked to objectives the entity seeks to achieve*

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*Committee of Sponsoring Organizations of the Treadway Commission: Strengthening Enterprise Risk Management for Strategic Advantage*
Response

- **Avoidance** — Avoiding undertakings that could result in a risk occurring
- **Transference** — Sharing the risk with someone else (e.g., insurance)
- **Mitigation** — Policies and procedures to reduce the likelihood and/or severity of risks to an acceptable level
- **Acceptance** — Accepting or simply monitoring the risk
Questions to Ask about Risk Oversight

- Board engagement & knowledge:
  - Is the board sufficiently engaged in oversight of key risks?
  - Do directors have sufficient understanding of the organization & its immediate environment to assess key risks?
  - Does the board have sufficient information about ‘bigger picture’ issues to identify risks?
Questions to Ask about Risk Oversight

Risk and Strategy:

• Does the board understand and discuss the linkages between strategy and risk?
• Does the board assess strategic plans in terms of their potential failure and the attendant consequences?
• Does the board integrate assessment of risk and choices about risk into strategic plans?
Monitoring and Learning

- *how does the Board monitor results and learn?*
- it follows the 7 habits of a best practice board
Seven Habits of a Best Practice Board

1. It concentrates on what is crucial to its success
2. Focus is on measurable results within defined timetables
3. Engages in regular monitoring on how operations are conducted
4. Challenges for efficient use of resources
Seven Habits of a Best Practice Board

5. Decision making is transparent
6. Provides excellent accounting to stakeholders
7. Has crystal clear role/responsibility/accountability definitions between board and staff/volunteers
1. Concentrates On What Is Crucial To Success

- through an aligned strategic planning process and model, each Board member can explain the measures that are crucial to success
- a best practice board ensures that a BSC or TOC or similar logic model is completed and deployed
- the "measures" are the key performance indicators, indicating the status of critical success factors
1. Concentrates On What Is Crucial To Success

- risk assessment has a special prominence in the board's role
- the BSC or TOC logic models will identify key risks
- consequently risk measures are an integral part of the operational and capital planning
- this can solve the problem of risk assessment disconnected from operations
2. Focus Is On Measurable Results Within A Timetable

- the BSC or TOC targets are time based
- depending on the measures, stages of progress may be developed
3. Engages In Regular Monitoring Of Operations

- monitoring is comparison of actual to target results
- small organizations will do this in monthly meetings
- medium organizations will organize sub-committees with focussed monitoring roles eg. finance and program committees
- large organizations establish a purpose based meeting schedule
3. Engages In Regular Monitoring Of Operations

- best practice reporting is "exception" based
- attention is paid to variances in expectations
- meeting time is not spent reporting "we are on track", although this information is provided
3. Engages In Regular Monitoring Of Operations

• in medium and large organizations staff should report tactics being enacted to address the exceptions

• in small organizations, ad-hoc task forces of a few individuals are tasked with addressing critical exceptions
4. Challenges For Efficient Use Of Resources

- this is the habit that leads to continuous improvement
- note that having clear measures and targets in alignment with strategy ensures that the organization is effective
- but it does not guarantee that it is efficient, although usually some measures are of efficiency
4. Challenges For Efficient Use Of Resources

• the board challenges "the way it is always done" during:
  – retreats
  – annual budget review
  – multi-year cycle reviews of systems
4. Challenges For Efficient Use Of Resources

- this process of challenging applies in all sizes of organizations but it is not an excuse to:
  - micro-manage staff or volunteers
  - hijack meeting agendas with trivia
5. Decision Making Is Transparent

- Important board decisions are made by the full board (no executive committees) and include the seven steps of critical decision analysis:
  1. lucid presentation of the decision to be made
  2. preparatory materials that have been reviewed by the participants
  3. multiple alternatives are always provided
5. Decision Making Is Transparent

4. each alternative is compared to criteria of "must have", "relative best fit" and "adverse consequences" (risks) lucid presentation of the decision to be made

5. debate is open and impersonal

6. the decision is summarized, with rationale, in the minutes and read back to the participants before being finalized
5. Decision Making Is Transparent

7. decisions are published, other than matters that are confidential due to privacy or competitiveness

- this type of disciplined decision analysis may have to be taught to board members as part of their learning in a learning organization
6. Excellent Accounting to Stakeholders

- The role of the board of an NPO or Charity is ultimately about accountability to its stakeholders.

- Accountability means telling stakeholders openly and honestly: analysis:
  - what the organization has achieved, and
  - how it has managed its resources.
6. Excellent Accounting to Stakeholders

- **stewardship accountability includes:**
  - an annual report of activities, achievements and failures
  - both the BSC and TOC logic models provide a superb way to provide this reporting in an annual report
  - they convert the report from a "sales" document to true reporting
6. Excellent Accounting to Stakeholders

• **stewardship accountability also includes:**
  – the financial statements are freely available
  – there is a well constructed and open communications policy
  – there is a crisis communications policy
  – the board speaks as one
6. Excellent Accounting to Stakeholders

• stewardship accountability

*a board that operates with intention of providing this level of accountability will of necessity be focused on monitoring results and continuous learning*

• it will foster an organization driven to achieve its objectives
7. Has Crystal Clear Roles

- the best practice board has crystal clear roles, responsibilities and accountability definitions among board members, staff and volunteers

  *a common result from lack of clarity of roles is interference by board members in the activities of staff and volunteers*

- this leads to conflict and poor performance

- a clear understanding is critical to the quality of "monitoring" results
7. Has Crystal Clear Roles

• an extreme example of a response to this problem is the Carver Policy Governance Model

• a best practice board ensures there is:
  – no duplication of responsibilities
  – all responsibilities are assigned matching authority to act
  – all with responsibilities assigned are held accountable for their results
Conclusions

• the board role in developing & approving strategy, plans & budgets
  – adopt a logic model that connects the SWOT analysis to long and short term objectives, expressed through targets against which actual results are measured
  – BSC is an excellent model for NPO's
  – TOC is an excellent model for Charities
Conclusions

• aligning the resources for operational and capital planning
  – both BSC and TOC provide this alignment into plans and budgets
  – BSC was designed in the first instance to solve this problem in for-profit organizations
  – likewise TOC clarifies fuzzy thinking in Charity outcomes
Conclusions

• board monitoring and learning
  – board monitoring of organization results is an holistic process that includes continuous improvement
  – seven habits provide a useful summary of achieving this result in a balanced manner
  – participants in best practice boards reflect positively on their personal growth, & organizational achievements
Resources

Risky Business, Grant Thornton LLP
http://insights.grantthornton.ca/i/319479

20 Questions Directors of Not-for-Profit Organizations Should Ask about Strategy & Planning, H. Lindsay, CPA Canada

20 Questions Directors Should Ask about Strategy, 3rd Ed., K. Smith, CPA Canada

A Framework for Board Oversight of Enterprise Risk (Rev), J. Caldwell, CPA Canada
Resources

*Charities and Risk – a guide for trustees*, Charity Commission of England and Wales

*Legal Risk Management Checklist for Not-for-Profit Organizations*, Carters Professional Corporation

*Board Oversight of Management’s Risk Appetite and Tolerance*, T. Leech, Conference Board of Canada, 2011

*A Guide to Financial Statements of Not-for-Profit Organizations*, CPA Canada
Resources

*Strengthening Enterprise Risk Management for Strategic Advantage*,
Committee of Sponsoring Organizations of the Treadway Commission

http://www.coso.org/documents/COSO_09_board_position_final102309PRINTandWEBFINAL_000.pdf
Thank You

we hope this workshop will enhance your ability to enable a healthy third sector