Risk Management:

How to Protect Your Assets

Your organization's assets include far more than property. Don't put them at risk.

By Nora Kathryn Duncan

What is risk management and why should you be concerned with it? Risk management is simply doing all you reasonably can to protect your organization from financial loss due to natural disasters and people's actions. Every organization needs to have a risk management plan in place and review it periodically to make sure that, no matter what happens, the organization's mission will be carried out. Here are the steps to take.

> If you operate in a building that doesn't belong to you, be sure your insurance covers ***your*** property, not that of the building's owner.

Assess Your Assets

The first step in risk management is to analyze your organization's assets and think through possible events that might put them at risk. The Nonprofit Risk Management Resource Center (www.nonprofitrisk.org/advice) categorizes nonprofits' assets as follows:

• **people:** board members, volunteers, employees, clients, donors, and the public

• **property:** buildings, facilities, equipment, materials, copyrights, and trademarks

• **income:** sales, grants, and contributions

• **goodwill:** reputation, stature in the community, and the ability to raise funds and appeal to prospective volunteers.

Consider Your Risks

Keeping your assets in mind, you can begin constructing your risk management plan by asking questions like these:

• **Would your organization close down** if a bird flu epidemic infected half the staff?

• **How would your organization survive** if a fire or storm destroyed the building in which you keep records or provide services?

• **What would a general downturn of the economy** do to your organization?

• **What if someone associated with your organization** made a false statement to the press, destroying years of goodwill? Would the organization be able to stay in business and reestablish its good reputation?

These are a sample of possible risks you need to anticipate. It won't take you long to brainstorm many others. If your organization's work concerns children or health care, for example, you'll need to be aware of many state and federal laws, including safety laws, employment laws, and laws governing the service your organization provides.

Create a Risk Management Plan

Nonprofits are private organizations that operate for public purposes with public support and thus should strive to accomplish their missions ethically, openly, and with good stewardship of resources. A good risk management plan will include these considerations.

One of the first things people have to learn when they work with or for a nonprofit is that good inten-

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tions and charitable feelings don't always prevent lawsuits, public outrage, and liability if something goes wrong — even if the problem is the result of an accident or natural disaster. The nonprofit organization, although it may be working for the public good and doing a public service, probably has no charitable immunity from lawsuits.[1] The federal Volunteer Protection Act may keep individual volunteers from being sued,[2] but neither the organization nor its employees are covered. Furthermore, there are some important limitations on what the Volunteer Protection Act does cover.[3] Therefore, it's crucial for nonprofit boards to take a proactive, preventative approach to risk management and do everything possible to avoid problems due to inadvertence, inattention, and carelessness.

Everyone is familiar with strategies of risk management: You buy insurance to help with costs in case of accident, injury, or natural disasters. You teach your children not to play with fire, not to talk to strangers, and how to call 911. You maintain your vehicles to keep from having problems due to parts wearing out. Maybe you fence your yard to keep your dog from hurting anyone. These strategies can be classified as: insurance, training, maintenance, and prevention. They are all proactive actions to avoid potential legal problems.

When managing risks for your nonprofit, you can apply the same approaches, along with a few others. Here are the eight areas you should focus on when devising your risk management plan:

1. Legal structure: Whatever your organization's legal structure (corporation, trust, association, foundation), it is a creature of state or federal law, and there are certain legal criteria you must meet to maintain that status. The powers, rights, and duties of every officer and board member are set forth in your charter documents and bylaws. They are your organization's rules of procedure. If they're not followed exactly, your organization's acts are invalid. Moreover, individuals acting outside the requirements in these documents may subject themselves to personal liability for their actions.

2. Policies and procedures: Your policies and procedures — as well as whether everyone working with the organization uses them — can make or break your nonprofit. Policies and procedures set forth the rules of conduct for every aspect of your organization. They show your organization's character and the methodology you'll use to achieve your mission. If staff, clients, and donors don't understand and follow these policies, they and the organization may be liable.

Bad press from a fundraising event can do more to damage community goodwill and future fundraising than almost anything else.

3. Training: Training at all levels is of utmost importance. Board training familiarizes board members with their legal obligations to the organization and the public. Employee training involves employees in the mission; defines their legal rights and responsibilities toward clients and one another; reviews local, state, and national laws affecting the organization's work; and covers any specialized education they may need. Volunteer training instructs volunteers in what they can and cannot do, how their activities impact the organization's mission, and what rights and responsibilities they have. Without proper training, a nonprofit with the best policies and procedures in the world can be destroyed because the people act without knowledge.

4. Maintenance: In planning for proper maintenance, consider not only your furnishings, buildings, and equipment but also intangibles such as goodwill, donor base, trademarks, and copyrights. In the same way that you must plan for supplies, repair, and replacement of equipment, you must plan to keep lines of communication open with your donors, community, clients, other organizations, and government agencies to maintain your niche as a service provider.

5. Legal restrictions: Your organization's legal restrictions involve activities you undertake to attain your mission. There may be laws governing:

- ***the client population,*** such as children, the elderly, or the disabled
- ***activities*** such as food handling
- ***issues of safety,*** such as motor vehicle regulations, special equipment needed, or background checks for volunteers.

You must comply with all laws governing such activities. In addition, there may be fees to pay and permits you must receive before beginning the activity.

6. Insurance: Some nonprofit managers think that having insurance *is* risk management. Insurance is only *part* of risk management, but it's an important part.

Insurance is a way to share the cost of a misfortune with the insurance company so that your organization doesn't have to pay the whole cost if sued. The insurance policy is a contract between your organization and an insurance carrier and must be carefully negotiated and understood. The contract states *who* is covered (the organization, volunteers, employees, general public), *what events* are covered (unintentional mistakes, fire, accident), *how much the company* will pay for a covered incident (limit of policy), and *how much the organization* must pay before the insurance company pays (deductible).

Examine your contract to be sure the insurance you need is included. Most policies include a duty-to-defend claim that obligates the insurance company to find and hire legal counsel. Defense costs can be either "inside" or "outside"

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the policy limits. Many times, the most expensive parts of the claim are litigation costs and legal fees. If there's a $1,000,000 policy limit and the costs are inside the policy limits, the real amount of the coverage is reduced. If it cost $500,000 to defend the suit and the settlement or judgment was $600,000, the organization would still be required to pay $100,000 because the policy limit had been reached.

When seeking insurance, look for an agent who's familiar with nonprofits. Nonprofits have some characteristics that other businesses don't, and special clauses must be added to accommodate these anomalies. For instance, nonprofits typically use volunteers; a nonprofit may conduct activities in buildings owned by someone else; and volunteers or paid staff may need to go to clients' homes to provide services. These and other considerations should be allowed for in the contract and may take special underwriting by the insurance company. The best way to find out what insurance products are available is to go through a state- or area-wide nonprofit group or trade organization specifically servicing the nonprofit sector.

At a minimum, your organization should have the following types of insurance:

Directors' and officers' (D & O) liability insurance protects board members and managers from paying damages due to unintentional harm caused by a negligent management decision. There may be some personal immunity if the person was acting within the scope of assigned duties and wasn't malicious, negligent, or reckless. To protect the organization, "entity coverage" must be included in the policy. The D & O policy can be worded so that volunteers who aren't directors are covered as well. If your organization has D & O coverage, it will be easier for you to recruit directors and volunteers.

D & O insurance covers a broad scope of activity. D & O claims may include employment claims; age discrimination; sexual harassment; misappropriation of funds; and discrimination grounded on race, sex, national origin, disability, or religion, to name a few.

Property insurance covers your organization's physical assets. If your nonprofit owns land, buildings, supplies, or any kind of equipment (computers, copy machines, and the like), you have property you need to insure. If you have intangible property rights like copyrights and trademarks, you need to protect those rights too. If you operate in a building that doesn't belong to you, be sure your insurance covers *your* property, not that of the building's owner. Even if your assets include only used furniture and donated equipment, you'll still need to replace them in case of fire, flood, tornado, hurricane, or theft. So be sure your property insurance covers replacement costs.

Commercial general liability insurance is the third major category of insurance every nonprofit should carry. It comes into play when a customer, client, or member of the public is injured at your organization's office or the location where you deliver services. It differs from D & O insurance in that it covers "slip and fall"-type claims where someone is injured due to a negligent act. Sometimes both D & O and general liability policies may cover the same incident, but the scopes of the two types of policies are different.

Other types of necessary insurance are workers' compensation insurance and vehicle insurance if your organization owns vehicles. Both kinds of insurance are required by law. You may need other special types of insurance depending on your organization's work.

There are exclusions in every insurance policy. Exclusions are people, acts, or events that the insurance company eliminates from coverage so that it has no liability in that area. Regularly excluded from coverage are: criminal acts; intentionally harmful, rash, or grossly negligent acts; and acts that are outside the scope of an employee's duties.

7. Fundraising: Many nonprofits don't consider the risks of fundraising. Here are some of the regulations

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you need to keep in mind:

• ***Tax regulations*** require you to list on your income tax form the names of donors who give over a certain amount.

• ***When holding a fundraising event,*** you must obtain permits and adhere to security requirements.

• ***Sales tax liability*** may be incurred when selling anything for your organization.

• ***Public health regulations*** may affect an event.

Any event or solicitation has to be thought through and analyzed to make sure it's lawful. Some fundraising events may be too costly to host when all the legal requirements are considered. Bad press from a fundraising event can do more to damage community goodwill and future fundraising than almost anything else.

8. Partnering with other organizations: Partnering can help your organization share risks. If one partner has vans for transporting clients, for instance, all transportation can be done by that organization, thus eliminating that risk for the other partners. Programs may be conducted in municipal buildings and thus covered by the municipality's liability insurance, reducing the risk to other partners. Whatever the arrangement, be sure the partnering contract spells out the responsibilities and liabilities of each entity.

Don't Court Disaster

Using this outline, you can develop a useful risk management plan. No matter the size of your

Partnering can help your organization share risks.

organization, you need such a plan to avoid financial loss. Without it, your organization is headed for trouble.

A risk management plan won't keep bad things from happening. But it will help your organization continue to function and carry out your mission if something does happen.■

Footnotes

[1] The legal term "charitable immunity" deals with whether or to what extent a nonprofit organization enjoys immunity from liability for damages merely because it is organized for charitable purposes. Most jurisdictions have abolished or severely limited the concept of immunity for nonprofit organizations. The annotation in 25 *American Law Reports*, 4th 517 ("tort immunity of nongovernmental charities — modern status") discusses the relevance of the doctrine on a state by state basis.

[2] 42 *United States Code Annotated*, 14501. For guidance on how this Act affects your organization, see these *Nonprofit World* articles at www.snpo.org: "What Are We Doing to Protect Our Volunteers from Lawsuits?" (Vol. 9, No. 4), "Don't Let Volunteers Put Your Organization at Risk"(Vol. 10, No. 1), "Volunteers: Resource or Risk?" (Vol. 15, No. 5), and "Volunteer Protection Act: What Does It Mean for You?" (Vol. 16, No. 2).

[3] Employment claims are excluded; legal expenses in defending against a claim are excluded even if the act itself is covered; actions outside the scope of the volunteer activity are excluded, as is harm caused as a result of gross negligence, an intentional act, or reckless misconduct. In cases in which licenses are required, volunteers may not be protected if they weren't properly licensed.

Your Planning Kit

For more help in preparing your risk management plan, see these *Nonprofit World* articles at www.snpo.org:

• **Six Steps to Good-Reputation Insurance** (Vol. 15, No. 1)

• **How Risky Is Your Special Event?** (Vol. 20, No. 1)

• **Does Your Board Need Liability Insurance?** (Vol. 12, No. 6)

• **The Most Likely Lawsuits — and How to Protect Yourself** (Vol. 19, No. 1)

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• **Why You Should Consider Trademark Protection** (Vol. 23, No. 4)

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