

HELP Risk Management Seminar

August 11, 2011




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Quick Review

- **Risk** = Anything that can stop you in achieving your mission
- **Risk management** = understanding risk & deciding what to do about it
- **3 Types of Risk** – Hazard, Business & Strategic
- **3 Risk Management Strategies**
 - Prevent
 - Mitigate
 - Transfer


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Duties, Responsibilities, Policies & Procedures

BOARD BASICS

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Duties

- Duty of Care → • Prudent management
- Duty of Loyalty → • No conflict of interest
- Duty of Obedience → • To charter & bylaws

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Basic Responsibilities

The law requires a Director and/or officer of a Kentucky Non-profit Corporation to act on an informed basis, in good faith and in a manner which he/she honestly believes is in the best interest of the corporation.

- **Establish a mission and purpose** for the organization and articulate goals.
- **Select an executive director** and establish his or her responsibilities.
- **Ensure effective organizational planning**, establish programs and services consistent with the organization's mission and assist in implementing and monitoring the plan's goals.
- **Ensure adequate resources** so that the organization may fulfill its mission.
- **Provide financial oversight** and assist in developing an annual budget and ensuring that proper financial controls are in place.
- **Ensure legal and ethical integrity** and maintain accountability for adherence to legal standards and ethical practices.
- **Recruit and orient new board members** and assess board performance.
- **Non Profit Directors and Officers must always act for the benefit of their organization**, avoid any conflicts of interest and exercise the utmost skill and care in decision-making.

Responsibilities will vary by organization and must be clearly articulated.

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Policies & Procedures

- **Board Selection**
- **Board Expectations**
- **Board Protocols**
- **Board Communication**

Be intentional & systematic!


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Understanding Risks for Directors & Officers

BASIC BOARD RISKS

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4 Main Risks

Most of the risks for non-profit boards can be summarized in these four categories

- Ineffectiveness
- Non-compliance
- Damaged Reputation
- Lawsuits

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Who Can Sue a Non-Profit?

- Current & former staff
- Volunteers
- Vendors & suppliers
- Competitors
- Creditors
- Clients & recipients of services
- Donors
- Members
- The Entity or its Director can sue the board
- State Attorney General
- Other Government Officials (IRS, Dept of Labor, etc.)
- *Anyone affected by the boards decisions*


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Some Facts & Stats

- **Volunteer Protection Act and other state immunity laws will not prevent** board members from being named in a suit
- The **average cost to defend D&O claims is \$100,000** (more than the operating budget for most non-profits)
- The **majority of claims are brought by current and former employees**
- **55% of claims are brought by those with financial interest** in the boards' decisions

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Some Examples

People <ul style="list-style-type: none">• ADA claim – disability or inconvenience?• Professional liability - Volunteer counselor gets too personal• Double trouble – sexual harassment	Financial <ul style="list-style-type: none">• Misrepresentation or market forces?• Organ Donation – misuse of funds
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Four examples taken from www.nonprofitrisk.org/library/articles/insurance0901997.shtml


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The Biggest Risks for Directors & Officers

TOP 10 BOARD RISKS

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Risk #1 – No D&O Insurance

- Without D&O insurance, the only indemnification is the *non-profit's bank account*
- Individual board members can be named in a lawsuit and their *personal assets* may be at risk
- *No other policy* covers this risk


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Risk #1 – No D&O Insurance

<h3>What does D&O Cover?</h3> <ul style="list-style-type: none"> • Criminal lawsuits • Civil lawsuits • Administrative or regulatory proceedings • Alleged wrongful acts committed by directors, officers, trustees, employees, volunteers & members 	<h3>Who does D&O Cover?</h3> <ul style="list-style-type: none"> • The Organization & Subsidiaries • Past, present & future: <ul style="list-style-type: none"> – Directors – Officers – Trustees – Employees – Volunteers – Members • Spouses of Insureds • Estates, Heirs, Legal representatives or assigns of deceased or incapacitated insureds
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Note: These are general answers and not specific to your insurance policy. Check with your insurance agent to see what & who your policy covers.



Risk #2 – Non-Compliance with Charter & By-laws

- In Kentucky, a failure of an organization to follow its own Articles of Incorporation, Bylaws, Policies and Procedures can constitute negligence per se and act as an independent cause of action against the non-profit corporation.
- It is important to set achievable rules, regulations, policies and procedures. Avoid aspirational polices in this regard because these can usually not be attained.

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Risk # 3 - Board Ineffectiveness

Ineffective	vs.	Effective
• Disengaged		• Engaged
• Unfocused		• Focused
• Imbalanced		• Balanced
• Lack of Trust		• Trust
• Unproductive arguing		• Healthy debate
• Can't make decisions		• Able to make decisions
• Strife		• "All In"
• Doesn't get results		• Gets results


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Risk # 3 - Causes for Ineffectiveness


Ineffective	Effective
<ul style="list-style-type: none"> • Poor leadership • No “new blood” • Poorly run meetings • Lack of communication • Size (too large or small) • Lack of training • Wrong people • Poor Relationships 	<ul style="list-style-type: none"> • Great leadership (Level 5) • Healthy growth & turnover • Well-run meetings • Good communication • Size & makeup • Systematic Training • Right people • Strong relationships

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Risk #4 – EPLI Claims


- What is EPLI?
 - **Employment Practices Liability Insurance**
- What are some types of EPLI Claims?



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graph LR
    A[Hiring/Firing] --> B[Sexual Harassment]
    B --> C[Discrimination]
          
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- Who can these claims affect?
 - **Employees, Volunteers, Clients, Vendors**

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EPLI Risk Management


Prevent & Mitigate

- Systematic hiring process
- Employee handbook
- Communication process for complaints
- Document everything

Transfer

- EPLI Policy – may not cover the board
- D&O – only policy that covers the board explicitly
- Most D&O policies have the option of adding EPLI
- Concern of combined limits


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Risk #5 – Loss of Tax-Exempt Status (IRS 990s)

- Just because you have a Kentucky Non-Profit Corporation does not mean that you have tax-exempt status. In order to be a tax-exempt corporation, you must apply for Internal Revenue Code Section 501(c)(3) (or other similar) status.
- Enlist the assistance of an accountant to help with this process. Failure to comply with the myriad IRS rules may result in a loss of tax exempt status.

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Risk #6 – Financial Mismanagement

- **Duty of Care** – financial oversight
- **Examples of Mismanagement**
 - ✓ Negligence
 - ✓ Misuse of donations
 - ✓ Breach of contract
 - ✓ Late or missed payments
 - ✓ Bad decisions
 - ✓ Other?


8/11/2011 *Examples taken from Gateway Specialty Insurance



Financial Management Best Practices

<h3>Board Requirements</h3> <ul style="list-style-type: none"> • Require Board Participation in fiscal affairs • Require regular, timely reports from the internal staff (budgets, financial statements, annual 990s) • Don't just take at face value. Ask critical questions. 	<h3>Equipping Your Board</h3> <ul style="list-style-type: none"> • Provide training <ul style="list-style-type: none"> – How to read financial statements – The financial goals and practices of the organization – The organization's budget • Provide resources <ul style="list-style-type: none"> – Books or journal articles – Audited financial statements for previous year w/narrative highlights – Consolidated audited financial statements from past 5 years – Approved operating budget (current) – Financial policies & procedures – Investment policies & procedures
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Good book by Andrew Lang *How to Read Nonprofit Financial Statements* can be ordered on amazon.com
Financial Risk Management: A Guide for Nonprofit Executives from www.nonprofitrisk.org



Risk #7 – Firing (or not firing) Board Members

- “Bad Actors”
 - Behaviors?
- Risks
 - Firing:
 - Keeping:

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Risk Management for Firing Board Members

Prevention <ul style="list-style-type: none">• Board job descriptions• Orientation & training• Coaching• Communication protocols• Meeting protocols• Clear structure• Keep Members Engaged!	Mitigation <ul style="list-style-type: none">• Timely follow-up on concerns• Board “interventions”• Disclosure and formal action• Documentation
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Risk #8 – Major Situations

- Crisis **Planning**
- Crisis **Management**
- Post-Crisis **Evaluation**


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Risk #9 – Conflicts of Interest

- What is a **conflict of interest**?
- What is a **related party transaction**?
- What **duty** is violated with a conflict of interest?
- What's the **risk**?


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Risk #10 – Leadership Succession

- How big of a risk is Leadership Succession to your organization?
- Does your organization have a plan for recruiting and mentoring future leaders?
- Do you have a succession plan for your Director & other key leaders?

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In Conclusion


It all comes back to MISSION...

which requires great LEADERSHIP...

which requires great SACRIFICE...

which requires great PEOPLE.


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In Conclusion

- Take a minute and write down your KEY 3 take-aways from today's discussion
- We appreciate your feedback
- Questions?

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Thanks!

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Contact Information

Todd Anderson, Risk Advisor

tanderson@peelholland.com

(270) 527-6152

Jennifer Revell, Business Development

jrevell@peelholland.com

(270) 527-6130

Chip Adams, Attorney

wcadams3@wcadamslaw.com

(270) 753-1292



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