



Charity Law  
Information  
Program

We realize the potential of  
not-for-profit organizations

# Charity Law Information Program (CLIP)

## Risk Management for Canadian Charities

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# Who We Are – Capacity Builders

- Capacity Builders is a division of the Ontario Community Support Association (OCSA) and it runs the **Charity Law Information Program (CLIP)**
- **CLIP provides training, workshops, and webinars to Canadian charities to enhance their understanding of their legal, ethical, and governance obligations**
- <http://www.capacitybuilders.ca/clip>
- CLIP Communiqué – sign up for free
- (416) 256 – 3010 x 232 or 1-877-484-3030
- [clip@capacitybuilders.ca](mailto:clip@capacitybuilders.ca)
- The Charities Directorate of CRA has provided funding for CLIP

# Who We Are – Blumbergs

- Blumberg Segal LLP is a law firm based in Toronto, Ontario
- Mark Blumberg is a partner at Blumbergs who focuses on non-profit and charity law
- Assists charities from across Canada with Canadian and international operations and foreign charities fundraising here
- [www.canadiancharitylaw.ca](http://www.canadiancharitylaw.ca) and [www.globalphilanthropy.ca](http://www.globalphilanthropy.ca)
- Free Canadian Charity Law Newsletter. Sign up at: <http://www.canadiancharitylaw.ca/index/php/pages/subscribe>
- (416) 361 – 1982 or 1-866-961-1982
- [mark@blumbergs.ca](mailto:mark@blumbergs.ca)

# Charities Directorate of CRA

- Regulates registered charities
- Based in Ottawa and other offices throughout Canada
- Website: [www.cra.gc.ca/charities](http://www.cra.gc.ca/charities)
- E-mail list: [www.cra-arc.gc.ca/esrvc-srvce/mlist/sbscrbchrts-eng.html](http://www.cra-arc.gc.ca/esrvc-srvce/mlist/sbscrbchrts-eng.html)
- Webinars: [www.cra-arc.gc.ca/tx/cmmnctn/sssns/wbnrs-eng.html](http://www.cra-arc.gc.ca/tx/cmmnctn/sssns/wbnrs-eng.html)
- Telephone:           1-800-267-2384 (English)  
                                  1-888-892-5667 (Bilingual)
- Through CPOP supporting 19 charities conducting educational work on legal and *Income Tax Act* compliance.



# Introduction

- Legal information not legal advice
- Views expressed are our own
- Questions during and at end
- Handout
- Logistics and timing

# What is a Registered Charity?

- 1) Purposes must be exclusively and legally **charitable**  
(4 heads of charity – relief of poverty, advancement of education; advancement of religion; and other purposes beneficial to the community in a way the law regards as charitable)
- 2) Must be established for the benefit of the public or a sufficient segment of the public (**Public Benefit**)
- 3) Application must be accepted by the Charities Directorate of CRA (**Registered**)



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# Risk Management

# Why Risk Management?

- Helps achieve objects and aims;
- Know risks and monitor them enabling board and charity to be more effective and avoid embarrassment; and
- Improved planning for the future.

## In UK

In UK with annual filing directors have to include a

"statement confirming that the major risks to which the charity is exposed, as identified by the trustees, have been reviewed and that systems have been established to manage those risks".

Extensive use of **Charities and Risk Management** from the UK

Charity Commission in this presentation. July 2007

<http://www.charity-commission.gov.uk/investigations/charrisk.asp>

# How Can Risks Be Managed

- 1) Transfer financial risk to third parties or sharing it (e.g. insurance, outsourcing);
- 2) Avoid risky activity completely;
- 3) Manage or try to mitigate risk; or
- 4) Accept risk (e.g. assessed as an inherent risk that cannot be avoided if the activity is to continue).

# Types of Risk

- **Governance risks** – eg inappropriate organisational structure, difficulties recruiting trustees with relevant skills, conflict of interest;
- **Operational risks** - eg service quality and development, contract pricing, employment issues; health and safety issues; fraud and misappropriation;
- **Financial risks** - eg accuracy and timeliness of financial information, adequacy of reserves and cash flow, diversity of income sources, investment management;

## Types of Risk (Cont.)

- **External risks** - eg public perception and adverse publicity, demographic changes, government policy;
- **Compliance with law and regulation** - eg breach of trust law, employment law, and regulatory requirements of particular activities such as fund-raising or the running of care facilities.

# Board's Role in Risk Management

- **Board is ultimately responsible.**
- **Can delegate but still responsible to ensure it is done**

# Board's Role

“This is likely to involve:

- Ensuring that the identification, assessment and management of risk is linked to the achievement of the charity's operational objectives;
- Ensuring the process covers all areas of risk e.g. financial, governance, operational and reputational and is focused primarily on major risks;
- Ensuring that the process seeks to produce a risk exposure profile that reflects the trustees' views as to levels of acceptable risk;

## Board's Role (cont.)

- Reviewing and considering the principal results of risk identification, evaluation and management;
- Ensuring that the risk management is ongoing and embedded in management and operational procedures.”

# How to Identify and Manage Risk

UK Charity Commission suggests:

1. Establish risk policy.
2. Identify risks and controls.
3. Assess risk.
4. Evaluate what action needs to be taken.
5. Periodic monitor and assess.

# 1) Establish Risk Policy

- Risk is an inherent part of being charity
- Risk comes from action and inaction
- Activities can be low risk or high risk or in between
- What is your charity and board's risk tolerance
- Is activity necessary to achieve mission
- Board must communicate to staff and volunteers what are acceptable and unacceptable risks.

## 2) Identify Risks and Controls

- In small operations board can review operations
- In large operations may need staff, other volunteers and professionals.
- Checklists – helpful, but not enough
- Need some creativity
- Subjective
- Be reasonable (not absolute)

# Identify Risks and Controls (cont.)

- The charity's objects, mission and strategy;
- The nature and scale of the charity's activities;
- External factors –law, reputation, funders;
- Past mistakes and problems;
- Corporate structure – what are your partners, agents, affiliated charities doing;
- Review what similar area/size charities are doing; and
- Checklists of risk factors prepared by other charities or other organisations.

## 3) Assessing Risk

- Likelihood of undesirable event or outcome— high or low
- Severity of impact on operational performance
- Can have matrix
- Also can score them
- “Severity of impact could be scored from 1 (least serious) to 5 (most serious) and similarly the likelihood of occurrence could be scored from 1 (remote) to 5 (almost certain).”
- But cannot ignore other risks.

## 4) What Actions Should Be Undertaken

- Take appropriate action
- Are adequate controls in place
- What additional actions are needed
  - Transfer, Avoid, Manage, Accept

## 5) Periodic Monitoring and Assessment

- Risk assessment is not one off event
- Needs to be imbedded in organization
- Need to be those responsible for implementation
- Report new risks
- Report failures in control systems
- Board show review at least annually
- Consider occasionally new risk from external factors such as legislation, regulatory requirements or funders.

# UK Summary

“Major risks” are those risks which have a high likelihood of occurring and would, if they occurred, have a severe impact on operational performance, achievement of aims and objectives or could damage the reputation of the charity, changing the way trustees, supporters or beneficiaries might deal with the charity. Risk management should therefore not be seen purely as a compliance issue nor as being solely focused on the prevention of disaster. The process enables trustees to focus on the management of risks that would prevent the charity achieving its strategic objectives. In so doing, charities are able to take opportunities and develop with an understanding of the risks faced, and with confidence that reasonable steps have been taken to manage them.”



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# Ethical Standards

# Legal vs. Ethical

**Legal** – binding minimum rules and regulations

**Ethical** – higher standard than legal – ‘applied ethics’ – trying to achieve moral and ethical outcomes in real-life situations consistent with our values and standards.



# Ethical Concepts

Integrity

Fairness

Trust

Transparency

Responsibility

Privacy

Honesty

Justice

Human Rights

Cooperation

Sustainability

Respect

# Charity Stakeholders

- Members
- Board
- Employees of charity
- Volunteers
- Government (CRA, federal, provincial, and municipal)
- Partners
- Media
- Public
- Donors
- Beneficiaries, clients

# What is an Effective Charity

- Hallmark 1: Clear about its purposes and direction
- Hallmark 2: A strong board
- Hallmark 3: Fit for purpose (structure and policies allow it to deliver services efficiently)
- Hallmark 4: Learning and improving
- Hallmark 5: Financially sound and prudent
- Hallmark 6: Accountable and transparent

The UK Charity Commission Hallmarks of an Effective Charity: <http://www.charity-commission.gov.uk/publications/cc10.asp>

# Useful Questions or Imperfect Rules

- What is your gut feeling?
- Would it pass the sniff test?
- Would you mind if all your associates, family and friends were aware of it?
- Can you justify it to a committee of your peers?
- If our charity does this lots, what type of organization would we be?
- Using your imagination, is there another better alternative?

# Weaknesses in Ethical Decision Making

- Do not recognize issues
- Do not have adequate facts
- Lack of education on issues
- Fairness to some stakeholders, not others
- Short term benefit – end justifies the means
- Focusing only on legal
- But we have always done it this way ...



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# Governance

# What is Governance?

- *Governance* comes from the Greek verb [*kubernáo*] which means *to steer*
- **The process of decision-making and the process by which decisions are implemented (or not implemented)**
- No one size fits all – e.g. small volunteer charity vs. large national charity

<http://www.unescap.org/pdd/prs/ProjectActivities/Ongoing/gg/governance.asp>



# Who is Responsible for Governance?

Directors ultimately responsible for  
governance and charity

# Can We Operate on Trust Alone?

- In an ideal world, perhaps – we don't live in ideal world
- Most people are honest, but some are not
- Some are honest but will be tempted if there are no guidelines, rules or financial controls
- Some funders and donors will not support organizations without appropriate rules and financial controls
- Understandable rules and good financial controls are a win-win for everyone
- Policies and good financial controls can help prevent or limit personal liability in event of problems

# Board Responsibilities – 7 Key Tasks

- a) Setting the mission and strategic objectives, evaluating progress in achieving these objectives;
- b) Making sure the organization operates in a fiscally responsible manner and complies with all laws and regulations applying to it;
- c) Selecting and evaluating the performance of CEO;
- d) “Boundary Spanning”: (i) by bringing the concerns of the outside community and particular constituencies into the organization; and (ii) by representing the organization to the community and constituencies;

# Board Responsibilities – 7 Key Tasks

- e) Ensuring necessary financial resources;
- f) Ensuring management operates organization as efficiently as possible and uses the best available systems, policies and administrative practices to do so;
- g) Ensuring that the board itself functions as effectively as possible (e.g., finds best people to serve, provides adequate training for members, manages its meetings and committees well).

“Improving Board Performance” by Vic Murray in The Philanthropist  
(Volume13, No.4)

<http://journals.sfu.ca/philanthropist/index.php/phil/article/view/161/161> 36

# Governance Gremlins

- Lack of consensus about the mission and vision of the organization
- High Board/CEO turnover
- Lack of consensus on Board role
- Board members do not fully understand their duties and liabilities
- Board members have difficulty reading financial statements
- Unresolved conflicts on the Board or between the Board and the CEO

## Governance Gremlins (cont.)

- Lack of understanding on roles of Officers, or how one gets to become an Officer
- Current board practice or structure does not match by-laws
- Confusion over conflict of interest
- Too many committees
- Committees that are not engaged in important work
- CEO-run Board
- Rubber-stamping by the Board
- Board micro-management

## Governance Gremlins (cont.)

- Decision paralysis
- Lack of strategic direction and clear priorities for the Board
- The Board runs well but focuses on the wrong issues
- Board members do not speak as a united front once they leave the Board room
- Poor attendance at Board or committee meetings
- Poorly chaired meetings

# Governance Gremlins (cont.)

- The Board is not getting the right information in the right format
- Lack of clarity on role of Board vis-à-vis staff
- Poor relationships with stakeholders
- Members of the organization are not involved or consulted
- Volunteer fatigue or staff burnout

<http://www.iog.ca/boardgovernance/html/prasig.html>

# How to Go from Gremlins to Great

- Recruit diverse and talented board
- Put in place appropriate governance model
- Ensure board and staff/volunteers understand role
- Continuous learning and improvement for board and staff
- Focus on mission
- Invest in people
- Invest in organization

# Recruiting Good Boards

- Identify skills, experience, knowledge, contacts, required and weaknesses in current board
- Advertise widely to get greater diversity and quality – include job description/expectations
- Check carefully (references, background, conflicts)
- Select carefully – interview
- Formally bring on to board
- Orient well – orientation, board binder, site visit



# Misuse of Charity's Assets

# What is Misuse of a Charity's Resources?

- Mistakes
- Fraud
- Money laundering
- Terrorism
- Violence against aid workers and kidnapping
- Private benefits
- Misappropriation of resources
- Using charities for tax evasion

# Mistakes

- Happens every day with major charities with large finance staff
- Why would it not happen with small and medium charities or foreign intermediaries
- Everyone makes mistakes
- Mistakes can lead to embarrassment and false accusations
- Minimizing and catching mistakes is win/win

# Fraud

- Common in commercial enterprises and non-profits
- 10% of fraud reported is in non-profit sector
- Charities with weak controls are vulnerable
- Madoff and other scandals
- Impossible or prohibitively expensive to absolutely prevent – can you discover and minimize
- Average fraud = \$190,000 but ¼ are over a million
- Estimate of 5% of revenue lost to fraud across all organizations
- Smaller and less financial controls suffer disproportionately more

# Examples of Fraud

- Payroll fraud
- Assets misappropriated
- Intercepting or diverting resources coming to charity
- Skimming cash before recorded in accounting system
- Expense reimbursement fraud
- Fraudulent billing
- Using office to get unauthorized benefit (bribes, self dealing transactions, conflicts of interest)
- Falsification of organizations financial statements
- Steals confidential information to apply for credit card or loan
- Fraudulent use of official donation receipts

# Preventing Fraud

- Good financial controls
- Internal spot audits
- External audit
- Encourage employees to come forward (whistleblower)
- Encourage suppliers and customers to report

# Money Laundering

- Money laundering is the process used to disguise the source of money or assets derived from criminal activity.
- Turn “dirty” money into “clean” money
- This criminal activity can include drug trafficking, smuggling, fraud, extortion and corruption
- Criminals must launder the profits and proceeds from these crimes to be able to enjoy them
- International Monetary Fund (IMF) estimated that some \$500 billion (U.S.) is laundered worldwide each year.

# Money Laundering Red Flags

- Donations conditional upon particular individuals or organizations being used to do work for the charity
- Offers of donations in cash, for a certain period of time, the charity to receive the interest, but the principal to be returned to the donor at the end of the specified period
- Donations in foreign currencies, with the provision that the principal be returned to the donor in the form of a different currency

# Avoiding Abusive Charity Gifting Tax Shelters

- Over \$5 billion in gifting tax shelters over last 5 years
- Over 175,000 Canadians being audited
- If it sounds too good to be true, it probably is
- Be careful of advice from people who have a financial benefit in the transaction

# How Terrorists May Try to Use Charities

- Money raised by charities to fund terrorist organizations;
- Using charities to smuggle people into countries illegally;
- Using residential schools as military recruitment and training centres;
- Using charities set up for providing facilities for young people for organization and recruitment;
- Using charities as a base to spread propaganda; or
- Using charities for money laundering purposes.

<http://www.charitycommission.gov.uk/supportingcharities/ogs/g096.asp>

# Avoiding Terrorism

CRA Checklist for Charities on Avoiding Terrorist Abuse

<http://www.cra-arc.gc.ca/tx/chrts/chcklsts/vtb-eng.html>

UK Operational Guidance: Charities and Terrorism

<http://www.charitycommission.gov.uk/supportingcharities/ogs/g096.asp>

U.S. Treasury Dept. Anti-Terrorist Financing Guidelines –  
Voluntary Best Practices for U.S.-Based Charities

<http://www.ustreas.gov/offices/enforcement/key-issues/protecting/charities-intro.shtml>

16 Steps for Canadian charities and non-profits to avoid  
involvement with Terrorism by Mark Blumberg

[http://www.globalphilanthropy.ca/images/uploads/Terrorism\\_and\\_Canadian\\_charities\\_and\\_Non\\_Profit\\_organizations.pdf](http://www.globalphilanthropy.ca/images/uploads/Terrorism_and_Canadian_charities_and_Non_Profit_organizations.pdf)

# Safety of Charity Staff

- Goal is to implement humanitarian program
- Violence against aid workers increasing problem
- Kidnapping, extortion, unlawful detention, civil unrest, random criminal violence, workplace violence, travel
- Neutrality is no guarantee of safety
- NGO roles are vitally important
- Board, employee, funder concerns
- ‘Hope’ is not a security plan

# Violence Against Humanitarian Workers

- Have security plan
- Look at programs, threat and vulnerabilities
- Plan from proposal stage for security
- Training before project and briefings during
- Pick right people – maturity, expertise, medical fitness
- Physical security of office, home, lodging, facilities
- Be aware of local laws, customs and sensitivities
- Check what insurance will cover and not cover
- Careful who you hang out with and where

# Private Benefits

Charity should be about helping beneficiaries, not yourself

- Private benefit is acceptable only if it arises directly through pursuit of the charitable purpose, is incidental to the pursuit of that purpose, and is reasonable in the circumstances
- Questionable benefits: generous salaries, luxurious living expenses, travel, self promotion of founder/leader etc.
- CRA referring to governance issues in Guidance on Fundraising



# Internal Controls – Quick Overview

# The Elements of Internal Control

Six important elements of an internal control system are:

1. Control cues (lead by example)
2. Policy communication
3. Segregation of duties
4. Record keeping
5. Budgets
6. Reporting

McLaughlin, Thomas A., *Streetsmart Financial Basics for Nonprofit Managers*, 3<sup>rd</sup> ed. (Hoboken, New Jersey: John Wiley & Sons, Inc., 2009).

# Segregation of Duties

- Break up duties
- Avoid one person dominating
- Checks and balance
- Danger from within – only takes one person
- For very small organizations – complementary control

# Two Person Segregation of Duties

## Treasurer/Employee – First Person

- Post accounts receivable
- Mail checks
- Write checks
- Post general ledger
- Reconcile bank statements
- Post credits/debits
- Give credits and discounts
- Approve payroll
- Open mail/receive cash
- Disburse petty cash
- Authorize purchase order
- Authorize check requests
- Approve invoices for payment

McLaughlin, Thomas A., *Streetsmart Financial Basics for Nonprofit Managers*, 3<sup>rd</sup> ed., p 230.

# Two Person Segregation of Duties (cont.)

## CEO/ED/Chair/President/Volunteer – Second Person

- Sign checks
- Sign employee contracts
- Custody of securities
- Complete deposit slips
- Perform interfund transfers
- Distribute payroll
- Reconcile petty cash
- Record initial charges and pledges
- Approve employee time sheets
- Prepare invoices
- Complete check log

McLaughlin, Thomas A., *Streetsmart Financial Basics for Nonprofit Managers*, 3<sup>rd</sup> ed., p 230.

# Controls over Incoming Funds

Cheques and cash in mail

- Two people opening
- Record immediately
- Secure unopened mail

Public collections and fundraising events

# Expenditure Controls - Cheques

- Governing documents provide for people authorized to sign cheques
- Abide by governing documents or change them
- Should have two unrelated signatories on cheques
- Have adequate pool of signatories
- Best not to sign cheques to yourself
- Keep cheques in safe and secure place
- Do not sign blank cheques
- Have agreed bank limits
- Only sign cheques with corresponding invoice

# Expenditure Control - Salaries

- For many charities this is their largest expense
- Significant charity and director liability for failure to withhold and remit source deductions and for payment of wages
- Proper employment agreement with each employee setting out salary and termination provisions etc.
- Are deductions for CPP, EI and income taxes being made?
- Are funds being remitted as required?
- Check that salaries are correct
- Spot check with larger organizations for “fictitious employees”

# Investments

- Directors have duty to invest funds that are not immediately required
- Many charities have limited powers of investment
- Look to letters patent and by-laws for power to invest or trust document if trust
- Wording of powers is important
- A trustee must exercise the care, skill, diligence and judgment that a prudent investor would exercise in making investments
- Act prudently and reasonably

# Financial Management Resources

- [www.capacitybuilders.ca/clip](http://www.capacitybuilders.ca/clip)
- [www.canadiancharitylaw.ca](http://www.canadiancharitylaw.ca)
- [www.cra-arc.gc.ca/tx/chrts/prtng/menu-eng.html](http://www.cra-arc.gc.ca/tx/chrts/prtng/menu-eng.html)
- [www.boardsource.org](http://www.boardsource.org)
- [www.fme-online.org](http://www.fme-online.org)
- [www.oxfam.org.uk/resources/](http://www.oxfam.org.uk/resources/)
- [www.johncammack.net](http://www.johncammack.net)
- [www.globalphilanthropy.ca](http://www.globalphilanthropy.ca)
- [www.mango.org.uk](http://www.mango.org.uk)



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# Save the Dates!

## February 22 & 23, 2010

### ***Being Good at Doing Good: Safeguarding Yourself and Your Charity in a Complex World***

Plan to join us in February for this groundbreaking conference that will explore good governance and accountability, financial controls, and how you can prevent your resources from being misused.

For more information, visit <http://www.capacitybuilders.ca/clip>

**Location: Toronto Board of Trade**

# Evaluation

- Your feedback is important to the Charity Law Information Program
- Please complete the Evaluation Form and add any comments that will help improve our program
- If you have any additional feedback contact [clip@capacitybuilders.ca](mailto:clip@capacitybuilders.ca)
- Thank you for your participation today!