OPEN ROAD

KEEPING IMPACT ON TRACK

RISK IN PHILANTHROPY

A FRAMEWORK FOR EVALUATION

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Contents

Executive Summary

To help both grantmakers and NGOs better identify, assess, mitigate, and plan for risk in their portfolios, Open Road Alliance offers the following framework for evaluating risk. This brief framework is designed to provide grantmakers and NGOs with tools to conceptualize and describe risk and its implications within the scope of their philanthropic work.

Background:

The world is unpredictable. No amount of planning can prevent unscripted events from causing disruption. However, the philanthropic financial market is not structured to deal with the unexpected.

Most traditional grantmaking programs have inflexible, restrictive, slow, and unwieldy procedures for releasing funds. Many do not provide funds outside of their fixed grant cycles at all. These practices leave grantmakers unprepared to help non-profits who need funds quickly to manage contingencies.

This structure leaves well-conceived programs with little or no access to capital when unanticipated obstacles are encountered mid-implementation.

The result? Many projects stall or stop completely. Alternatively, the implementing NGO pushes forward on insufficient resources or diverts other allocated funds to the detriment of efficiency, effectiveness, and ultimately impact. The funders who invested in the project at the outset forfeit their social return alongside the non-profits and beneficiaries who may suffer even more severely.

In a community of philanthropists seeking to maximize impact through deploying capital, this structure is a poor investment proposition, and one that we can change.

Basic Premise:

The world is unpredictable and since it is impossible to anticipate all future events, our philanthropic investments carry risk, just as financial investments do. It behooves all actors (funders, NGOs, and implementing partners) to recognize, assess, and manage risk where possible.

Defining Terms:

Project Risk: The likelihood of disruptive events occurring which interfere with the successful conduct of a project or program managed by an NGO or other grantee.

Investment Risk: The likelihood that a funder will lose some or all of the intended social impact of their investment as a result of disruptive events that affect programs.

Real Examples of Project Risk:

Risk is a spectrum, not a binary value. Examples of project risk range from significantly harmful or not; likely or not; and predictable or not. Here are some examples of disruptive events that fall along this spectrum. All of these are real-life examples from Open Road's portfolio.

- A private donor pulls out post-commitment; fails to fulfill pledge
- Local partner fails to properly account for funds or turns out not to have the capacity to deliver as promised
- Government/Multi-lateral donor delays funding decision; delays payment; changes payment terms to reimbursable only, etc.
- Armed robbery and assault of staff
- Major flood during the dry season
- A used truck dies three years sooner than expected
- Parliament divides one state into two states
- A major donor is arrested for embezzlement, his assets frozen
- Fluctuations in exchange rates cause a project budget to lose 30% of its value



Assessing and Mitigating Risk

In order to avoid the potential harmful consequences of such events, Open Road Alliance advocates for grantmakers and NGOs to take a pro-active approach to assessing and mitigating risk at the earliest stages of project design and the RFP process. Open Road recommends the following basic steps to assess and mitigate risk involved in each initiative.

Basic Steps:

- **Identify** potential risks through direct conversation, past experience and SWOT analysis
- **Evaluate** identified risks according to probability of occurrence and severity of harm
- Determine whether the risk can be mitigated—if not, plan for contingencies

Assessing risk balances two considerations:

1. The **probability** that a particular event will occur.
2. The **severity of harm** resulting if such an event does occur.

We can map these two considerations on the matrix below.

Severity of Harm	Probability of Occurrence		
	High	Moderate	Low
Severe	D	B	A
Moderate		C	E
Low	F		

We can then map different risk scenarios against this matrix. For example:

A. Major flood during the dry season
B. Delayed grant payment jeopardizes payroll
C. Local partner mismanages funds
D. Rebels attack
E. Co-worker steals from petty cash
F. Co-worker steals lunch from break room refrigerator

Risk Mitigation: Influence and Control

After settling on an estimate of the probability and severity of potential risk, the next step is determining how much influence and control a funder or NGO can exert and whether it is worth the effort. Can the project actors reduce the probability of negative events occurring or reduce the severity of harm should they occur? This third variable should cause all parties to think carefully about how they can plan for and ward off probable disruptive events.

For example:

Project Risk: Local partner will mismanage funds

Degree of Influence: If identified in advance as a potential risk, there is a significant level of influence that the actors have over the likelihood of this occurring. Preventative steps include providing financial training for the receiving partner, tightly structured financial protocols, heightened accounting oversight, etc.

Control or influence is not to be confused with probability or predictability. Just because you can anticipate a potential risk, doesn't mean you can influence it.

For example:

Project Risk: Rebel attack in Eastern DRC

Probability of Occurrence: High

Degree of Influence: In some regions, like Eastern DRC, the probability of a rebel attack may be high and therefore somewhat predictable. However, none of the actors involved can prevent it from happening.

Moreover, as demonstrated in the examples on page two, some risks—like a truck breaking down—may seem more probable in hindsight than at the time of the project planning. Thus, while measures such as regular truck maintenance can influence the likelihood of a truck breaking down, they are not necessarily sufficient to ensure success.

As mentioned earlier, risk is not a binary value but a spectrum of possibility. In a similar manner, predicting risk in philanthropic projects cannot currently be determined through mathematic equations.[1] In reality determining what is or isn't in your control, and what is of high or low probability and severity is more art (based on experience) than science. However, we believe that talking these scenarios through in advance increases the probability of good outcomes.

1. The private sector, particularly the insurance sector, has spent decades building, testing and refining algorithms and other measures of risk. Yet, this level of actuarial accounting does not yet exist in philanthropy.

Given three variables—probability of occurrence, severity of harm, and level of influence and control—it is useful to try and mitigate when risks are:

- ➤ Moderate to High Severity of Harm
- ➤ Moderate to High Probability of Occurrence *and*
- ➤ Moderate to High degree of influence

Some basic mitigation techniques include:

- ➤ Identify project risks
- ➤ Adjust project plans, timelines, and/or budgets
- ➤ Consider additional training, partners, or resources
- ➤ Adjust expectations



Risk Contingency Planning

When identified risks are less predictable or cannot be managed through advance planning, grantmakers and NGOs should consider creating *contingency plans*. Contingency plans kick in after the disruptive event(s) have occurred.

For example:

Potential Risk: Parliament divides a state into two

Probability of Occurrence: Very Low

Degree of Influence: Very Low

Possible Mitigation Activities: None. Neither a grantmaker nor NGO can control parliament. Even members of parliament can't control parliament. Moreover, the probability of this happening is very low to the point of total unpredictability.

Try to create contingency plans when risks are:

- Moderate to High Severity of Harm
- Low Probability of Occurrence *and/or*
- Low degree of influence

Creating effective contingency plans requires advance planning and decision-making both internally and between partners. Some contingency planning techniques to consider include:

- Funder sets aside $X or X% of project budget for contingencies
- NGO budgets $X for contingencies in original project budget, justifying this amount within the larger budget narrative
- Pre-identify areas of flexibility within timelines, project scope, or budget allocations
- Pre-identify additional resources (financial, personnel, partners, training) that can be applied as needed
- Pre-establish channels of communication and decision-making protocols in the event of contingency risks
- Adjust expectations

It's important to notice that none of these contingency planning techniques are scenario-specific but rather speak to creating processes and policies that enable the actors involved to be flexible, adaptable, and responsive in the face of unpredictability and/or a low degree of influence. Through these practices, a given project is thereby 'insured' against a whole variety of potential disruptive events. With thorough contingency protocols both project and investor risk as a whole can be reduced.

For example:

Potential Risk: Currency exchange fluctuation decrease the value of an international grant.

Mitigation Activity: None. You can't control currency fluctuations or international markets.

Contingency Activity: Set aside additional funds in the grant making budget to hedge against potential fluctuations. Only release the funds if/as needed.

Actionable Steps for Managing Risk

1. **Ask** your grantees about the potential risks that their project could face; as an NGO
2. **Tell** your donors about potential risks, even if they don't ask
3. **Talk** with grantees/funders, potential grantees/funders and other relevant partners (joint-funders, implementing NGOs, local and government partners) about what can be mitigated and what may require contingency planning. Have this conversation before project activities begin.
4. **Plan** for contingencies**:** What happens if…? Create and document a process for
    a. **Communication:** who is in charge of telling whom what?
    b. **Decision-making:** how will decisions be made and what will the timeline be?
    c. **Action:** who is responsible for providing additional resources/time/training/scope adjustments/etc.? Do the relevant partners have the necessary structures in place to implement contingency plans?

All funders and NGOs want to see their projects and investments succeed. We are united by a common desire to create impact, solve problems, and leave this world a better place than we found it. But the altruism and generosity that motivates our work does not change the harsher landscape that we operate in.

Risk is real. It needs to be acknowledged by funders and NGOs, and incorporated in the grant application, planning and budgeting process. We hope that this framework begins to provide both funders and NGOs with the tools and vocabulary necessary to put risk squarely on the table and prominently on the agenda.