

# NPO Governance, Risk Management, Compliance and Internal controls

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# NPO Governance

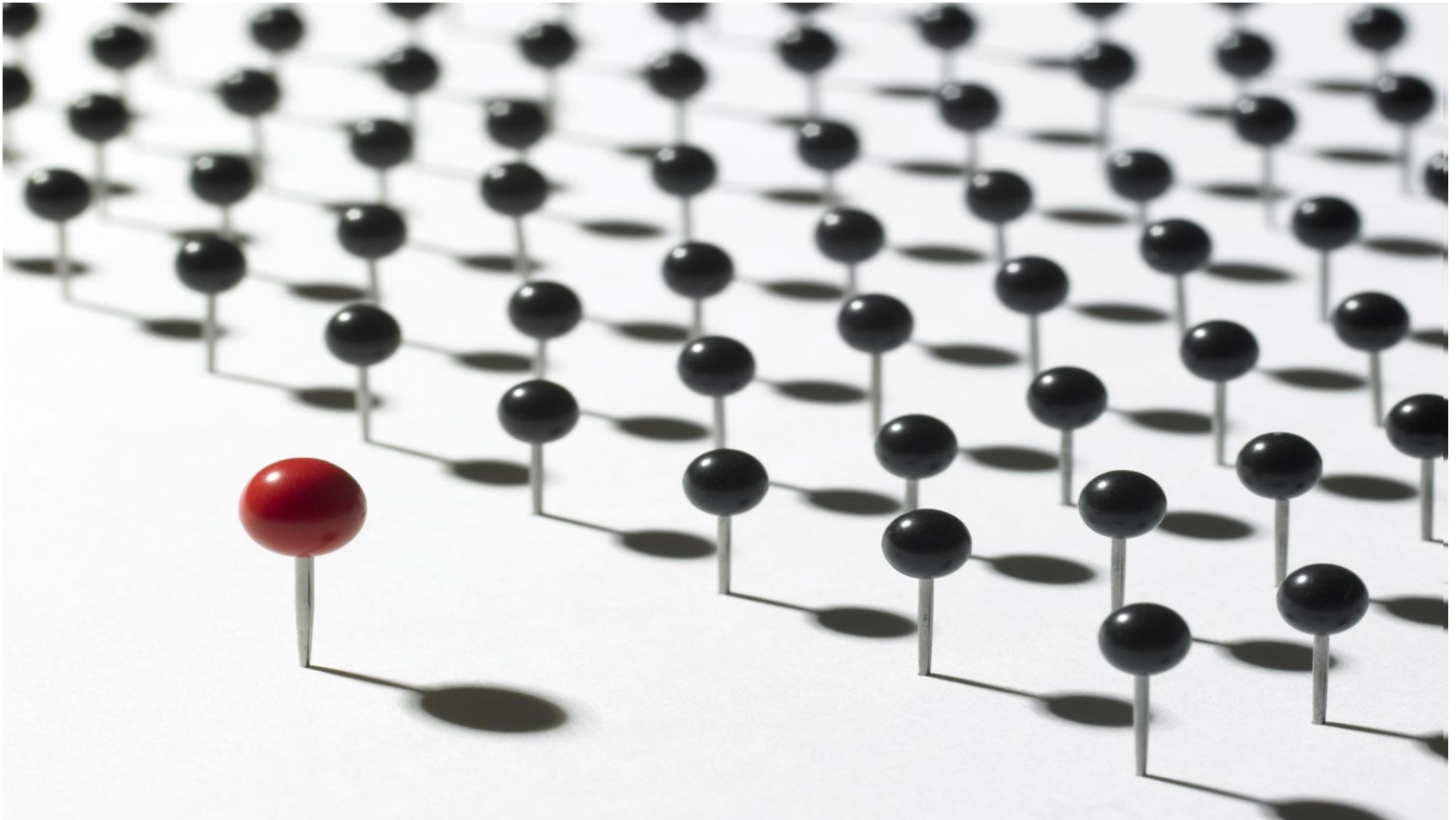


# What is Governance?



- ❑ Governance relates to decisions that define expectations, grant power, and verify performance.
- ❑ Regarding NPOs, governance relates to consistent leadership, management, cohesive policies, processes and decision-rights for a given area of responsibility.

# What is good Governance?



# Good Governance

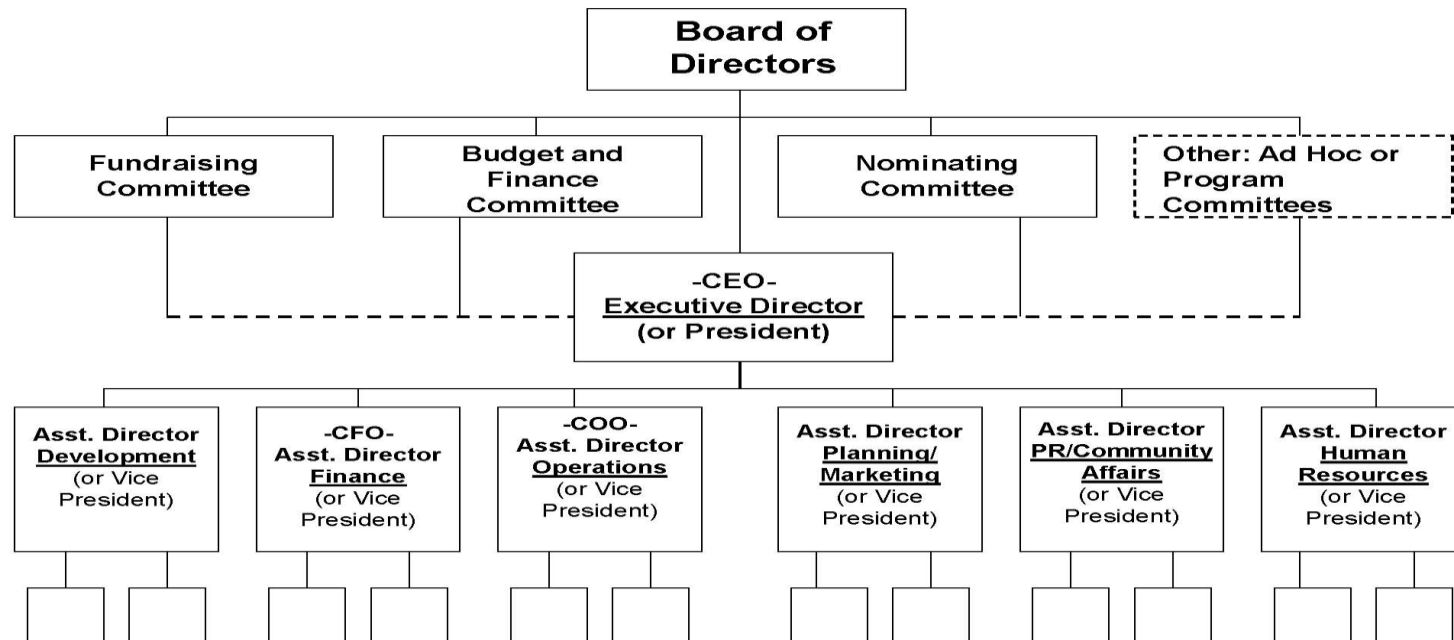


- ❑ Nonprofit board governance is the combination of systems, guidelines, and processes used to make decisions, hold decision makers accountable, and act.
- ❑ Good governance is crucial for a nonprofit to not only effective, but to attract the kind of board members, volunteers, and staff that make the organization stronger over time.

# Sample Structure for NPO



## Traditional Nonprofit Organizational Structure



# Principles of Nonprofit Governance



❑ Nonprofit governance is linked with several basic principles that are inherent to the nature and purpose of nonprofit organizations.



# Principles of Nonprofit Governance cont..



## ☐ Independence and commitment

Nonprofit organizations must have a committed board of directors that is independent in thinking and decision making.

## ☐ Fairness and equity for stakeholders

Boards of directors must ensure that all stakeholders are treated in a fair and equitable manner.

# Principles of Nonprofit Governance cont..



## □ Accountability to the public

Nonprofit organizations are publicly supported entities. Therefore, they are accountable to both internal (members, beneficiaries, employees, volunteers) and external stakeholders (donors, local communities, suppliers, creditors, policy makers, regulating agencies)

# Principles of Nonprofit Governance cont..



## □ Transparency:

Nonprofit organizations must disclose information about the roles of stakeholders in their operations, the outcomes related to such operations, and the financial statements that clarify the use of financial resources received from the public (e.g., donations, grants, endowments, etc).

# Principles of Nonprofit Governance cont..



## ❑ Ethical conduct:

Board members of nonprofit organizations should be community members and citizens of high ethical standards.

NPO must develop and enforce a code of ethical conduct, especially with respect to financial management, service delivery, and all operations and activities performed by board members, managers, staff, or volunteers

# Governance and Board of Directors



# Governance and Board of Directors Cont..



- ❑ Governance is more about the structures and process of decision making than the decision itself.
- ❑ Successful organizations maintain a governance system that enables them to make informed decisions when addressing their most complex problems or issues.

# Governance and Board of Directors Cont..



- ❑ The role of the board of directors is to ensure that a nonprofit organization is run, managed, and properly led with the aim to protect the interests of its constituencies.
- ❑ In other words, the board has a responsibility to hold managers and leaders accountable for their actions and their performance

# Governance and Board of Directors Cont..



- ❑ The metrics for such an endeavor reside in the existence of vision and mission statements that set the purpose of a particular nonprofit organization.
- ❑ The vision and mission must be translated into action plans, policies, programs, projects, and services that are carried out by management and staff



# Legal obligations of the board of directors



## ❑Fiduciary duty:

Board members of nonprofit organizations have a fiduciary duty to be trustworthy by acting in the best interests of their constituencies.

**A fiduciary is a person who, by law, is responsible for acting in the best interests of another person**

# Legal Obligations of the Board of directors cont..



## ❑ Duty of loyalty and fair dealing:

The duty of loyalty and fair dealing requires that a board member put organizational interests ahead of his/her own personal interests. In other words, board members should not use their position to gain personal advantages or make personal profits

# Legal obligations of the board of directors cont..



## ❑ Duty of care:

Board members are expected to carry out the business of a nonprofit organization with the reasonable care of any prudent individual.

# Legal obligations of the board of directors cont..



## ❑ Duty of supervision and accountability:

Directors should exercise their oversight responsibilities with a high level of effectiveness. Effective oversight starts with the adoption of policies of ethics and accountability that set standards of behaviors for board members, the executive director, and managers

# Board Duties as a good governance



- ☐ Establish, review, and approve organizational budgets
- ☐ Approve major or significant financial transactions
- ☐ Review auditing and accounting policies and practices
- ☐ Establish benchmarks to measure organizational performance
- ☐ Set executive compensations
- ☐ Contribute to fund-raising, advocacy, and collaborations or partnerships for organizational growth and financial sustainability

# Governance and Executive Director Selection and Evaluation.



## ❑ Board membership:

Recruitment, orientation, education, and development of board leadership.

## ❑ Selection and evaluation

Of CEO who, in turn, becomes the organization's manager. The chief executive makes day-to-day and standard management and marketing decisions without interference.

# Risk Management



Board decision-making is informed by an understanding of risk and how it is managed.

- ❑ The board oversees a risk management framework that aligns to the purpose and strategy
- ❑ Directors seek and are provided with information about risk and how it is managed
- ❑ The board periodically reviews the risk management framework.

# Risk Management Cont..



Risk is inherent in all human endeavors – including in the activities of organizations.

The role of the board is to understand the organization's risk, to make decisions based on this understanding and to oversee a framework that manages risk on an ongoing basis.

**Risk is not something to be avoided, but to be understood and leveraged in pursuit of an organization's purpose.**



# Risk is everywhere



# What is Risk?



- ❑ The International Organization for Standardization (ISO) defines risk as “the effect of uncertainty on objectives”
- ❑ Importantly, risk is not inherently bad. It arises because the future is unknowable and therefore the outcomes of decisions are always uncertain to Some extent.
- ❑ **USAID withdrawing funds unexpectedly**

# All decisions are based on assumptions about



- ❑ Internal factors (such as structure, staff skills and resource availability);
- ❑ External factors (such as the regulatory environment, funding availability, interest rates); and
- ❑ Wider factors (such as political changes, public sentiment about donations, or climate change).

# What is a risk management framework?



❑ The way that organizations take uncertainty into account when they make decisions is called ‘**risk management.**’ The goal of risk management is to increase the certainty that a decision’s intended outcome will be achieved. It involves the identification, evaluation and prioritization of risks.



# Risk Management



- ❑ Risk management should not be considered as a discrete activity. Rather, it should be embedded in the practices, processes and policies within an organization that are concerned with making decisions and ensuring that these decisions continue to be valid.

# Risk Management



However, organizations can adopt more formal processes to facilitate better management of risk. This is called developing a risk management framework.

**Risk management is a process of undertaking coordinated activities to control or reduce risk.**

# Risk Management Framework



❑ A risk management framework is a set of components that provide the foundations and organizational arrangements for designing, implementing, monitoring, reviewing and continually improving risk management throughout the organization.

# Sample Risk Framework

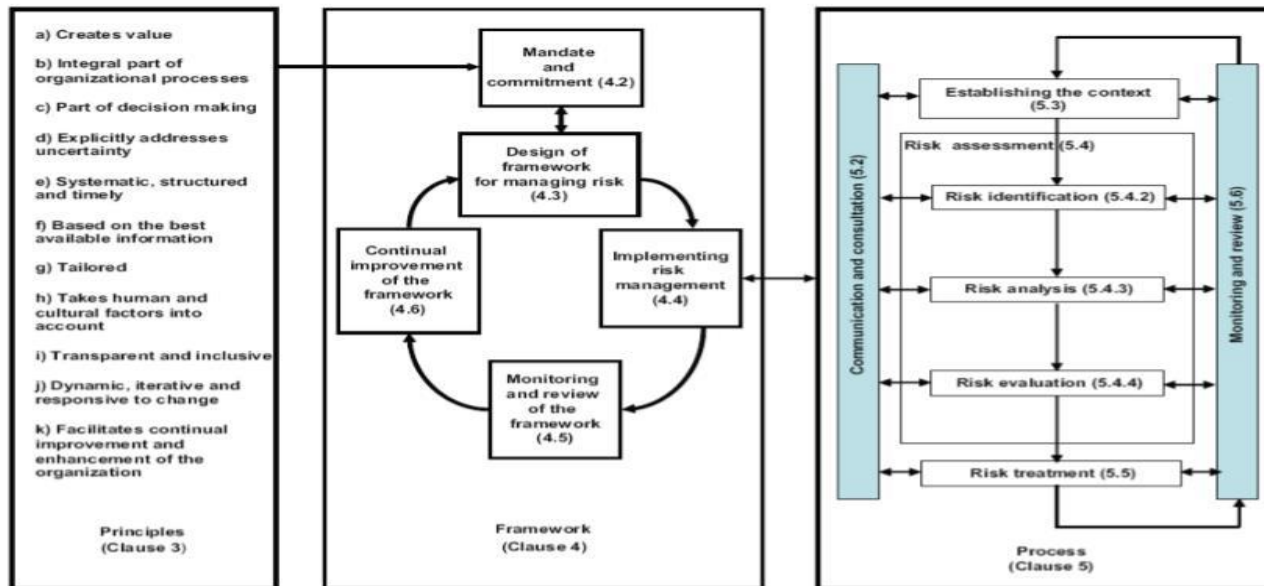




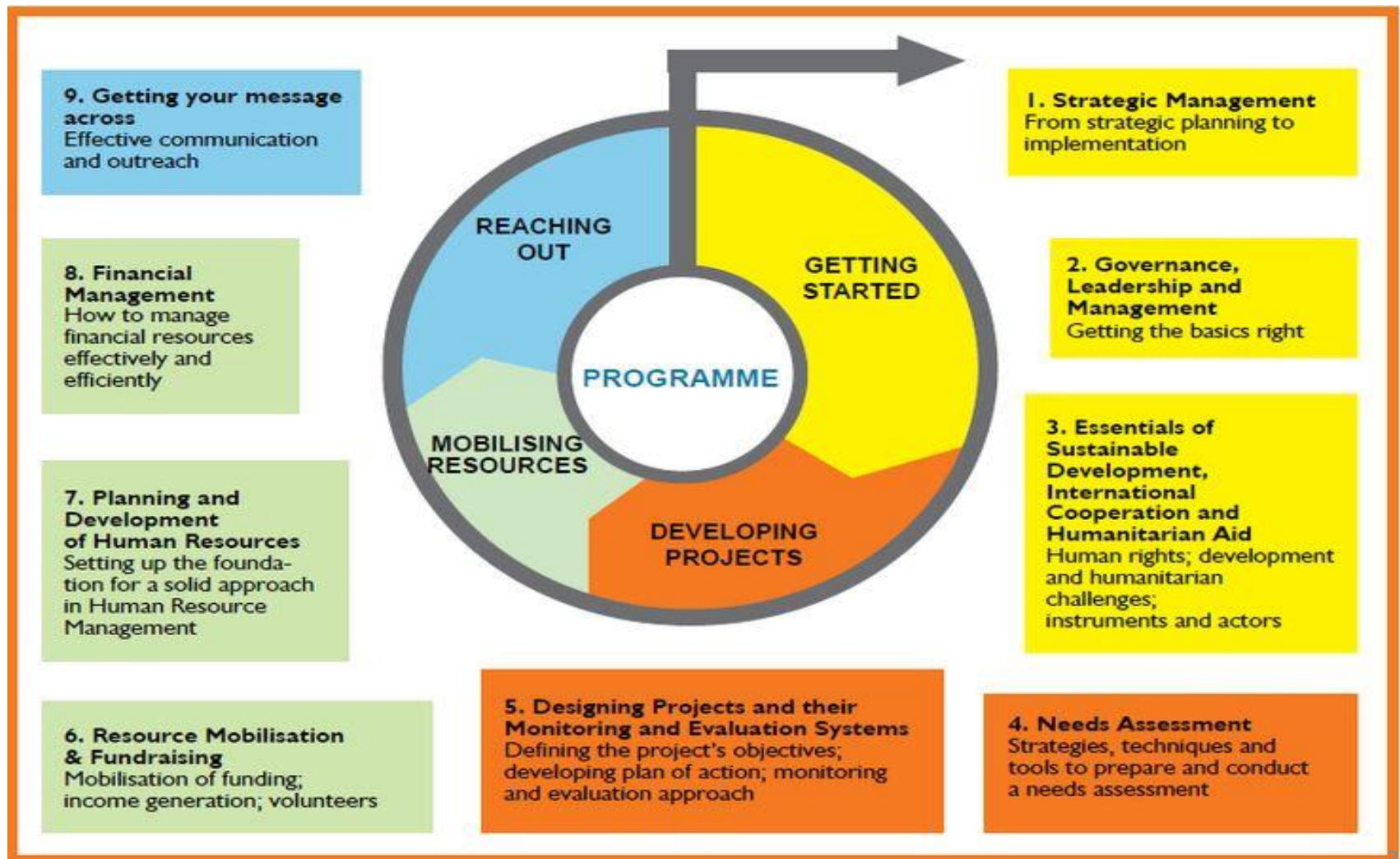
# Detailed Risk Management Framework



## Risk Management Framework



# Risk management for NPO



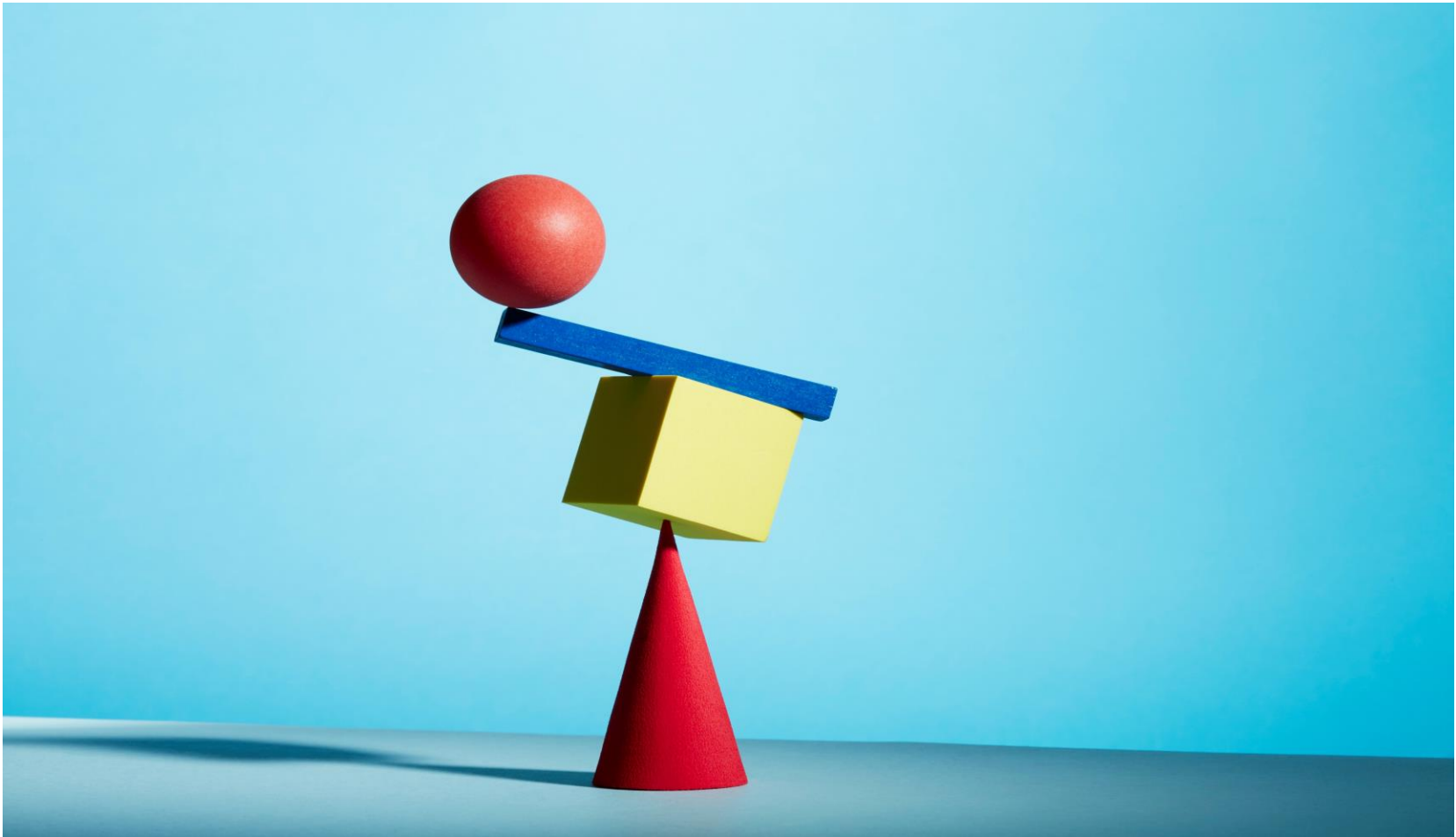
# Risk Matrix



Risk Matrix

		Consequence				
		Insignificant 1	Minor 2	Moderate 3	Major 4	Catastrophic 5
Likelihood	A Almost Certain	High	High	Extreme	Extreme	Extreme
	B Likely	Moderate	High	High	Extreme	Extreme
	C Moderate	Low	Moderate	High	Extreme	Extreme
	D Unlikely	Low	Low	Moderate	High	Extreme
	E Rare	Low	Low	Moderate	High	High

# Why do you need to manage risk?



# Why do you need to manage risk? Cont..



Risk management is a good practice. It helps an organization make more efficient use of resources, increase performance and minimize harm to staff and beneficiaries.

# Benefits of Risk management



- ☐ Reduce the likelihood of potentially costly surprises
- ☐ Prepare for challenging events and improve overall resilience
- ☐ Improve the quality of decision making at all levels
- ☐ Improve planning process
- ☐ Increase performance – **no funds to be returned**

# Types of Risks



<b>Contextual Risks</b>	External and outside organization e.g., Natural disasters, terrorisms , lack of public infrastructure
<b>Programmatic Risks</b>	Relates to how program projects are designed and implemented- not meeting beneficiaries needs or turns out to be disastrous to the community
<b>Organizational Risks</b>	Relates to the organization such as security and safety of staff, Reputation etc



# Risk Appetite





# Risk Appetite Cont..



- ❑ Risk appetite is the level of risks an organization is prepared to accept or pursue.
- ❑ In general organizations are more likely to have a n appetite for low level risks than high level risks but the decision is based on each individual organization.

# Risk Mitigations; Recommendations



- ❑ Build risk mitigation and risk co-ownership into contracts
- ❑ Broaden the partner management function
- ❑ Do not compromise staff safety to meet partnership expectations.
- ❑ Include force majeure clauses in awards to proactively allocate and share risks between donor, prime award recipient, and any sub-awardee

# Risk Mitigations; Recommendations Cont..



- ❑ Act as partner, not police not partners and awardees
- ❑ Ensure partners' administrative costs are covered
- ❑ Donors should cover the additional costs of risk management and compliance requirements in high-risk settings by including additional, field-based indirect cost recovery lines in project budgets.
- ❑ ETC

# Make Risk management part of you



# Compliance



It's always a privilege to work with NPOs. What's so striking about all of them is their people. They have a calling; they are on **a mission to improve some aspect of the world.**

It doesn't matter whether they are **helping children, working to restore human rights or providing humanitarian aid to disaster victims, these people are committed to their causes**



# Kudos to NPOs



# Compliance Cont..



Unfortunately, pure belief in their cause is not enough. **Doing “good” in the world requires funding.**

And funding always comes with **strings attached**. There are always expectations to meet and expectations to manage. How well an NPO manages these expectations directly relates to their success as an organization.

# Compliance Cont..



You would think that an NPO would be measured purely on their ability to carry out their mission. **Big NO**

When you consider the **strings attached with funding**, most funding sources want reports, not just on successful efforts, but also on how and where the money was spent.



# Compliance Cont..



This is where compliance and reporting come in. By keeping accurate records of every transaction, NPO's can report on exactly how money was spent.

This reporting enables them to comply with the commitments usually associated with funding. **Sadly, this is the one area where most NGO's fail.**

# Non- Compliance to A tax man



# Areas of Compliance



# Taxes and Taxation



# Taxes and Taxation Cont..



- ☐ WHT is due by the 20th day of the month following the month of deduction.
- ☐ Upon deduction and payment of WHT, a person is required to keep a record of the name of the payee, PIN, gross amount paid, nature of payment and amount of tax deducted
- ☐ Withholding tax accounting is now supposed to be fully done through iTax platform
- ☐ Upon paying the tax, the iTax platform should generate a certificate that should be sent to the payee to enable the payee claim credit against income tax

# Penalties and interest for non-compliance



- ❑ For purposes of recovery of tax, withholding tax is demanded from the payer as though it were the tax of the payer (recall WHT belongs to PAYEE and not PAYER)
- ❑ A penalty of 20% should apply for late payment of withholding tax –up until 9 June 2016, the penalty used to be 10% but capped to KES 1 million
- ❑ Late payment interest of 1% per month is chargeable on any tax remaining unpaid after the due date –the late payment interest charged is capped to the principal tax involved

# Penalties and interest for Complex issues/ KRA audit issues



- ☐ **The tax point (actual payment vs accrual)** –Should w/tax be based on actual payment or accrual?
- ☐ **Mixed supplies** –WHT applies only to services. What happens where fees to be paid under a contract relate to both goods and services?
- ☐ **Disbursements and reimbursements**—should w/tax be based on disbursements and reimbursements? What is the difference between the two?
- ☐ **Gross up problem** –where a contract is negotiated net of tax, should w/tax be based on the contract fee or should it be grossed up?
- ☐ **Payment in kind** –How should w/tax be accounted if payment is made in kind?

# WHT- Done





# Three



# Value Added Tax



- ❑ Introduction
- ❑ VAT status of supplies by NPOs
- ❑ VAT status of supplies to NPOs
- ❑ Process of applying for zero rating/exemption
- ❑ Potential VAT issues for NPOs

# Introduction



- ❑ VAT is chargeable on taxable supplies or importation of taxable goods and services
- ❑ Applicable VAT rates; zero or 16%
- ❑ Certain items also exempt from VAT
- ❑ Registration threshold –taxable supplies of KES 5 million (app. USD 50,000)
- ❑ Registered person liable to charge and account for VAT on taxable supplies

# VAT status of supplies by NPOs



## Exempt supplies?

- ❑ The supply of social welfare services by charitable organizations is exempt. This is on condition that:
  1. The charitable organizations are registered as such; or
  2. Such charitable organizations are exempted from registration by the Registrar of Societies or by the Non-Governmental Organizations Co-ordination Board and their income is exempt from VAT under Para 10 of the First Schedule to the Income Tax Act (ITA).

# VAT status of supplies by NPOs



## Taxable supplies?

- ☐ VAT is applicable where social welfare services are rendered by way of business.
- ☐ Business defined to include:
  1. Trade, commerce or manufacture, profession, vocation or occupation;
  2. Any other activity in the nature of trade, commerce or manufacture, profession, vocation or occupation;
  3. Any activity carried on by a person continuously or regularly, whether or not for gain or profit and which involves in part or whole, the supply of goods or services for consideration;
  4. A supply of property by way of lease, license, or similar arrangement.
- ☐ Important to note that, while ITA may exempt gains or profits from business, VAT Act considers such income as subject to VAT.

# VAT-Kwisha



# In Summary



- ☐ Tax apply to all
- ☐ Be vigilant with new regulations
- ☐ Consult where necessary
- ☐ Attend refresher courses such as this one
- ☐ Don't be a lone ranger- share and shout
- ☐ ETC

# HURAA!





# Compliance to NGO Coordination Board



- Bank openings and operations
- Signatories to all banks
- Work permits for International staff
- Annual Returns Form 14
- Audited accounts within 3 months of year end

# Donor Requirements



- Donor requirements vary and are in all donor contracts.
- The best practice is to do a checklist before signing contracts on all requirements.
- Projects audits
- Monitoring and evaluation both mid and final
- Reports as required by donors
- Take note of disallowable in all contracts

# Thank you



# THE END

