

## FOCUS

## Aligning International Best Practices for Higher Accountability & Relevancy

### Interview with Lieut-Colonel Ian Swan, Officer Commanding of The Salvation Army Hong Kong and Macau Command

Lieut-Colonel Ian Swan was commissioned as an officer of The Salvation Army (the Army) in 1987 and has been serving this international church and NGO ever since. He first came to Hong Kong in 1996 and was later appointed as the Officer Commanding for the Army's Hong Kong and Macau Command in 2013.

The Army was found in 1865 and reached Hong Kong in 1930. With the International Headquarters in London, UK governing Territories and Commands at work in over 130 countries and areas, the Army is obliged to create international governance standards to carry out its mission as "an evangelical part of the universal Christian Church". Governance practices with stringent documentations have been established very early on. "I can show you over 30 years of our strategic plans. It has always been a requirement," Lieut-Colonel Ian said. "Every three years, we are audited internationally. Annually, we have to report on the goals set for the year, and explain the challenges and achievements." There are also international "non-negotiable principles" on board composition including compliance to local legislations, gender equity, and generational distribution. The Army has a Command Governance Council Charter for each Command to ensure newly appointed leaders understand these requirements and are able to maintain an international and localized governance structure with smooth succession.

The unique structure of the Army is based upon a military model. Traditionally, the leadership of the Army are either appointed or elected within its hierarchy. In the then Command Finance Council of Hong Kong, the Officer Commanding was the highest level of policy maker with the support of other senior members of the Command, reporting directly to the headquarters. This model was effective for quick decision making, but focused mainly on financial concerns.

Being back to Hong Kong the second time as the Officer Commanding, Lieut-Colonel Ian felt that there were voices calling for higher standard of NGOs' accountability. "The public want NGOs to do better in due diligence and compliance. The bottom line is a trust issue. For us, because The Salvation Army has been working for 150 years, we are not prepared to sacrifice our reputation. Procedures and policies must be in place to protect the Army and individuals serving within the organization or on the board."

To celebrate its 150<sup>th</sup> anniversary, the Army started the "Accountability Movement" internationally in 2016 to improve its overall efficiency and relevancy. The Hong Kong and Macau Command then went through a rigorous review of its governance structure. A new "Command Governance Council" was formed in January 2018 to increase diversity and accountability with representation of external stakeholders. "My mantra in the last two years' journey of renewal was not compliance but best practice," Lieut-Colonel Ian shared his beliefs.

In the process of uplifting international governance standards and promoting accountability, Lieut-Colonel Ian said that there was some resistance encountered. "Some of the traditionalists would say we have adopted a corporate model and given up some of the church values," he stated. "And I would say, no, that is why we have this document. Principles of good stewardship, mutual accountability and wise decision making are all key governance standards written in 'A Salvation Army Theology of Governance' with specific references to the Bible, explaining how good governance is consistent with gospel values of integrity, servanthood and transparency."

Lieut-Colonel Ian admitted that leading spiritual and mission renewal is challenging. "There are times that we have to make difficult decisions, but we still want to demonstrate that we recognize God." He reminded leaders to exercise good stewardship in using resources to make a difference, keep in mind that all the strategic plans and budgets will help street sleepers, young people, elderly and other people in need.



Lieut-Colonel Ian (the fifth from right) and the department heads and managers of the Hong Kong and Macau Command



Lieut-Colonel Ian's visit to Bradbury Home of Loving Kindness

# GOVERNANCE IN ACTION

## Reserve of NGOs – Building Financial Resilience for Sustainability

Lately there are public concerns on whether NGOs should keep reserve and what level of reserve should be maintained. In the Governance Forum organized by HKCSS in November 2018, accounting professionals shared their views on various issues related to NGO reserve. The discussions in the Forum were organized and presented here to enhance the public's understanding of the subject matter and to provide a reference for NGOs in managing reserve and formulating related policies.

### What is reserve?

In accounting practice, reserve is the asset after liabilities deducted. It is the resource that an organization accumulated and can be set aside for a particular purpose, e.g. renovation of premises. Reserve is a separate item shown in the balance sheet. When “reserve” was discussed in the Forum, the focus was on the “Survey on Financial Reserves of Social Service Agencies” jointly conducted by Deloitte China and HKCSS, and the information collected on Lump Sum Grant (LSG) reserve and general & non-designated reserve.

As stated in the “Quick Guide on Reserve Policy” published by the Hong Kong Institute of Certified Public Accountants (HKICPA), reserve can be used for emergency spending and future commitment.<sup>1</sup> Reserve allows organizations to meet unexpected needs without affecting the current and planned services. For instance, when donation approved is not released as scheduled, in responding to new service demand or paying non-budgeted expenses, organizations have to make use of reserve to cope with these situations. Reserve is also the cornerstone supporting long term development, providing resources for formulating strategic plan, ensuring sustainable and quality services for the clients.<sup>2</sup>

### Level of reserve

Given the importance of reserve to daily operation and long term development, how much reserve should NGOs maintain? There is no definite answer. Each agency has its unique mission, background, scale, services, income sources and distribution. The level of reserve to be maintained is subject to the operational needs of each agency.

Ms Melissa Fung, Partner, Risk Advisory of Deloitte China, shared the implications from the findings of the Survey.<sup>3</sup> A total of 100 agency members of the HKCSS responded to the Survey questionnaire, including both recipients of LSG from Social Welfare Department (SWD) and those which are not. On average, the agencies' LSG reserve can support related expenditure for three months. This indicates that agencies are compliant with the requirement on the maximum level of cumulative reserve at the financial year end stipulated in SWD's LSG Manual. Regarding the non-designated reserve, on average it can support agencies' related expenditure for 11.2 months, while the duration is 7.7 months and 12.7 months respectively for agencies with and without recurrent funding support. Ms Fung stated that this shows agencies without stable income from recurrent funding usually maintain a higher level of reserve to ensure continuity of services. Information from USA, UK and Australia also reveal that the reserve maintained by NGOs there are sufficient for 8 to 15 months' operation.



*Plenary Session of NGO Governance Forum 2018: Reserve for Stability & Sustainability*

<sup>1</sup> *CPA for NGOs Quick Guide Series: Reserve Policy*. Hong Kong Institute of Certified Public Accountants. Source: <https://governance.hkcss.org.hk/node/72>

<sup>2</sup> *Reserves and financial sustainability* (November 2018), Hong Kong Institute of Public Certified Accountants. Source: <https://governance.hkcss.org.hk/node/243>

<sup>3</sup> *Insights from the Survey on Financial Reserves of Social Service Agencies* (November 2018), Ms Melissa Fung, Partner, Risk Advisory, Deloitte China. Source: <https://governance.hkcss.org.hk/node/312>

# GOVERNANCE IN ACTION

## Planning and monitoring of reserve

Agencies need to plan and monitor the use of reserve prudently in order to make reserve performs its role effectively. Findings of the Survey show that 62% of the responding agencies have set up finance or investment committees to formulate reserve plan and decide on the use of reserve. Committee members come from accounting, financial and legal sectors, amongst which over 80% are accounting professionals.<sup>4</sup> They provide knowledge and experience from different expertise to enable agencies plan and use their reserve prudently.

In the process of making decision on reserve management, the responding agencies on average went through a 3-tier mechanism which includes the management and the board.<sup>5</sup> Such cautious procedure ensures proper check and balance, and is a good reference that worth adopting by our sector.

Ms Loretta Fong, Vice Chairman of the Finance and Administration Committee, Hong Kong Young Women's Christian Association, shared in the Forum their experience in reserve planning and management and the importance of reserve planning on agencies' sustainable development. She stated that the Finance and Administration Committee was set up under the Board, with members from independent professionals. The Committee regularly monitors and reviews the level and status of reserve to ensure they are effectively used.<sup>6</sup>

## Reserve policy

Reserve policy plays a critical role in agencies' financial governance. It explains to the public and stakeholders the prudent financial management of agencies, provides a well-justified explanation on the level of reserve, and demonstrates the agencies' financial capacity to sustain their mission pursuit. According to the Survey findings, more than 60% of the responding agencies have or are formulating policy on reserve management and investment. It demonstrates that they are striving for higher accountability and transparency.<sup>7</sup>

Mr Richard Tse, Chairman of Community Services Working Group, HKICPA, reminded agencies that reserve policy should be formulated in light of the actual financial status, direction of strategic development and the level of risk appetite, and that polices should be reviewed in appropriate time interval and updated regularly. The "Quick Guide on Reserve Policy" published by HKICPA suggests key steps in formulating reserve policy: 1) Stating the reasons for maintaining reserve, 2) Reviewing income and expenditure pattern, 3) Understanding and assessing financial impact on risk, 4) Determining the target reserve level, and 5) Communicating the reserve policy.<sup>8</sup> Mr Tse pointed out that disclosure of reserve policy could increase public confidence in the agencies, subsequently enhance their social and financial capital which is conducive to the organization's development.<sup>9</sup>

## Concluding remarks

Prudent financial management by the board and the management is crucial to agencies' sustainable and healthy growth and for them to create social impact. Reserve is a critical element in ensuring financial resilience. An appropriate level allows agencies to meet operational needs, pay for unexpected spending, and formulate long-term strategic plan.

<sup>4</sup> Ibid

<sup>5</sup> Ibid

<sup>6</sup> *Case sharing on setting reserves and investment policies* (November 2018), Ms Loretta Fong, Vice Chairman of Finance and Administration Committee, Hong Kong Young Women's Christian Association. Source: <https://governance.hkcss.org.hk/node/314>

<sup>7</sup> *Insights from the Survey on Financial Reserves of Social Service Agencies* (November 2018), Ms Melissa Fung, Partner, Risk Advisory, Deloitte China. Source: <https://governance.hkcss.org.hk/node/312>

<sup>8</sup> *CPA for NGOs Quick Guide Series: Reserve Policy*. Hong Kong Institute of Certified Public Accountants. Source: <https://governance.hkcss.org.hk/node/72>

<sup>9</sup> *Responses to the Key Findings of the Survey on Financial Reserves of Social Service Agencies* (November 2018), Mr Richard Tse, Chairman of Community Services Working Group, Hong Kong Institute of Certified Public Accountants. Source: <https://governance.hkcss.org.hk/node/313>

## UPCOMING ACTIVITIES

### Seminar on Compliance Requirements for Charities with Recognition of Tax Exemption Status under the Inland Revenue Ordinance

With 98% of our agency members being tax exempted charities, the Council has invited representatives of the Inland Revenue Department to update on the compliance requirements for tax exemption of charitable institutions at this upcoming seminar, including the definition of charitable purposes, requirements on governing instruments and Directors' remuneration, etc. The speakers will also share on other issues that charities should be aware of to retain the tax exemption status. Details as follows:

<b>Date:</b>	22 February 2019 (Friday)
<b>Time:</b>	6:30pm - 8:00pm
<b>Target:</b>	NGO Board and committee members (top priority), advisors, company secretaries, agency heads and senior management of HKCSS Agency Members

For event details and enrollment, please browse <https://governance.hkcss.org.hk/node/324>.

## SNAPSHOTS



### "NGO Governance Health Survey" Debriefing Sessions

A survey on "NGO Governance Health" was conducted in 2018 together with HKU and GAME. Debriefing sessions were held on 24, 25 and 29 January 2019 to introduce the governance health check tool, present the landscape findings and explain to the participating NGOs how to interpret the content of their individual reports. Around 200 participants had fruitful exchanges on various governance issues revealed in the survey.



### Governance Engagement Day

The first Governance Engagement Day was organized on 6 December 2018. It provided a platform for Rotarians from various professions to meet with the NGO representatives, enhancing their mutual understanding. Participating NGOs may consider inviting these professionals with the passion to serve the community to join them as consultants or Committee members so as to strengthen their governance capacity for long term development.