What Motivates Nonprofit Organizations to Implement Risk Management: A Comparative Analysis of Germany and the United Kingdom

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Abstract

In a time of global uncertainty, effective risk management has become a critical strategic issue in the commercial sector, and policy makers continue to focus on mechanisms to improve corporate governance and manage organizational risks. Despite these developments, there is little research on risk management in the nonprofit sector and factors associated with the implementation of an institutionalized risk management framework. Research is needed to identify key drivers and provide insights as to why some nonprofit organizations are responding to a changing environment by embracing a systematic approach to managing risks and others are not.

Drawing on an exploratory qualitative field study of 30 organizations, internal as well as external factors associated with the stage of risk management implementation are examined using a unique setting in which large nonprofit organizations in Germany and the United Kingdom are confronted with very different regulatory requirements. Building on an integrated framework of resource dependence and institutional theory the effects of coercive, normative and mimetic isomorphism are documented. Based on this analysis, some new directions for more advanced theoretical and empirical research about risk management in nonprofit organizations are briefly outlined.

Keywords: nonprofit, risk management, institutional theory, resource dependence, qualitative field study

1. Introduction

Effective management of risk is fundamental to the proper functioning of any organization. This is even more the case for organizations that operate in changing, or otherwise uncertain, environments and where the outcomes of decisions cannot be perfectly predicted. Even though objectives can differ greatly from one nonprofit organization to another, most organizations are faced with a complex and volatile social environment in their attempt to accomplish their mission (Greenlee & Tuckman, 2007; Grace, 2010; Young, 2009). As a result, nonprofits encounter risk in many different areas including financial, personnel, program and capital expenditure decisions (Young, 2009; Chew & Osborne, 2009).

Taking into consideration that the objectives of nonprofits are likely to be based on some form of mission continuation or expansion, a systematic approach to managing risks serves at least two purposes. First, nonprofits have an interest in protecting themselves against potential outcomes that could threaten their survival and their capacities to address their missions. To the extent that risk management is able to increase the prospects of survival for the organization, it reduces the costs of obtaining future funds (Grace, 2010; Greenlee & Tuckman, 2007). Second, as nonprofits consider alternative ways to address their mission and make strategic decisions, they may often find themselves in situations where the options which promise greatest impact also entail greater risk or are less certain. In this context, nonprofits need to find the “right” balance between the “return” they want to achieve and the risk they are willing to take (Benjamin, 2008; Young, 2009).

Despite the fact that the literature acknowledges that risk management can provide significant benefits to nonprofits, research is still in its early stages, and significantly, the individual driving forces behind the implementation of risk management in nonprofits as well as circum-

stances that favor and facilitate the adoption process are not clear (Greenlee & Tuckman, 2007; Benjamin, 2008; Young, 2009; Grace, 2010). Why do some nonprofits embrace risk management practices more readily than others and what internal and external factors motivate them to manage their risks systematically? Drawing on an integrated framework of institutional and resource dependence theory this article uses an empirical approach to explore organizational factors influencing the level of risk management adoption in nonprofits. Based on data gathered from 30 organizations in Germany and the United Kingdom it highlights the importance of regulatory requirements, sources of funding, strategic positioning and organizational size. Additionally a link between the degree of professionalism of the organization and stage of risk management implementation can be shown.

The first section of this article reviews the literature on risk management in nonprofits and factors associated with the adoption of risk management practices that have been studied in the for-profit arena. It highlights specific differences in the nonprofit and commercial settings, providing the foundation for needed adjustments. Based on the review of the existing literature an initial conceptual framework of possible influences on risk management in nonprofits is developed and theory-driven expectations are derived. The second section outlines the method and data used in the study. An analysis of relevant internal and external factors based on the exploratory study is described in the third section. The article concludes with a discussion on the practical implications of the findings for nonprofits and offers some directions for future research.

2. Background and research questions

2.1. Risk Management in Nonprofit Organizations

Over the past two decades an extensive body of literature has emerged on risk management in for-profit organizations (Haslett, 2010; Power, 2010). However, as Greenlee and Tuck-

man (2007) highlight, the application of for-profit risk management techniques to the nonprofit sector is in its early stages and more research is required to fully understand how risk affects nonprofit organizations and to develop tools that nonprofit managers need for managing risk. Grace (2010) and Young (2009) argue that the current body of applied research on risk management in the for-profit field does not necessarily translate well into the nonprofit arena for at least three reasons: (1) discrepancies in risk perception, (2) performance measurement and (3) different management control mechanisms.

Determining the "acceptable" level of risk tolerance is a non-trivial exercise in a commercial setting. What makes it even more problematic and difficult in the nonprofit arena is the definition and measurement of success metrics and how to evaluate the trade-off that exists between "return" and the cost of risk (Sawhill & Williamson, 2001; Kaplan, 2001; Grace, 2010). In many areas of nonprofit decision making, the financial return does not matter as much as achievements measured in terms of social or mission impact which may be less clear or tangible. Consequently the notion of thinking in terms of risk vs. return is not as natural as in the for-profit arena (Grace, 2010; Young, 2009).

Greenlee and Tuckman (2007) point out that an additional layer of complexity stems from the absence of both shareholders and a widely agreed upon bottom line in the nonprofit world. In a for-profit setting, shareholders as owners bear the risk of the business activities and ultimately hold executives responsible for managing their assets to achieve maximum financial returns within clearly defined bounds of risk tolerance (Culp, 2002; Fraser & Simkins, 2009; Merna & Al-Thani, 2008). In contrast, in a nonprofit neither executive staff nor the trustees bear the risk of actions taken and are left to interpret what is appropriate in terms of the risks they

should assume and the levels of social return they should seek (Young, 2009; Scanlan & Dillon-Merrill, 2006; LeRoux & Wright, 2010).

Although research identified significant differences between nonprofits and for-profit organizations that affect risk management implementation, the existing literature on risk management in nonprofits is fragmented and not focused on the broader issue of risk in nonprofit organizations. In many cases managing risks is more a “by-product” of research in a variety of other areas of nonprofit decision making (Young, 2009; Grace, 2010). One area is the literature on nonprofit governance, drawing on the prudent deployment of resources to achieve the organization’s purposes. Ostrower and Stone (2006) identify two normative models of nonprofit governance: (1) the corporate model, being more sympathetic to strategic risk taking and (2) the stewardship model, with a strong tendency to asset preservation. Drawing on the idea of “safeguarding” as a guiding principle for managing risks in nonprofits, the tenor of much of the literature suggests the pervasiveness of the “asset preservation” view, with its emphasis on reducing risk rather than trading it against potential gains (Bielefeld, 1992; Gibelman & Gelman, 1999; Overton, 2002; Herman, 2004). Along this line of thinking, Overton (2002) concludes “insurance is a possible solution to the problem of risk” (Overton 2002). This negative and preventative approach to risk may be useful in instances where risks can be reduced without loss in performance, impact or contribution to mission. However, viewing risk as a problem and reliance on risk reduction alone may have the consequence of incurring large opportunity costs because this may preclude focusing on decisions that may require accepting certain levels of risk in order to achieve desired goals or gains (Young, 2009).

More recently, research in the nonprofit field has started to adopt a strategic view of managing uncertainties and risks, that nonprofits face (Brown & Iverson, 2004; Fremont-Smith,

2004; Young, 2009; Grace, 2010). Still, more research is needed to understand motives, influencing factors and the strategic weighing of risks and benefits that allow organizations to have the greatest impact on their missions. This would allow then the development of a more proactive approach to risk management in nonprofit organizations.

2.2. Key drivers for Risk Management in For-Profit Arena

There has been an increasing body of literature studying key drivers and determinants of risk management adoption. However, with the exception of one study (Kleffner et al., 2003), thus far no empirical research has been conducted that includes nonprofit organizations, and in the existing study, nonprofits are only a small subcategory in the broader sample of firms analyzed. Still the research in the commercial setting provides a rich background and starting point for a study of factors in the nonprofit field. The academic literature can be classified into two main research streams based on the research methods applied.

The first stream of empirical studies is based on large sample cross-sectional research methods and has identified *financial leverage* (Liebenberg & Hoyt, 2003; Pagach & Warr, 2011; Ellul & Yerramilli, 2010), *strategy* including the existence of a Chief Risk Officer (Liebenberg & Hoyt, 2003; Kleffner et al., 2003; Ellul & Yerramilli, 2010; Pagach & Warr, 2011) and *organizational size* (Beasley et al., 2005; Gordon et al., 2009; Ellul & Yerramilli, 2010; Hoyt & Liebenberg, 2011; Pagach & Warr, 2011; Paape & Speklé, 2012) as internal factors associated with risk management adoption. Although the majority of studies support the intuitive hypothesis that risk management is related to size, some research yields different conclusions and does not find support for a significant impact of organizational size (Collier et al., 2007; Razali et al., 2011; McShane et al., 2011). Drawing on the hypothesis that strong corporate governance agents are likely to advocate for risk management implementation, Kleffner et al. (2003) and Beasley et

al. (2005) found that support from the executive staff was associated with the extent of risk management implementation. Studies of external factors for risk management adoption, such as *institutional ownership* and *shareholder influence*, have yielded mixed results (Kleffner et al., 2003; Eckles et al., 2011; Pagach & Warr, 2011; Paape & Speklé, 2012). The same is true for *regulatory pressure* as another external factor (Kleffner et al., 2003; Collier et al., 2007; Paape & Speklé, 2012). Kleffner et al. (2003) reported that Canadian companies cited compliance with stock exchange guidelines as the third most important reason for their risk management adoption indicating a relationship between regulatory requirements and risk management implementation. Paape and Speklé (2012) also found that stock exchange listing helped to explain risk management adoption, but their analysis does not lend support for a supposed influence of corporate governance regulation. Along similar lines Collier et al. (2007) found only limited support for the importance of regulatory requirements in the context of risk management implementation in exchange-traded companies in the United Kingdom.

The second, more recently emerging, research stream uses small-sample case and field studies to understand risk management as an organizational and social practice. This research is critical of quantitative empirical studies for their failure to explain the actual mechanism through which their explanatory variables affect proposed outcome variables (Hall et al., 2012; Mikes & Kaplan 2013). Mikes and Kaplan (2013) argue that large sample cross-sectional studies focus on the adoption, or not, of a particular risk management framework, ignoring the impact of people and leadership in the process of risk management implementation. However, since people are the ones that identify, analyze and act on risk information, organizational and cultural disparities can cause companies to implement and use their risk management function very differently (Mikes, 2009; Yaraghi & Langhe, 2011; Mikes & Kaplan 2013). In addition, risk experts do not operate

in a vacuum, but interact and depend on decision makers requiring a more in-depth analysis of risk management processes. Drawing on three comparative case studies Arena et al. (2010) document a continuous and evolving interaction between existing organizational management practices and risk management. Mikes (2009, 2011) as well as Yaraghi and Langhe (2011) seek to explicate and understand the reasons for different risk management implementation, studying cultural variances including the roles of risk experts, firm strategy and organizational structure. Against this background, Mikes and Kaplan (2013) are proposing a contingency approach for risk management as a theoretical framework.

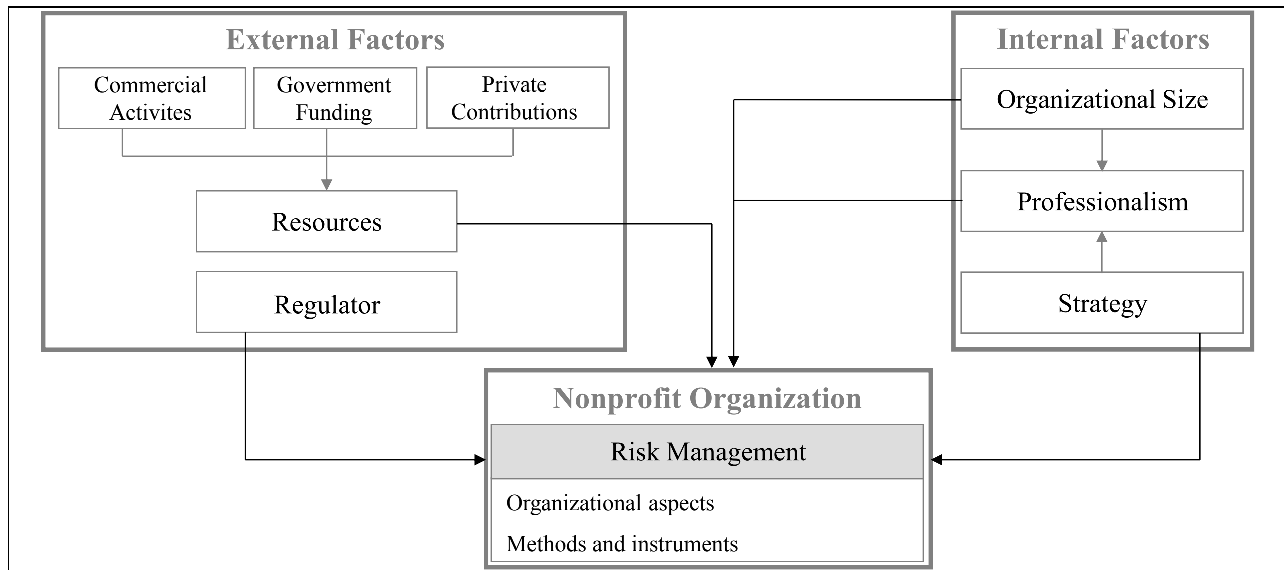
Although this second body of research makes a first attempt to link risk management practices with meta theory and has enhanced the understanding of processes and mechanisms that influence risk management adoption, as with the large sample cross-sectional studies, field researchers struggle to produce persuasive comparisons across their multiple studies and observe findings that can be generalized. Due to the complexity of the different risks faced by an organization, the practices observed in one firm differ substantially from those observed elsewhere (Mikes & Kaplan 2013).

2.3. Potential Factors Influencing Risk Management in Nonprofits

Since both streams of existing literature struggle to explain the variety of risk-management practices in the business arena with some contradictory results, it can be expected that findings seen through the lenses of the for-profit world are a starting point, but do not necessarily translate well into the nonprofit sector. A comprehensive model would have to take into consideration the highlighted differences in conceptual requirements for nonprofit risk management as well as their unique financing considerations and funding sources (Kearns et al., 2012; LeRoux & Wright, 2010).

With regard to funding, literature has identified three major revenue sources for nonprofits: (1) private contributions, (2) government funding, and (3) commercial activities (Tuckman & Chang, 1991; Froelich, 1999; Trussel, 2002; Bies, 2010). Fischer et al. (2011) demonstrated that resources used are generally related to the charitable mission of the organization, but as Kearns et al. (2012) highlight, nonprofit leaders also evaluate different funding sources from a strategic perspective. Along similar lines, an extensive body of research has analyzed nonprofit revenue choice and the relationship between revenue diversification and volatility. Although Kingma (1993) and Jegers (1997) assume, based on modern portfolio theory, that more diversification reduces volatility for nonprofits, recent research suggests a more nuanced view, including resource dependence aspects and compositional change in the portfolio (Bowman, 2011; Frumkin & Keating, 2011; Mayer et al. 2012; Chikoto & Neely, 2013).

Figure 1: External and Internal Factors Influencing Risk Management in Nonprofits



Building on previous studies in the for-profit world and including the specific characteristics of nonprofit funding, Figure 1 presents a theoretical model that integrates potential internal and external factors influencing risk management in nonprofit organizations. It identifies five

broad groups of factors that can be expected to be associated with the extent of risk management implementation: (1) regulatory influences and requirements; (2) main funding resources; (3) organizational size; (4) degree of professionalism; and (5) strategy. As highlighted, the main resources for a nonprofit organization can be grouped into commercial activities, government funding and private contributions. In this context strategy encompasses primarily decisions made by nonprofit executives with regard to funding sources and determining the revenue mix (Kearns et al., 2012). As Hwang and Powell (2009) indicate, it can be expected that both organizational size and strategic decisions are related to the degree of professionalism especially when taking into consideration that there is an interaction between existing organizational management practices and risk management (Arena et al., 2010; Bies, 2010).

2.4. Research Questions and Theory-driven Expectations

Based on the theoretical framework of potential key drivers for risk management in nonprofit organizations as presented in Figure 1 and the analysis of the literature, the study examines the following three research questions:

1. What is the impact of *regulatory requirements* on the implementation of risk management in the field of nonprofit organizations?

As highlighted, large sample cross-sectional research studies in the for-profit area have yielded mixed results when it comes to the influence of regulatory requirements (Kleffner et al., 2003; Collier et al., 2007; Paape & Speklé, 2012). Additionally these studies do not provide any insight into the internal processes of nonprofit organizations and the causal chain of risk management adoption. Drawing on the theory of institutional isomorphism (DiMaggio & Powell, 1983), which has been used in previous nonprofit research to gain insight into nonprofit behavior (Miller-Millesen, 2003; Sowa, 2009; Bies, 2010), the aim of this research question is to explore

the path of influence from regulatory requirements to risk management implementation. Institutional theory refers to external constraining influences as coercive, mimetic, and normative isomophism to explain why organizations adopt certain procedures. Building on *coercive isomorphism* it can be expected that pressures on the organization stemming from the regulator facilitate risk management adoption and drive organizations to similarity and a more homogenous approach to risk management, especially where ties between nonprofits and governmental agencies are close (Verbruggen et al., 2011).

2. What is the relationship between *strategy*, *size*, degree of *professionalism* and risk management adoption in nonprofits?

As for regulatory requirements, findings are not consistent as far as the impact of organizational size on the implementation of risk management techniques is concerned (Collier et al., 2007; Razali et al., 2011; McShane et al., 2011). Research suggests that size alone is not the driving force behind the adoption of risk management. Mikes and Kaplan (2013) indicate that both, people and leadership, as reflected in the organization's strategy and degree of professionalism, play important roles in the process of risk management implementation. *Normative isomorphism* stemming from the level of professionalization and formal education, as well as professional networks leads to the spread of insights, models, and normative rules (DiMaggio & Powell, 1983; Verbruggen et al., 2011). As studies from Christiaens (1999) and Verbruggen et al. (2011) suggest, professionalism in nonprofit organizations is shaped by the background and education of the board of directors and executive management. Based on this it can be expected that the degree of risk management implementation depends on the degree of professionalism being additionally influenced by organizational size and strategy. As the degree of professionalism varies

more greatly in the nonprofit than the for-profit sector (Mannsky, 2011), it can be suspected that the same is true for risk management implementation.

3. How do the main *funding sources* impact the process of risk management implementation in nonprofit organizations?

Since funding as well as the concept of institutional ownership and shareholder influence differs greatly in nonprofits as compared with for-profit organizations, there are no studies to build on as far as risk management adoption is concerned, and even existing research in the for-profit world on these aspects has yielded mixed results (Kleffner et al., 2003; Eckles et al., 2011; Pagach & Warr, 2011; Paape & Speklé, 2012). However, drawing on *resource dependence theory* (Pfeffer & Salancik, 1978), which has been used in several studies to gain insight into several aspects of nonprofit behavior (Oliver, 1991; Greening & Gray, 1994; Carpenter & Feroz, 2001; Guler et al., 2002; Guo, 2007), a theory-driven expectation can be identified. According to resource dependence theory, organizations are driven to compliance with the requirements of strategic resource providers to deal with the pressures of uncertainty and scarcity in their environment (Froelich, 1999; Verbruggen et al., 2011). These resources can be material resources, such as money and human resources as well as information, and social or political support (Verbruggen et al., 2011). Froelich (1999) highlights that the degree of dependence increases with concentration and importance of resources provided. This means that nonprofits that depend heavily on one or very few resources are likely to experience stronger constraining influences from their environment. Based on this, it can be expected that the perception of, and significance risk management has to critical resource providers will translate into the organization's willingness to embrace risk management techniques. In this context the study aims to explore in particular the influence of governmental funding, donors and commercial activities.

3. Empirical Methodology

3.1. Qualitative Research Approach

Cross-sectional field studies based on qualitative data are suggested as a viable approach if research can be grounded in existing theory, but there remains doubt or disagreement surrounding either the nature of the constructs, the relations between them, or their interpretation in a different context as shown in Lillis and Mundy (2005). Given the existing body of literature in the for-profit arena, but the lack of research on how and why risk management is adopted by nonprofit organizations, this approach was selected to collect empirical evidence for the initial conceptual framework of possible influences and to gain insight into different internal and external forces affecting risk management implementation (Ahrens & Dent, 1998; Wouters & Roijmans, 2011). This method differs from the empirical studies conducted on key drivers and determinants of risk management adoption in the for-profit world and takes a position between the existing streams of empirical literature. As highlighted in the literature review, two main empirical research methods have been employed so far: studies based on large sample cross-sectional surveys and single or small-sample comparative case studies. Cross-sectional field studies diverge from these more common approaches to survey and case methods in that are less structured in their data collection than surveys, and involve shorter, less intensive data collection on site than in-depth case studies (Lillis & Mundy, 2005). Although drawing on a larger number of observations than in-depth case studies, and consequently being more generalizable, this approach still addresses the more complex ‘how’ and ‘why’ questions as intended with this study (Eisenhardt, 1991; Ahrens & Dent, 1998). Furthermore cross-sectional field studies can deepen insights into dependencies of constructs and provide the potential for revealing complex internal processes (Miles & Huberman, 1994; Mason, 2002; Johnson et al., 2007).

3.2. Sample and Data

The population of this study consisted of 15 nonprofit organizations in the United Kingdom and 15 nonprofit organizations in Germany. The average size of the organization analyzed measured by total expenditure was US$212 million in the United Kingdom and US$189 million in Germany and ranged from US$6 million to US$1,080 million in the case of the United Kingdom and US$8 to US$816 million in Germany. Selecting organizations of similar sizes in both countries was done to control for any differences stemming from the organizational size in comparing the two subsamples. Additionally, at the outset of the study it was expected that nonprofits of the sizes included in the sample would have at least some level of risk management implementation. In order to get a broader view on the phenomenon of risk management in nonprofits and especially the influence of different funding mixes, organizations from various fields of nonprofit activity were included in the study. Building on research on the structure of the nonprofit sector in the United Kingdom (Kendall & Almond, 1999) and Germany (Anheier et al., 1999) the subsamples aimed to replicate the composition of the nonprofit sector in both countries and include organizations operating in the fields of education, development, culture, social services and health care. A comparison between the United Kingdom and Germany was chosen because of significantly different regulatory requirements in the two countries, thus allowing an analysis of the impact of the regulator on risk management adoption (Bies, 2010; Hyndman & McDonnell, 2009). Whereas in Germany no explicit requirements for nonprofits exist, in the United Kingdom the Charity Commission regulates nonprofit organizations and has made a minimum standard of risk management implementation mandatory (Hyndman & McDonnell, 2009).

The first stage of data gathering included 30 semistructured interviews with risk management experts and key decision makers in nonprofit organizations. All the data was collected

between April 2012 and November 2012. One interview was conducted in each organizations and at the time of the interview, all interviewees had been with the organization for at least two years working in the same position. Interview protocols included the same set of open-ended questions about risk management methods and instruments the organization had implemented, educational background of the individuals involved in risk management, overall degree of professionalism and perceived dependence on key resource providers. To determine the degree of professionalism, indicative questions, such as implemented management methods, organizational structure and educational background of the management as identified by Hwang and Powell (2009) and Mannsky (2011), were asked. Each approximately one hour-long interview was recorded and transcribed.

Figure 2: Descriptive Characteristics of Nonprofit Organizations Analyzed

United Kingdom	Germany
Total Expenditure	
• 6% (1) less than US$7 million • 27% (4) US$7 to US$ 35 million • 40% (6) US$35 to US$ 200 million • 27% (4) more than US$ 200 million	• 0% (0) less than US$7 million • 33% (5) US$7 to US$ 35 million • 47% (7) US$35 to US$ 200 million • 20% (3) more than US$ 200 million
Sector	
• 20% (3) Education • 27% (4) Social Services • 13% (2) Health Care • 13% (2) Development • 20% (3) Culture • 7% (1) Other	• 7% (1) Education • 33% (5) Social Services • 20% (3) Health Care • 20% (3) Development • 7% (1) Culture • 13% (2) Other

(N = 30)

The second stage of data gathering included the examination of publicly available information such as financial statements and annual reports. All passages relating to any type of risk management adoption were highlighted and subsequently treated in the same manner as the in-

terview transcripts (Babiak & Thibault, 2009). The use of multiple sources of data was intended to provide both methodological and data triangulation and aimed to enhance the reliability and validity of the study (Denzin, 2009).

To systematically examine the collected material, a qualitative content analysis was conducted (Mayring, 2004; Miles & Huberman, 1994). Each transcript was analyzed in two steps using deductive category application and inductive category development. Based on the existing theory in the for-profit area, passages of the text were assigned to prior formulated categories (Mayring, 2004; Hsieh & Shannon, 2005). To allow new insights to emerge from the data, in a second step, additional categories were derived from the data (Mayring, 2004; Miles & Huberman, 1994). During the analysis patterns of content were examined to validate the initial theoretical framework and identify the most important findings and themes (Silverman, 2006; Hsieh & Shannon, 2005).

4. Findings

4.1. Organizational Perspective on Regulatory Requirements

Previous research could find some, but not consistent, level of influence of regulatory requirements on risk management implementation in the for-profit world (Kleffner et al., 2003; Collier et al., 2007; Paape & Speklé, 2012). To avoid biasing their responses, at the outset of the interview, interviewees were asked the open-ended question on reasons and motives for risk management adoption. While in Germany none of the interviewees made reference to regulatory requirements, 73% (11) of the key decision makers in the United Kingdom mentioned the influence of the regulator, in addition to other considerations, as an important factor for their approach toward risk management. In this context, the formal pressure (DiMaggio & Powell, 1983)

stemming from the regulator and the impact on internal processes was described by one interviewee as follows:

> *"The Regulator requires that we deal with risk quite significantly in the way that we do it, and the board itself is aware of the key risks – sort of managing the organization. So the Regulator places a high regard to risk management."*

This and other comments made, lend support to the expected relationship between regulatory impulses and risk management implementation and indicate a process of *coercive isomorphism* in the United Kingdom resulting from macrosociological forces (Fernandez, 2008). As theorized by Meyer and Rowan (1977) and studied empirically (DiMaggio & Powel, 1983; Abzug & Galaskiewicz, 2001; Bies, 2010; Verbruggen et al., 2011) coercive isomorphism is expected to result in a more homogeneous behavior of organizations and an application of similar management techniques. This could be observed by contrasting the risk management methods used in the United Kingdom and Germany. While in the United Kingdom almost all organizations analyzed (93% (14)) had established a clearly defined process to regularly identify and evaluate risk, a wide range of approaches could be noticed in Germany, with only 33% (5) having a continuous method of risk identification and evaluation. Similar results could be found with regard to the documentation and degree of formalization of the organization's risk strategy. Since risk strategy, risk identification and risk evaluation are fundamental parts of the risk management process it was not surprising to see significant deviations, in Germany, in the subsequent steps of risk management implementation. In summary, it could be observed that in the United Kingdom all nonprofits have adopted at least a minimum set of risk management methods including a risk register, risk map and risk strategy, while in Germany the tools used differed greatly from organization to organization with some nonprofits having no systematic risk management approach at all. In explaining this difference between nonprofits in the United Kingdom having a generally

highly formalized risk management approach, and Germany having more informal and inconsistent structures, an interviewee commented:

> *"I think the phrase I always hear is, it has been around informally for years. But it hasn't been formalized until the Charity Commission had recommended that we had risk registers and documentation."*

This suggests that the pressure stemming from legal requirements has been a catalyst for these changes and pushed nonprofits to formalize and structure their informal processes better. Besides the formal pressure driving nonprofits in the United Kingdom to more similarity in their approach to risk management, the interviews revealed further layers and mechanisms of coercive isomorphism. DiMaggio and Powell (1983) mention informal pressures exerted on organizations and cultural expectations in the society as additional coercive forces. While highlighting the link between funding and the role of the regulator, the influence of these factors was described by an interviewee as follows:

> *"And people really trust it if it is a proper UK charity. Especially for charities that take money from the public so I think it is very important that the Charity Commission is quite firm with the rules."*

This is consistent with work by Meyer et al. (1987) who also found that coercive pressures had an important indirect effect, as the organizations they studied altered their organizational structures to adapt to the implicit and anticipated expectations of external funders and regulators. Taking this idea one step further, Verbruggen et al. (2011) linked coercive isomorphism with normative tendencies. In studying the compliance of nonprofit organizations with reporting standards they theorized that after a new legislation has been introduced, *normative isomorphism* is likely to follow. This assumption finds support in the comments interviewees in the United

Kingdom made, viewing risk management implementation as "best practice" and part of a well-run nonprofit organization. The following quotation illustrates this perspective:

> *"To be honest, it's something that happened in every charity I ever worked for so it is just kind of one of those things that you always do. If I arrived in a charity, where risk management didn't exist, then I would implement it."*

Additional support can be found in the fact that at least 27% (4) of the interviewees in the United Kingdom, when asked about reasons and motives for risk management adoption, did not mention regulatory requirements at all, indicating the legal obligation had in these cases deteriorated to subsidiary importance.

4.2. Organizational Perspective on Professionalism, Strategy and Size

In institutional theory another source of isomorphic organizational change is *normative* and stems primarily from professionalization and the pressure of professions (DiMaggio & Powell, 1983; Fernandez, 2008). When asked the open-ended question, what and who drove the implementation of risk management in the organization, 80% (12) of the nonprofits in the United Kingdom and 67% (10) of the organizations in Germany mentioned the influence of the educational background and work experience of the board and management. The importance and impact of the qualification and prior experience was described by an interviewee as follows:

> *"Because for me it is about what is the caliber of resource that you can draw in, what is their experience and qualification because people like M. expect to do these things in a well-run business."*

This finding is consistent with other studies that analyzed the importance of the existence of a Chief Risk Officer for risk management implementation in the for-profit world (Liebenberg & Hoyt, 2003; Kleffner et al., 2003; Ellul & Yerramilli, 2010). Hall et al. (2012) tried to gain insight into the process how risk managers become influential in organizations and how profes-

sionals compromise with nonprofessionals by studying two financial institutions. They were able to explain how functional experts may compete in the intraorganizational marketplace for influential ideas and the attention of decision makers. However, the study started at a point where a risk management function in the organization already existed and did not explain what triggered the initial implementation. In regard to this process, an interviewee commented that the background of the board and decision makers is a crucial point in initiating and facilitating risk management adoption:

> *"Basically the initiators are the decision makers and the board. As far as the operational implementation is concerned, I think, it is more the background of the ones being involved in day-to-day work that drives things."*

While it appears that the, "*if* question", i.e., whether or not risk management is implemented in a nonprofit depends very much on the attitude of board and top management, the "*how* question" or practical implementation of the risk management processes is primarily driven by the functional experts. This is supported by the observation that nonprofits in Germany which were governed and managed by decision makers with a business executive background were more likely to have risk management techniques in place. Building on previous research, a business executive background was understood as formal education in organizational decision making, corporate strategy and financial management or practical management experience in a for-profit institution (Olson, 2000; Hwang & Powell, 2009; Mannsky, 2011). Expanding this finding to the main sources of funding, it could be observed that in both countries nonprofits that depended primarily on commercial activities were in most cases governed by individuals with a business executive background and had implemented a risk management process. In the case of a nonprofit where the majority of the decision makers had changed recently to managers with more

of a business executive background, the chief executive commented on missing risk management instruments in the organization as follows:

> *"My colleagues and I didn't have anything to do with Charities so far. ... But we definitely have the goal to adopt industry standards of corporate finance."*

This indicates a *mimetic isomorphism* where business-like nonprofits (Dart, 2004) and nonprofits with more "corporate" members in their management tend to copy or imitate methods and instruments from the for-profit sector, modeling themselves on other organizations (DiMaggio & Powell, 1983). This is consistent with findings from empirical studies on the adoption of financial accounting principles in the public sector, where it could be shown that business-like organizations more readily embraced reporting and accounting standards from the for-profit world (Christiaens, 1999; Da Costa Carvalho et al., 2007).

Based on the findings concerning the impact of professionalism on risk management adoption, the influence of organizational size was analyzed. Although intuition might foster the expectation of a relationship between size and risk management implementation, existing empirical studies in the for-profit arena have yielded mixed results in this regard (Collier et al., 2007; Razali et al., 2011; McShane et al., 2011). Support for the idea that risk management adoption depends on organizational size could be found in the responses from the experts in the sample analyzed. As a reply to the open-ended question about what drove risk management implementation in the specific nonprofit, 47% (7) of the interviewees in the United Kingdom and 47% (7) in Germany, mentioned that the size of the organization is an important factor. One interviewee commented:

> *"We have reached now a size, where we are in a position to get external consultants on board, to help us with our processes."*

This comment together with findings on the impact of the organization's degree of professionalism lends support to the assumption that size can be linked with a *normative isomorphism* leading to the adoption of best practices. One way that size affects risk management implementation seems to be through the mechanism of better educated employees and involvement of external experts. In this context, size can be interpreted as a mediating variable that creates an environment which helps to facilitate the process of risk management adoption. This might help explain some of the mixed results yielded by previous research focusing only on organizational size as key driver for risk management implementation. At the same time it is consistent with the observation that even in smaller nonprofits analyzed, the adoption of risk management techniques was driven by experts within the organization.

4.3. Resource Dependence

While institutional theory (DiMaggio & Powell, 1983) analyzes how organizations adapt to pressures that stem from the institutional environment, resource dependence theory (Pfeffer & Salancik, 1978) stresses the pressures exerted by those who control scarce resources (Oliver, 1991; Verbruggen et al., 2011). To broaden the perspective on different aspects in nonprofit behavior and to use the convergent insights of resource dependence theory and institutional theory, interviewees were asked open-ended questions on the influence of resource providers. Almost without exception, the interviewees in both countries highlighted the importance of reputation and the public image as a critical resource. One interviewee summarized this with regards to risk management as follows:

> *"I think a reputational risk is one you are more worried about than any other because it could have such a major impact."*

This echoes academic scholarly work that identifies the relevance of legitimacy and reputation as a distinguishing mark between the nonprofit and for-profit sectors (Baruch & Ramalho,

2006; Sosin, 2011). It was noticeable that nonprofits that depended primarily on donations emphasized the importance of the organization's reputation to a greater extent. In the United Kingdom 86% (6 out of 7) of the donation-based organizations mentioned reputation an important factor while only 63% (5 out of 8) of the non-donation-based organizations made reference to it. In Germany the results were similar with 83% (5 out of 6) of the donation-based nonprofits highlighting the relevance of reputation and 67% (6 out of 9) of the non-donations-based organizations. However it could not be observed that the higher importance of the public image and reputations translated into a higher degree of risk management implementation in donation-based organizations. This may be explained by findings from a study Parsons (2007) conducted on donors' reactions to financial accounting information. Parsons (2007) found that the usefulness of financial information to donors and their decision-making process was not overwhelming, since small individual donors' gifts are often made on impulse. This is consistent with comments made by the interviewees in this study on the limited influence of small individual donors on risk management adoption, contrasted with the greater influence of large donors and governmental agencies. The following comment from an interviewee illustrates this perception:

> *"Quality expectations from donors towards nonprofit organizations are increasing. This may be the individual donor that is very interested and knowledgeable, but in particular large corporate donors who want to know how the organization is governed and operates."*

Resource dependence theory provides the theoretical background to explain nonprofits' behavior. The degree of dependence increases with concentration of the provided resources (Froelich, 1999), which means that organizations that depend heavily on one or very few resource providers, such as large donors or government funding are likely to more readily adopt their expectations on appropriate risk management processes (Verbruggen et al., 2011). The importance

of compliance with governmental expectations was described by one organization that primarily depends on government funding as follows:

> *"Reputational risk tends to fall into two categories. One of them is reputation with Government because we are tied to Government and we need to make sure that we are on the right side of them."*

In summary the influence on risk management implementation from strategic resource providers seem to depend very much on two factors: (1) the individual perception of risk management of the relevant resource provider and (2) the nonprofit's degree of dependence on this resource.

5. Conclusion and Issues for Further Research

This study used institutional and resource dependence theory to explain nonprofit organizations' adoption of risk management techniques. Nonprofit organizations are embedded in a complex network of stakeholders and depend on outside sources of funding to assure their survival. The choices and behavior of nonprofits are bound by pressures stemming from regulatory requirements, professions and the attempt to ensure legitimacy and financial support. When nonprofit organizations are convinced that governmental funding or donations depend on risk management adoption, they will make the necessary efforts to establish risk management as a function within the organization. In many cases, the government is both an important source of funding, and may at the same time be an enforcer of regulatory requirements, which results either "coercing" nonprofits to implement or not implement risk management techniques. Additionally, building on normative isomorphism, compliance with risk management standards is largely driven by the nonprofit's degree of professionalism and the educational background of individuals in the organization. Furthermore, this driving force is facilitated by organizational size and the extent to which the nonprofit organization already operates an a "business-like" manner.

In summary, the contributions of this study to the existing literature are threefold. First, institutional and resource dependence theory have been applied in an area of nonprofit behavior that has not been studied before. Although both theories have been used separately, as well as intertwined, to explain different aspects of organizational behavior, such as board involvement (Miller-Millesen, 2003; Hodge & Piccolo, 2005), nonprofit governance (Guo, 2007), financial reporting and vulnerability (Verbruggen et al., 2011; Froelich, 1999), no studies were found explaining motives for risk management adoption in nonprofits and how they differ from for-profit organizations. Second, risk management adoption has been linked to organizational theories, helping to better understand the internal processes that are not financially driven and facilitate risk management implementation. Third, large sample studies on factors influencing risk management have yielded mixed results in different areas, such as the impact of regulatory requirements (Kleffner et al., 2003; Collier et al., 2007; Paape & Speklé, 2012) and organizational size (Collier et al., 2007; Razali et al., 2011; McShane et al., 2011). In the nonprofit setting it could be shown that these factors are related and influenced by the degree of professionalism of the organization and the educational background of the decision-makers. Institutional theory with normative and mimetic pressures, provides the theoretical background for these findings.

The findings and limitations of this study suggest several avenues for future research. In order to better understand internal processes of risk management adoption a qualitative approach was taken. Some hypotheses could be tested and findings verified using a larger sample of organizations. Additionally different fields of service and types of mission could be studied in more detail since this study took a broad perspective on the entire nonprofit sector in both analyzed countries. More in-depth research projects on donation-based organizations and business-like

nonprofits seems to be promising, including the ethical, institutional and economic underpinnings for risk taking in these respective contexts.

Given the volatile environment in which nonprofit organizations operate, it is not likely that uncertainties and instabilities associated with nonprofit decision-making will diminish in the near future. This requires that nonprofits make necessary adjustments to ensure their survival and fulfill their mission. No doubt, an expanded capacity for and adoption of risk management techniques will help nonprofits to meet these challenges proactively.

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