

FOREST TRENDS

RISK MANAGEMENT

POLICIES & PROCEDURES

2020

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I. OVERVIEW

Since its founding in 1998, Forest Trends' original strategic design has been rooted in working with stakeholders from public and private finance and civil society to both promote and track new financial markets designed to advance forest and natural resource conservation. Our mission was to help build incentives, payments, and markets around ecosystem services and conservation. We viewed this as the path to build conservation into mainstream development agendas and the best strategy to adapt to looming issues such as climate change.

Forest Trends operates on the premise that real and lasting change comes through collaboration. Forest Trends seeks to be a catalyst for action, serving as the "connective tissue" that brings together diverse stakeholders to achieve conservation goals. Hence, a primary aspect of our work is to build and work with a large and diverse network of strategic partners with whom we carry out shared activities to achieve greater and lasting results.

Over the last 20 years, Forest Trends has worked across interrelated sectors - water, biodiversity, and carbon - helping to describe, define, and propel the universe of these emerging environmental markets. Potential exposure to certain risks is inherent in our activities and the complex and dynamic environment in which we operate. Therefore, we understand that identifying, assessing, and managing these risks is not only necessary, but the foundation upon which the organization must ground its decisions and shape its successes. Forest Trends' Risk Management Policy is therefore a central building block of the organization's governance framework.

From the beginning, Forest Trends embraced a set of core values: to be small, global, and agile. This has helped us avoid the inertia that often burdens bigger organizations while encouraging Forest Trends to always to seek deeper and more valued collaborations. These foundational values underpin the culture of Forest Trends. They support a vision that requires innovation, flexibility, and responsiveness, and reinforces our commitment to coalition building, equity in these emerging ecosystem markets, and efficiency - the delivery of results in a cost-effective way, across sectors, geographies, and scales.

A. Purpose and Benefits

The risk management process is designed to demonstrably contribute to Forest Trends' objectives and to the improvement of organizational performance in all areas of activity. Rather than done purely for compliance reasons and to meet legal obligations, this process assists Forest Trends in its risk management decision-making, resource allocation, program development and change management, among many other facets of the organization's operations.

Strong risk management also contributes to good governance and strategic business planning. It enhances organizational confidence that Forest Trends can deliver its desired outcomes for its stakeholders, manage risks to the organization to an acceptable degree, and make informed decisions about opportunities available to Forest Trends in its areas of focus.

B. Types of Risk

Risks may arise from internal operations and/or from external sources. Key areas of risk include:

- **Compliance risks** are those where the organization fails to meet its corporate and legal obligations. These include all types of reporting, accounting, workplace or employee relations, and work and health and safety activities, among others. These are obligations to which the organization must comply. Consequences

arising from such risks could include breach of contract duty, regulations, and rules and laws that apply to the operations of the organization.

- **Organizational risks** are those where the organization fails to achieve its objectives such as level of financing, service delivery, standard of service delivery, or meeting stakeholder expectations. These risks occur in numerous ways and have the potential to affect financial performance, reputation, health and safety, and the overall performance or sustainability of the organization. Consequences arising from such risks include loss of reputation or high staff turnover, among others.
- **Opportunity risks** arise from the pursuit of opportunities – “positive risks” – that may enhance the organization in some way or allow it to achieve its objectives more easily. Such opportunity risks can be listed separately from negative risks. Consideration is given in each case to the potential gains for the organization and resources required to pursue the opportunities vis-à-vis the potential gains.

C. Framework

The Risk Management Framework (Framework) is aligned with Forest Trends’ governance and strategic planning process. It includes work planning and activities, internal and external reporting processes, and communication mechanisms, and considers policies, procedures, values and culture.

The Framework clarifies accountabilities (Risk Ownership), reporting and escalation processes, as well as the communication and consultation mechanisms for internal and external stakeholders. The Framework also establishes processes and procedures for (i) identifying and assessing risks, (ii) determining appropriate responses, (iii) establishing procedures and controls to respond to and mitigate the risk, and (iv) to monitor mitigation and response efforts.

II. POLICY

Risks result from the Forest Trends' operational undertakings and from external sources. To fully understand such risks Forest Trends has established a Risk Management Policy which provides the Framework by which it manages risk. The process of risk management is a central building block of organizational governance and integrated to Forest Trends' strategic planning process. It is also intrinsically linked to day-to-day operations and decision-making processes. The Policy addresses both strategic and operational risks.

Using our skills and expertise (and utilizing outside expertise as needed), we identify risks by risk type across the organization. We assess the size or degree of each risk by taking into consideration their potential impact to the organization while considering controls that might already exist to reduce, mitigate, or eliminate them. Assessment of risk, controls and treatment plans are documented in a Risk Tracking tool maintained for this purpose.

The effectiveness of the Risk Management system is monitored by on a regular basis and reported out at across all levels of the organization, including managers, program directors, executive management, the CEO and Board of Directors.

A. Risk Tolerance

Our tolerance for adverse risks informs and determines which risks require Risk Treatment actions. When levels of risks are deemed unacceptable, Risk Treatment plans are developed to establish controls to manage such risk to acceptable levels. Risk Treatment plans are designed to reduce risks to acceptable levels which may include any combination of: (a) creating new controls where no or insufficient controls exist, (b) strengthening controls already in place or (c) taking other mitigating actions including stakeholder consultations. When treatment plans that adequately reduce or eliminate the risk are not readily evident or possible to determine, Forest Trends will delay initiating the action or plan under consideration until control measures that manage the risk to acceptable levels can be identified or refrain from the action altogether.

B. Integration with Governance and Planning

The Risk Management Policy addresses both strategic, reputational, and operational risks and the requirements imposed upon Forest Trends while operating in its field and regulatory environment. The Risk Management process is integrated with the strategic planning, and the annual planning processes.

C. Accountability and Identification and Assessment

Executive management- and manager-level staff across the Forest Trends are responsible for identifying, assessing, and monitoring risk within their respective functional areas. The accountability for monitoring and reporting on risk ("Risk Ownership") is assigned to relevant roles within the organization. Risk Owners periodically report progress or results of Risk Treatment actions, changes in existing risk assessments or identification of new risks to the Director of Finance and Director of Operations who, in turn, aggregate the data and report on the full Risk Management Framework to the President and CEO as needed but no less than quarterly and the Board of Directors as needed, but no less than annually.

D. Risk Management Oversight

Risk oversight responsibilities are given to relevant positions Forest Trends in different levels of management, and across functional areas. Ultimately, the Audit Committee of the Board of Directors provides the highest level of

oversight of Forest Trends' Risk Management Framework. This multi-tiered oversight of the effectiveness of our risk management processes and activities provides assurance to the Board and donors, supporters, staff and other stakeholders, continuous commitment to learning and improvement at all levels.

E. Reporting Monitoring and Review

Forest Trends monitors risks and Risk Treatment actions on an on-going basis. A formal review of the Risk Management Framework and outstanding treatment actions are reported to the Executive Committee of the Board of Directors at the Annual meeting of the Board.

F. Communication and Consultation

Forest Trends will communicate and consult with its stakeholders, including its staff, Board members, consultants, implementing partners, donors and collaborator on its approach and process to risk management. Methods of communicating the risk management processes and their mitigating controls range from staff orientation and onboarding programs to well-crafted consultant and partner or sub-recipient agreements with clear deliverables, deadlines, and agreed upon terms of references, that contain relevant provisions including reporting and monitoring processes, procurement requirements, and donor flow down provisions, among others.

The communication and consultation processes around risk are integrated into ongoing information exchanges and consultations that occur between Forest Trends and its stakeholders during all collaborative engagements. When identifying treatment plans for a new risk or a risk that is specific to new organizational processes or programmatic activities, one-on-one meetings or interviews will take place to gather the intelligence required to design effective controls and/or treatment plans.

III. FRAMEWORK

The Risk Management Framework is the whole set of activities carried out to (i) identify and assess risks to which Forest Trends is exposed, (ii) determine appropriate responses to such risks, (iii) establish procedures and controls to respond to and mitigate such risks, (iv) communicate and inform the organization and other stakeholders regarding such risks, and (v) monitor mitigation and response efforts.

A. Risk Identification and Assessment.

This step entails identifying all the risks Forest Trends may be exposed to, as well as their sources and causes, their potential consequences and areas of impact, and any risk management controls already in place.

1. RISK IDENTIFICATION.

Various events and activities give rise to risks that may impact Forest Trends' ability to meet its objectives and ensure organizational performance. When making plans or decisions related to Forest Trends' activities, the relevant Risk Owner must identify the possible risks that may arise. This can be done through activities such as working one-on-one with relevant managers or officers across Forest Trends, by running workshops with the relevant managers or officers, or conducting interviews.

A useful technique to employ in risk identification exercises is the cause-effect technique. This involves asking two related questions:

- What could go wrong in this part of Forest Trends? (Potential effect)
- Why might it happen? (Potential cause)

A cause may comprise several contributing factors. Identifying the various contributing factors may provide further insights into other risks and their flow-on effects.

2. RISK ASSESSMENT

Risk assessment entails defining the consequences of the risk and the likelihood the risk will happen given existing organizational controls. The assessment answers three key questions of

- 1) what type of consequence does the risk expose Forest Trends to?
- 2) how serious are the consequences of the risk? and
- 3) what is the likelihood that such consequences will occur?

a) Risk Type and Severity

Potential impacts may include financial, reputation, work health and safety, legal, operations, etc. Forest Trends considers five levels of impact ranging from insignificant to severe. Table B.1 provides examples of the types of potential impacts over a range of impact levels. Note that a single risk may have multiple consequences and affect multiple organizational objectives.

SEVERITY LEVEL	Financial	Management Effort	Work Health & Safety	Reputation/ community	Legal/ Compliance
CRITICAL (5)	Loss, error or omission >15% of annual budget or projected revenue	An event so severe in nature it could lead to a significant restructure of the organization or its major parts or a change in the management structure	Fatality and/or severe irreversible disability (>30%) to one or more persons or permanent disabling injury or disabling illness to one or more persons	Ongoing serious public or media outcry (state or national coverage)	Significant prosecution and fines, very serious litigation
MAJOR (4)	Loss, error or omission 10%-15% of annual budget or projected revenue	An event, which with proper management can be endured, may involve some changes in management, additional resources required	Series of significant but reversible disabilities requiring hospitalization	Serious public or media outcry (local coverage)	Major breach of regulation, prosecution or major litigation
MODERATE (3)	Loss, error or omission 5% -10% of annual budget or projected revenue	An event that can be managed under normal circumstances, additional resources required, potential reallocation of resources	Significant but reversible disability requiring hospital visit	Heightened and/or significant adverse media attention	Breach of regulation with investigation or report to authority with prosecution and/or moderate fine possible
MINOR (2)	Loss, error or omission 1% -5% of annual budget or projected revenue	An event, where the consequences can be absorbed but management effort is required to minimize the impact, potential reallocation of resources	First aid treatment required	Adverse media attention and/or heightened concern of local community	Minor legal issues, non-compliances and breaches or regulations
INSIGNIFICANT (1)	Loss, error or omission up to 1% of annual budget or projected revenue	An event, where the impact can be absorbed through business as usual activity	Minor incident not requiring first aid	Minor local adverse public attention or complaints	Minor compliance issue

b) Risk Likelihood Criteria

These criteria define levels of likelihood around a risk event occurring given current controls such as provisions in the Code of Conduct, IT protocols, financial oversight and controls, and other risk management procedures. They answer the question ‘How likely is it that Forest Trends will be exposed to risk x?’ Forest Trends adopts five levels of likelihood, and for each level they provide descriptors and an estimate of probability.

LIKELIHOOD CRITERIA		
LIKELIHOOD LEVEL	DESCRIPTION	PROBABILITY
Almost Certain (5)	Is expected to occur in most circumstances—frequently during the Yr	>95%-100%
Likely (4)	Will probably occur—once during the year	70%-95%
Possible (3)	Might occur at some time—once every 3 years	30%-70%
Unlikely (2)	Could occur at some time—once every 5 years	5%-30%
Rare (1)	May occur only in exceptional circumstances. This event is known to have occurred elsewhere—once every 5+ years	<5%

c) Develop the overall risk profile

The final stage of risk identification and assessment is determining the overall risk profile. The following risk matrix is used to evaluate the overall risk profile of a given action, decision, or event:

	ALMOST CERTAIN 5				
	LIKELY 4				
d)					
e) POSSIBLE 3					
f)					
g) UNLIKELY 2					
h)					
i)					
j) RARE					
k)					
l)					
	INSIGNIFICANT 1	MINOR 2	MODERATE 3	MAJOR 4	CRITICAL 5
	CONSEQUENCE				

Using the risk matrix, assign each risk a level and score. This is done by plotting the risk’s ‘consequence’ against its ‘likelihood’. For example, if a risk is ‘moderate’ (consequence) and ‘unlikely’ (likelihood), its risk level will be ‘medium’. It will have a score of 6 (3 (for consequence) x 2 (for likelihood) = 6). Because a given decision, action,

or event may have numerous risk consequences, a risk profile will include the score of all the risks. Develop a risk profile by plotting all the risks into the risk matrix.

B. RISK RESPONSE

The purpose of this step is to determine what response to the risks are needed, if any. Actions may include accepting the risk without the need for further controls, implementing mitigation measures to reduce a risk to acceptable levels, avoiding the activity due to unacceptable risk, or transferring the risk to a third party, for example through purchasing insurance or sub-contracting to a third-party with a lower overall risk profile.

1. Escalation and Assigning Risk Ownership

As each risk is assessed, assign the risk to a program manager or director with authority to manage risks and to allocate resources for risk treatment actions. This improves accountability for managing risks within acceptable, or valid, levels of tolerance and for escalating any risks deemed unacceptable.

Escalation ensures that appropriate individuals are informed of, and can make decisions regarding a response to significant risks. Such individuals then become the Risk Owners. At the same time, it allows for certain risks to be addressed without further escalation to ensure the agility of Forest Trends' decision-making process. The following chart lays out guidelines for treating and escalating risks based on their Overall Risk Profile.

RISK LEVEL	RISK TREATMENT GUIDELINES	ESCALATION AND RETENTION GUIDELINES
EXTREME	Immediate action required to actively manage risk and limit exposure	Escalate to the CEO and Board, risks generally not accepted or retained
HIGH	Cost/benefit analysis required to assess extent to which risk should be treated - monitor to ensure risk does not adversely change over time	Escalate to CEO, risks generally not accepted or retained
MEDIUM	Constant/regular monitoring required to ensure risk exposure is managed effectively, disruptions minimized and outcomes monitored	Escalate to relevant senior management level, specify risk management actions, risks may generally be retained and managed at operational level
LOW	Effectively manage through routine procedures and appropriate internal controls	Monitor and manage at the relevant officer, or operational level, risks generally retained

2. Risk Treatment

Once the Risk Owner is identified, the appropriate risk treatment must be identified and implemented. The options for risk treatment may include:

- avoiding the risk by not starting or carrying on the activity that gives rise to it, or by changing how the activity is undertaken
- removing the source or cause of the risk
- reducing the likelihood of the risk's occurring
- limiting or minimizing the consequences of the risk should it occur
- sharing the risk with another party or parties (i.e., insurance, contracts, partnering)
- retaining the risk by informed decision and approval of the Board or senior management.

These are just some options. They are not necessarily mutually exclusive. They may not be appropriate in all circumstances.

To choose the most suitable risk treatment option (or options), the Risk Owner must weigh the costs of implementing a treatment against the benefits it is likely to deliver. Issues to consider include:

- the financial and other resources required to implement the treatment
- the feasibility (including timing) of implementing the treatment
- how effective the treatment is likely to be in reducing or removing the risk
- the potential impact of the treatment on stakeholders' values, perceptions, and interests – some treatments may be more acceptable to stakeholders than others
- whether the treatment will compromise or conflict with any legal, regulatory, or other obligations your organization has
- possible unintended consequences of the treatment – risk treatments themselves may affect other existing risks, or may introduce new risks (known as secondary risks)
- the failure or ineffectiveness of a risk treatment is itself a risk.

C. DEVELOP AND IMPLEMENT RISK TREATMENT PLANS

Risk treatment plans ensure consistent and appropriate adherence to the selected risk treatment throughout Forest Trends. These may require development of additional policies and procedures or other guidance that can be distributed to appropriate stakeholders. Critically, the risk treatment plan must be periodically reviewed for effectiveness based on the plan's objectives and, if the plan is not meeting its objectives or creating additional risks, revised.

The implementation of a risk treatment may have varying degrees of success. It may lessen the risk, remove the risk entirely, or have no effect at all. If risk remains after implementing the control, that remaining risk (known as a "residual risk") must be re-assessed and re-rated evaluated based on the criteria described above to determine whether it is within a tolerable level. If not, one or more new or additional risk treatment plans must be implemented. In summary, implementing and reviewing risk treatments is a cyclical process of:

- implementing the risk treatment
- assessing its effectiveness
- deciding whether any remaining risk (known as residual risk) is at a tolerable level
- (if it is not tolerable) implementing a new risk treatment
- assessing the effectiveness of that treatment.

After implementing a risk treatment, we will also re-assess and re-rate the risk, but now with the treatment in place. The treatment, in other words, has become a new risk management control.

D. COMMUNICATION AND CONSULTATION (ONGOING PROCESS)

In all steps of the Risk Management Process, we will ensure that the appropriate stakeholders (external and internal) are consulted and/or informed about what's going on. Effective communication will ensure that those responsible for implementing the process, as well as other relevant stakeholders, understand the basis on which decisions are made and the reasons why particular actions are required. It will also support and encourage accountability for ownership of risks.

Internal stakeholders including the Board need to be fully informed of the outcomes of risk assessments and risk reviews. They must be informed of risks at levels beyond the acceptable or tolerable. Staff and managers need to be informed of the outcomes of risk assessments and risk reviews so they can manage risks appropriately and in accordance with risk management policy. In addition, formal and informal training must be conducted with personnel regarding both the risk management process and the implementation and review of relevant risk treatment policies.

External stakeholders like donors, consultants and partners may also need to be informed about risk assessments and reviews due to statutory and governance obligations. Besides that, you should think carefully about what you choose to communicate. For example, it is unlikely that you would inform potential suppliers about individual risks, though it may be beneficial to inform them that we have a Risk Management Policy and Framework to manage risks, because this information may assist in negotiating favorable terms or conditions for the procurement of goods and services.

A consultative approach will yield more successful outcomes by helping relevant stakeholders in the Risk Management Process and to integrate risk management into Forest Trends. For example, it will:

- help establish the context appropriately
- ensure the interests of stakeholders are understood and considered
- help ensure that risk categories and risks are adequately identified
- bring together different areas of expertise for analyzing risks
- ensure that different views are considered when defining risk criteria and evaluating risks
- secure endorsement and support for treatment plans
- enhance appropriate change management during the Risk Management Process
- develop an appropriate external and internal communication and consultation plan.

Senior managers or officers are usually involved in identifying, assessing, and managing risks, so they should be consulted. Ensure that those responsible for the organizational processes and outcomes in each risk category are consulted. Consultation can be done through one-on-one interviews, group workshops or other methods.

E. MONITOR AND REVIEW (ONGOING PROCESS)

Risk management must be responsive to change – both within Forest Trends and in the external environment. Therefore, the activities of monitoring and reviewing must be ongoing, and are integral to every step in the Risk Management Process. By monitoring risks, controls, and risk treatment plans, we can ensure that risks are being managed in accordance with your organization’s Risk Management Policy and Framework.

1. ESTABLISH FORMAL REVIEW AND REPORTING MECHANISMS

As well as conducting ongoing monitoring activities, Forest Trends will establish formal review and reporting mechanisms. These mechanisms are a requirement of good governance, provide the management team with regular and up-to-date information on risks, risk treatment plans and any issues arising, and assure the Board that risks are being managed in line with the Risk Management Policy and Framework.

Formal review and reporting mechanisms are:

- Annually review Forest Trends’ Risk Management Policy and Framework, risk assessment criteria, and the Risk Management Process and its integration and alignment with other organizational processes.

- Three times a year according to the Forest Trends Board meeting cycle, report to the CEO and Board with an update on the relevant risk assessments and risk treatment plans (particularly for 'extreme' and 'high' risks).
- No less than semi-annually review risks and risk treatment plans with Directors and Managers.