

## **Note on possible funding options for rating of Voluntary Organisations**

**Context** – World over there is a growing appreciation of the role of Voluntary organisations (VOs) in supplementing the efforts of the state in bridging the development divide. Indian policy towards role of VOs has always been appreciative, with 1st Five year plan stating, “Any plan for social and economic regeneration should take into account the services rendered by these agencies and the state should give them maximum cooperation in strengthening their efforts.” The spirit continues today also as reflected by the approval of the National Policy on the Voluntary Sector in 2007, by the cabinet of ministers of the Government of India. Through the policy, the government commits to encouraging, enabling, and empowering an independent, creative, and effective voluntary sector with diverse form and function, so that it can contribute to the social, cultural, and economic advancement of the people of India

The Global thinking on role of VOs/CSOs is captured through the World Bank statement that it has learned through three decades of interaction that the participation of CSOs in government development projects and programs can enhance their operational performance by contributing local knowledge, providing technical expertise, and leveraging social capital. It goes on to say that CSOs can bring innovative ideas and solutions, as well as participatory approaches, to solving local problems.

Indian context is characterised by a wide array of VOs/CSOs (recent estimates put the figure at around 1.5 million) involved in both welfare and empowerment with work areas as diverse as development, civil liberties, education, environment, health, and livelihood. The only unifying thread among these organisations is the legal charter as whether registered as a trust, society, or company, NGOs are subject to the Societies Registration Act of 1860 and the Income Tax Act of 1961.

### **Need for accreditation/rating<sup>1</sup>**

The logical question which follows the context is: if VOs are doing good work and the legal framework has served the broad needs, why introduce formal mechanisms like accreditation/rating which go against the spirit of VOs?

The initiative in the form of setting up a National Accreditation Council has to answer the above question, so that the initiative has acceptance in the sector. The exercise is to be seen as an attempt in having the concept of ‘accountability’ applied to the Voluntary sector also. This can be justified as under

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<sup>1</sup> The difference between accreditation and rating is explained later.

- 1) NGOs have become a de-facto partner in the establishment of national norms and standards, negotiating, influencing and proposing policy solutions to social public problems like the spread of communicable diseases, poverty, housing and education crises, shrinking wages, ecosystem fragility and human rights violations. NGOs have been vocal about democratic practice in governance, yet the public perception about NGOs is not so robust about their won democratic practice.
- 2) VOs now take upon many Public- Private partnerships as also benefit from Public policy in the form of financial aid and favourable tax treatment. The tax payer is entitled to know about the efficacy of VOs and optimal utilisation of public funds.
- 3) Recognising the above aspects, the national policy on voluntary sector also has “encourage volunteer organizations to adopt transparent, accountable systems of governance and management” as one of the key tenets.

The accountability initiative has not to be seen as a techno-bureaucratic exercise but a genuine attempt at closer interaction with the state and donors in a transparent manner. The working of NAC has to be flexible, participatory and involve the sector so as to gain wider acceptability.

The accountability matrix has both upward (donors, state) and downward implications (clients and other stakeholders) and is also beneficial to the sector.

### Accreditation Vs Rating of VOs: Why rating?

The accountability imperative brings us to the question of implementation framework. It is worthwhile to examine the accountability matrix so as to see what are the areas and who is asking what questions

What kind of question ?	Effectiveness	Reliability	Legitimacy
Who is asking?	Donors	Donors	Political Opponents
	Governments	Sector Associations	Advocacy partners
		Partners	Academics

Accreditation is a process wherein the very basic questions pertaining to VOs functioning like identity, area of work, years in operation etc can be captured to basically answers

some minimum questions relating to Reliability and Legitimacy. The process would result in classification of VOs, establishing a minimum benchmark and give them identity.

Rating of VOs goes beyond accreditation in as much as it captures the effectiveness/output domain as well as delves deeper into issues of reliability and legitimacy. Typical questions to be addressed in a rating exercise would be:

- How is democratic governance exercised?
- Whether the funds have been used for specified purpose?
- Assessment of organisational capacity to undertake future programmes as per its vision
- Whether the organisation has basic financial statements?
- Are the financial statements prepared in line with standards with correct treatment of various assets and liabilities?
- The outreach and effectiveness of interventions undertaken including client satisfaction with services provided

The effectiveness question is akin to social audit, wherein it has to be determined as to whether the systems, processes and outputs are in line with the stated mission and objectives of the programme.

The assessment of financial aspects in rating of VOs has to be substantially different from the rating of 'for profit' organisations. The focus in case of VOs has not be on judging their profitability or credit worthiness but its *trustworthiness*.

As rating involves added dimensions and goes into the question of assessing the performance, it has to be a scalar process as against the binary process of accreditation. ***Further, while accreditation could be the requirement of all NGOs, the process of rating should come into picture when public funds are used to fund VOs. The optimal use of public funds reflecting the accountability paradigm is both a need and a necessity.***

Cost factor also differentiates accreditation with rating. While accreditation being a basic check, its costs are limited and can be covered by levying membership fee, rating of VOs through professional external rating agencies would involve a cost. As such, the NAC has to decide on what should be the cut off financial assistance beyond which an external rating would be required.

Further, as rating VOs involved in diverse sectors would involve setting sector or sub sector benchmarks, there is no off the shelf product available in the market. Planning Commission and NAC would have to assign the task of building sector specific rating grid to rating agencies like M-CRIL<sup>2</sup>. The exercise would have to be in close association with agencies like CAPART and VOs themselves. Sceptics would argue that this is an impossible task, but the recent example of mainstreaming rating of microfinance institutions and evolution of sector benchmarks is an example. It has enabled the sector to grow exponentially as greater transparency and confidence has enabled channelization of funds in a greater measure.

If there is some kind of professional rating of NGOs, it would help both donors and NGOs. Donors, because they would feel more reassured about where their efforts and money are going and also how they are being leveraged. From the NGOs point of view too, ratings are good because they force them to become more accountable and professional, apart from drawing in more resources. **Hence ratings would help donating become less of 'charity' and more of 'support'.**

### **Funding framework**

As indicated earlier, ratings would involve a cost. This leads to question on – who bears the cost? To answer this, it is worthwhile to remember the scenario in mainstream financial markets. Recent global economic crisis has demonstrated the need for sound financial oversight which includes raters with impeccable integrity. Post crisis many questions were raised on the integrity of rating process as highly rated entities started melting one after another. Questions have been raised on this flawed business model, wherein there is a distinct possibility of conflict of interest. Financial Times, London in its article, 'How Moody faltered<sup>3</sup>' presents this dilemma as Moody went for higher market share and profit maximisation.

To avoid such dilemmas, it is imperative that rating mechanism for VOs is backed by a business model wherein the rating is commissioned by the funder rather than the entity receiving funds. This is also borne out of the practical realities as VOs are 'not for profit' entities and many of them lack resources to bear the cost.

Donor agencies other than state agencies would also find the rating mechanism of use in making their funding decisions, rather than going for their own due diligence. To operationalise a funder driven initiative, the following broad steps are suggested

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<sup>2</sup> Micro Credit Ratings International Limited ([www.m-cril.com](http://www.m-cril.com))

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- NAC should be the body administering the rating fund, empanelling rating agencies and deciding on fee structure in consultation with the rating agencies
- The funder agency (Government ministries/departments) making use of VOs in implementing programmes and providing funding support should be free to use any of the accredited agency for rating.
- The rating reports should be displayed on NAC website for wider dissemination.
- The corpus of rating fund to be maintained by NAC can be built through
  - ✓ Annual Contributions from Government ministries/departments like Ministry of Rural Development.
  - ✓ Contributions from donor agencies active in India.
  - ✓ Contributions from Apex agencies like NABARD, SIDBI, CAPART which increasingly fund VOs to implement development interventions
- The fund requirement can be assessed based on the market assessment. For an estimate, rating of 2500 VOs @50,000 each would require a fund of Rs 12.50 crore. The amount in isolation may appear high, but has to be seen in the context of financial flow to the sector and the objective assessment to be provided by such an exercise. A small cost for ensuring accountability in allocation of public funds.
- Going ahead, NAC can also think of having revenue from selling rating reports to interested parties.

If broad consensus evolves on the subject, detailed work will have to be done on designing the structure of rating fund at NAC, its financial model based on market assessment, funding guidelines as well as process flow.

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