XLERANT

Budgeting Brief

Mission-Driven:
Budgeting Success in Nonprofit Organizations and Associations

NON-PROFITS: ENRICHING OUR SOCIETY

Nonprofit organizations and associations enrich our lives in innumerous ways – addressing social problems and community needs while creating an opportunity for service, volunteerism and philanthropy. And contrary to common misconception – nonprofits contribute significantly to the nation's economy employing approximately 10% of the private workforce (approximately 10.7 million employees) – the third largest workforce in U.S. industry following manufacturing and retail trade.1 In fact a study by the Urban Institute reveals that since 2008, the nonprofit sector has grown faster than business and government sectors in both wages and employees.[2] And this growth is expected to continue.

A 2012 report from the Nonprofit Finance Fund[3] showed 85% of organizations surveyed experienced an increase in demand for their services, and the 2013 Nonprofit Employment Trends Survey[1] found that 44% of nonprofits surveyed planned to create new positions. As noted in this report: "These studies illustrate that nonprofit services remain in demand even during difficult economic times. In response to this demand, it is likely that the sector will continue increasing its workforce in the coming year."

UNIQUE CHALLENGES OF BUILDING SUSTAINABLE PROFIT IN A NON-PROFIT WORLD

As most of us learned as children, doing the right thing, for the right reason, the right way – is rarely the easy thing to do. And for mission driven non-profit organizations and associations the path to sustainability is not an easy one. While some of these challenges are the same as those shared by any business – most of the challenges in the non-profit sector are unique, requiring innovative strategies and solutions. Adding to the complexity, many of these challenges are intertwined and inter-dependent – requiring a thoughtful, holistic approach to this delicately balanced financial ecosphere. And while these challenges are numerous – this document is limited to a few key issues that have a significant impact.

> "Our organization is like most nonprofits – we never have as much money as we would like to accomplish our mission. So I think budgeting is really critical to be sure that we're allocating the resources that we do have in the best possible way. And our budget really helps drive that decision-making process."
>
> - Jill Larsen, Treasurer and CFO
> Baptist General Convention of Texas

FIVE KEY ISSUES IMPACTING NONPROFIT BUDGETING, FORECASTING AND FINANCIAL MANAGEMENT:

1. Culture

While culture is one of the strongest assets of a mission-driven organization – it comes with certain inherent challenges. Non-profits often attract passionate employees dedicated to a cause, and this natural self-selection process (coupled with variables such as grant funding requirements) can result in an organization highly staffed with program and service delivery experts but with minimal operations infrastructure or expertise. In addition, this can result in an organizational culture that leans towards optimism – which, if unchecked, filters into financial decisions and forecasts. And occasionally, in an organization with a mission-driven culture dedicated to a cause – discussions around finances or operations can be dismissed as an impediment to getting the "real" work done. Furthermore, this dynamic can extend to the board, resulting in an advisory team of philanthropic or cause-oriented individuals who have minimal business experience or understanding of the budgeting and financial needs of a nonprofit organization or association.

2. Human Resources

For many nonprofits "staff" is a mix of full and part-time employees, volunteers and temporary workers. This personnel mix may be subsidized with consultants or outsourcing of key business functions for high cost or needed areas of expertise. While the challenges of managing this staffing model are obvious – such as accountability, the altruistic but transient nature of volunteers, and a lack of historical organizational knowledge (especially important for financial operations – such as budgeting and grant management.)

Turnover of direct employees is also a critical issue for nonprofits – according to a recent report the turnover rate for nonprofit employees is as high as 17%, with the biggest retention challenges occurring in the biggest areas of need, including direct services, program management and fundraising/development.

Nonprofit turnover can be driven by a lack of funding (a grant that is ending or a drop in donor income), and on the opposite end of the financial spectrum – it can also be driven by an improving economy. The slow, continuous improvement in the economy, and the growth in the nonprofit industry as a whole – is increasing demand and competition for qualified employees. But for nonprofit organizations burnout is also a driver in employee attrition. One study finds that, "When staff are eliminated 74% of the time responsibilities are picked up by current staff".[1] But turnover is not just driven by workload – it may also be work "type". A study by Carolyn Dewa at the University of Toronto found that "employees in the nonprofit sector may be particularly vulnerable to burnout given the mission- driven nature of their work."[4] Turnover may also be exacerbated by the limited human resources infrastructure in these organizations, which has resulted in a lack of retention strategies (only 10% of nonprofits reporting the presence of an active retention program[1]) despite the critical role of staff for program delivery and sustainability.

3. Communication

Effective communication is challenging for any company – but the issues discussed in the previous Culture and Human Resources sections complicate communication for nonprofits. Ensuring all members of the organization understand the strategic plan is critical for success – but can be especially challenging with volunteers, part-time staff, and a consistent stream of "new" faces. In addition, the lack of historical knowledge can make it challenging for a new team or program lead to successfully step into the budgeting process – not to mention managing the detailed tracking of grant requirements like expense reporting. In a nonprofit, regular internal communication builds a spirit of collaboration and inclusion. And providing a channel for two-way communication increases engagement and ownership.

4. Funding

The financial barriers and challenges facing nonprofits and associations in the quest for sustainability are so varied and so complex, a simple list does not begin to capture the scope or impact. Some of the more obvious "suspects", include issues like:

- Visibility and competition for donations
- Loss of donor support (individual and corporate); donor fatigue and skepticism
- Variability in membership dues due to a shifting economy or member interests
- Lower returns on investment income
- Timing of income (tied to annual grants, fees, etc.)
- Reductions in grants or changes in the interest/focus of grant foundations

In addition to financial limitations – including restrictions in where and how funds can be spent – grants present a significant administrative burden with highly specific reporting and accountability requirements.

In many nonprofits, funding is further complicated by the reliance on the role of the development director for donor funds. As mentioned in the Human Resources section, this role experiences one of the highest turnover rates in the nonprofit world – and often results in long vacancies. Median vacancies for the development director position average 6 months, and among smaller organizations, median length of vacancy jumps to 12 months.[1] Part of the reason for the long vacancies is that the pool of qualified development directors is much smaller than the demand. But one study reveals that many Development Directors report they do not feel included in strategic planning and have little input into annual budgeting[5] - which contributes to a lack of ownership and inclusion in the organizations they serve.

5. Technology

Information technology or "IT", has traditionally been a challenge for nonprofits for many of the reasons discussed above. Lean budgets (often driven by grants that didn't cover overhead or infrastructure costs), coupled with a staff that is expert in program development and delivery (but not necessarily "high tech"), contributed to low interest and even less funding for investment in this area. Additionally, with small operational teams – technology planning and evaluation was not usually an expertise available internally.

But the last few years have shown dramatic changes in technology adoption. Cloud-based software solutions have resolved many of the traditional barriers to adoption, providing nonprofits with an affordable, relatively low-risk, and low-maintenance solution. And it's a solution many organizations have turned to as they seek new social media channels for increasing awareness of their mission, managing fundraising, increasing transparency and relevance to their donor and volunteer base.

However, investment in business management solutions continue to lag – perhaps due in part to the mindset that operations is "overhead" rather than an essential part of program delivery. This is especially true when it comes to budgeting and forecasting solutions, as many nonprofits continue to execute budgeting in the "no-cost" Excel environment. The "do-it-ourselves", lean grassroots culture is so ingrained in many organizations that they don't consider the true cost of this approach – both in time spent managing spreadsheets and manually tracking critical grant expense/personnel requirements, and in the financial cost (and liability) of errors associated with spreadsheets. (Studies show nearly 9 out of 10 spreadsheets have errors in them, adding up to mistakes in an incredible 88% of all spreadsheets.[6]) Errors that nonprofits simply cannot afford.

NAVIGATING NONPROFIT BUDGETING: STRATEGIES FOR SUCCESS

The Nonprofits Assistance Fund describes budgeting as: "Just another version of a mission statement or strategic plan expressed in a different language, the language of numbers. In order for this to be true in practice, a budget must be the cumulative effort of all who implement the organization's mission, including key leaders from all areas of the organization – board members, program directors, executives, HR leaders, and finance staff."

While this approach may be easier to articulate than to put into practice, there are a number of strategies that can help nonprofits improve the budgeting process – and increase sustainability by ensuring the entire organization is executing on the strategic plan:

BENEFITS OF PROGRAM-BASED BUDGETING:

- Accurate insight into the true "total" cost of an initiative or service offering
- More informed decision making
- Increased transparency for grant and donor reporting

›››› Program Based Budgeting: Most organizations follow a traditional department-based budgeting structure. However, for nonprofits program-based budgeting (also called strategic-program budgeting) offers unique advantages. A program-based approach provides transparency into the true costs and profit (or loss) of each outreach initiative or service offering – enabling non-profits to make informed decisions on the value of that program to the overall mission, vision and strategic plan. (Many organizations will opt to continue initiatives that operate at a loss – but can do so with clarity about the true cost of that decision.)

This approach also provides external organizations and non-financial advisors transparency into operational or overhead expenses (such as outsourcing, staffing, benefits, etc.) by tying these costs to the individual program served. This level of scrutiny also encourages managers to run programs more effectively and efficiently – and makes the overall budget process easier for them to understand.

›››› Scenario Planning:

Compared to an expense-first approach, scenario planning helps nonprofits account for their own unique fundingsituation. For organizations with varying or uncertain year-to-year revenue streams (which grants will be won, which donor will increase or decrease their annual gift, etc.), scenario planning offers the opportunity to build real-life budgets that account for each potential circumstance.

As described by the ASAE Center for Association Leadership: "Focusing on expenses first only encourages budget planners to inflate revenue numbers." For example, "Many managers start budgeting by adding new activities, estimated pay raises and new staff positions to last year's budget to determine what it will cost… [then] they'll automatically increase projections in several revenue categories to balance the budget. An alternative is to begin the budgeting process with the revenue side of the budget."[8] By applying "what-if" scenarios around anticipated funding, nonprofits can develop a proactive and realistic plan of programs to be cut or funded and the associated staffing implications of these decisions.

BENEFITS OF COLLABORATIVE BUDGETING:

- Increased motivation & ownership
- More accurate budgeting results
- Improved quality of forecasts

›››› Collaborative Approach:

The mission-driven culture and hybrid staffing model of nonprofits make them uniquely suited to a collaborative budgeting approach. Collaborative budgeting empowers the people who are impacted by a budget to be actively involved in the budget creation process. Collaborative budgeting is at the core – a communication process. Leadership communicates the strategic plan, objectives and goals. And then the budgeting managers use their individual area of expertise and front-line experience to build a budget designed to achieve that strategy. It is a bottom-up approach that lends to the creation of budgets that are more achievable than top-down budgets imposed on a company by senior management.

This style of budgeting is better for morale and tends to result in greater efforts by employees to achieve what they predicted in their budgets. A collaborative budgeting model requires employees to own their numbers and to take accountability for their decisions, leading to a stronger sense of connection and commitment to the organization.[9]

Following this system, employees are likely to feel their concerns are heard and respected. Even if they don't ultimately end up with an ideal budget, all parties understand each other's outlook and expectations and can work together to make the most of the budget they have."[10]

This approach can increase employee engagement – an especially important benefit with the high turnover rates in nonprofits, where employees are often a critical resource. In addition, a collaborative budgeting approach can improve engagement of perhaps the most important funding resource: the Development Director – increasing ownership in the organization's annual strategic planning and communication process.

›››› Purpose-built Technology:

For nonprofits, where operations is often treated as "overhead", business management software is the last bastion of investment. Many organizations still use Excel for budgeting because Excel is seemingly free. However, there is a high cost paid for errors from broken links, incorrect formulas, and time spent manipulating spreadsheets instead of analyzing data and managing to strategy. This is especially relevant in nonprofits – where an error in budgeting or grant management can be financially devastating. In addition, most employees (whether full time staff or volunteers) are not familiar with Excel and find it challenging to work with – so rather than being engaged in the budgeting process they dread it and/or rush through as quickly as possible.

Sound financial management is the heart of a nonprofit organization's viability and long-term success. Budgeting software can simplify complex expense tracking – enabling nonprofits to achieve more accurate forecasts with easy monthly reconciliation. And other mission-critical processes that are time-consuming and difficult in Excel (such as scenario planning and personnel allocations) become easily executable with just a few keystrokes – providing valuable, and actionable insight for senior management. A dedicated budgeting solution can also improve transparency for financial reporting to boards and outside entities – including donors and grant agencies.

Perhaps most importantly for nonprofits – purpose-built cloud-based budgeting software solutions engage employees, empowering them to make more informed decisions – and helping the entire organization to achieve the strategic plan and mission. Purpose-built software offers user-centered design which makes the budgeting process more intuitive for non-financial staff, as well as improving communication with the ability to capture notes that detail and justify the reasons behind each decision and budget item. In addition, the system can capture and maintain this historical data – easily allowing a new employee to step in and pick up a program or departmental budget at any point in the process.

ABOUT XLERANT

Purpose-built Budgeting and Forecasting for Mission Driven Organizations

XLerant, Inc. helps nonprofit associations and organizations achieve strategic budgeting and forecasting success with BudgetPak, a cloud-based SaaS solution. BudgetPak's user-centered design and built-in intelligence pave the way for engagement and empowerment by giving employees the tools for flexible and reliable budgeting, forecasting, and reporting. This user-friendly solution does more than make the process easier – it provides a platform for communication of the organization's annual objectives and ensures managers are building their budgets against those objectives.

Because BudgetPak doesn't force users to think in a restricted 'row and column' Excel format, it is a more engaging experience for non-financial staff. At the same time, BudgetPak allows Finance to control the aspects of the budget that are important to them within a straight-forward finance-friendly format, and direct integration with Excel for analysis in a familiar environment.

XLerant offers a full suite of modules built into BudgetPak including expense planning, revenue planning, headcount, salary planning and asset planning, as well as approval workflow, what-if scenarios, out of the box reporting, variance reporting, and custom reports. A unique feature called ActionPaks allows users to budget multiple line items at the same time for their department or program-specific projects and initiatives. If the project is not approved, all the dollars across all of the affected line items are removed from the budget with one click.

For more information about XLerant, and our work with mission-driven nonprofit organizations and associations contact info@XLerant.com and visit www.XLerant.com

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> "We believe a system that has budget intelligence built into its core makes for a more robust and user friendly process for everyone involved – which ultimately delivers more meaningful results."
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> ~Joanne Brunn
> CEO, XLerant