

# Using a Balanced Scorecard in a Nonprofit Organization



Here's how to adapt this powerful tool to transform your organization.

By Joel Zimmerman

“Balanced scorecard” has been a corporate management buzzword for about a decade. Like many management movements, it's migrating from corporations to nonprofit offices.

The idea of creating a balanced scorecard is as valid for nonprofits as for businesses, but it must be modified to make it work effectively in the nonprofit world. In this article, we'll look at what a balanced scorecard is all about and how to apply the idea to your organization.

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## The Reason for a Balanced Scorecard

Historically, organizations have measured their performance mainly, if not totally, with financial measures. In the 1990s, a group of researchers and consultants from the Nolan Norton Institute, the research arm of the accounting firm KPMG, began to study commonly used performance measures. Their hypothesis was that these practices were hindering organizations because the measurement focus was too narrow.

The study confirmed their suspicions. After careful analysis, the

researchers suggested that leaders ought to balance the way they assess their organizations by looking at more than financial performance.<sup>1</sup> The original balanced scorecard, which has been carried forward formulaically by most companies that use it today, was organized around four perspectives:

- financial
- customer
- internal
- innovation and learning.

## Common Mistakes

Rather than understanding what a balanced scorecard is supposed to accomplish, why, and how, many managers simply implement it as if it were a recipe. While the technique described in professional literature accumulates the wisdom and experience of many people and represents a form of best practice, it shouldn't be copied blindly under the assumption that one size fits all. The four dimensions (financial, customer, internal, and innovation and learning) can and should be modified to fit an organization.

Other common mistakes are jumping into a measurement program too fast and making the program too complicated. Deriving meaningful measurements, gathering reliable data, developing useful analytical techniques, and educating managers about how to use the data are all difficult steps. Doing everything at once with a bucketful of 50 different measures is doomed

to failure. Managers who don't have experience with measurement programs, or fail to heed the warnings of those who do, typically underestimate the difficulties of using a balanced scorecard program.

## Creating Organizational Measures

Despite the pitfalls, the balanced scorecard is a valuable management tool. You can use it successfully if you take a thoughtful approach to the process.

The real trick behind any measurement program is to figure out first what you want to measure, and then how to measure it. Many times, managers who want to evaluate their work groups simply jump into collecting measures, not because the measures relate to organizational attributes in which they're interested, but because the measures are simple and available. Thus, managers build assessments based on measures such as attendance data, production records, budget deviances, and computer system up-time. When you build an assessment program around the measures you have available, instead of building metrics<sup>2</sup> around concepts you need to measure, then you have a classic case of the tail wagging the dog.

You can tell what's important to measure by referring to your organization's strategic plan. The plan lists your goals and the strategies by which you hope to achieve them. Goals relate to outcomes, and strategies relate to procedures.

Measures can and should relate to both. Process measures reflect how well your organization is executing its strategies. Outcome measures show how well your strategies actually accomplish their intended results.

In short, start with planning; then create a measurement process to gauge how well you're executing your plan. When you build your measures around your plan, they'll do more than provide data. They'll become the basis for a management tool.

For example, suppose you decide it's important to have a larger base of active donors. In your strategic plan, you set a goal of expanding your donor mailing list by 25% over the year. As one of your strategies, you plan to do aggressive acquisition mailings using several new rental lists.

You can collect *process* measures indicating how many acquisition mailings you do and how many use the targeted lists. You can examine the increase in your house file as an *outcome* measure. These are excellent measures because they relate directly to what you intended to do and what you hoped to accomplish.

Your mail list manager also may give you many statistics describing your donors' demographics. What about using those data for a balanced scorecard? Sure, these measures are readily available; but do you need them? The question isn't "What statistics are available?" The questions are "What have we planned to do this year? How have we planned to do it?" and then, "Does this statistic help us answer either of those questions?" For a balanced scorecard, you should use only those metrics that relate directly to your organization's planned processes and targeted outcomes.

### The Balanced Scorecard Categories

Like any tool, a balanced scorecard is a means to an end, not an

end in itself. In some organizations, however, a higher power simply mandates that the organization shall implement a balanced scorecard. In this case, the balanced scorecard foolishly becomes the end in itself. Eventually, the management group will realize that the benefits accruing from the balanced scorecard (as they have implemented it) are too few to justify the work going into it.



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If you understand the ideas behind a balanced scorecard, you'll be free to modify the classic formula so it becomes a better tool for your organization. To make the balanced scorecard more relevant for nonprofits, you should also expand the original four measurement perspectives into six categories:

1. revenue and funding
2. resource allocation (including budgets)
3. product and service recipients
4. donors and board members
5. internal operations
6. staff development.

The first category—revenue and funding — is extremely important for any nonprofit organization. It includes fundraising approaches, investment strategies, alternative funding sources, fundraising costs, the use of fundraising consultants,

and so on.

The second category—resource allocation — involves financial and non-financial resources from an internal perspective. Organizations start the year with a budget, created to support their plans and reflect their priorities for the upcoming year. Alas, every year brings unforeseen events, changes in priorities, emergency allocations, and the like. Therefore, a complete budget plan should also include principles for budgetary reviews and, as necessary, reallocations. That's the focus for this category of measurement.

The third category — product and service recipients — relates to the "customer" category of the original balanced scorecard. In the classical for-profit company, a major goal is to satisfy customers, since they're the primary source of revenues. So, a balanced scorecard can focus simply on customers. The situation is more complex for nonprofits. Most nonprofits deliver some type of product or service, which often is the source of only a portion of revenues, and may be a source of no revenue at all. In a drug treatment facility, for example, customers (drug abusers) don't pay for treatment, and their satisfaction with the facility's treatment may be irrelevant to the most important measures of organizational performance. Nonetheless, even in such a case, the nonprofit is most likely concerned about how it interacts with service recipients and will want to measure that somehow.

The fourth category — donors and board members — also pertains to the original "customer" category, since donors and board members are treated as customers even though they probably don't receive the nonprofit's services. These are the people who contribute dollars, labor, and advice to support the nonprofit. It's their satisfaction, often more than that of direct service recipients, that's crucial to keeping a nonprofit operation going. It's therefore totally appropriate to separate out these two types of customers (service recipients vs.

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You can tell what's important to measure by referring to your organization's strategic plan.

donors and board members) within an organization's strategic plan and thus within the balanced scorecard.

The fifth category — internal operations — is fairly similar for for-profit and nonprofit organizations. It is, however, more critical for nonprofits. For-profits are concerned, of course, about the efficiencies of internal operations. Yet they plan to operate with a margin of profit, which, in poorly performing years, can simply slim down or disappear to cover the effects of less-than-optimal performance. In contrast, many nonprofits work on virtually no margin of error. A year of poor performance can result in dramatic cutbacks, since many nonprofits have no safety buffers built into their budgets.

The final category — staff development — addresses the fact that organizations need to continuously grow, adapt, and improve, and that future development is tied to the organization's staff. For most nonprofits, developing the organization means, in a literal sense, developing its employees.

### Putting It All in Play

Once you understand what a balanced scorecard is all about, you're ready to apply it. This is a multi-step process that's not for the weak of heart or the short of patience. While it does, over time, lead to more efficient and effective practices, the balanced scorecard requires an organization to invest substantial time, energy, and talent up-front to make it work well. Worse, if the balanced scorecard technique isn't well planned, the result is likely to be a disappointing waste of time with little to show for it.

If you're up for the challenge, here are your steps:

**1. Get your board and managers educated** on the basics and committed to the effort.

**2. Appoint someone on staff** to be in charge of creating and maintaining the balanced scorecard.

**3. Consider hiring a consultant** to help you implement a balanced scorecard (depending on your organization's size and the knowledge of the person you've put in charge).

**4. Build your scorecard categories** to match what's in your strategic plan. Or, build your strategic plan around the categories you'll use for the scorecard. Or, modify your existing strategic plan so it matches the scorecard categories.

**5. Derive the balanced scorecard measures**, metrics, and analytical techniques, and use them in test mode for two or three months.

**6. Use the test experience** to improve the balanced scorecard measures and processes.

**7. Collect, analyze, report, and archive scorecard measures** on a regular (monthly or quarterly) basis.

With a balanced scorecard, as with all management tools, the devil's in the details. The balanced scorecard is highly appealing in theory. In practice, it's a challenge to implement it correctly. If you can do it, though, the benefits will be substantial and fully demonstrable. ■

### Footnotes

<sup>1</sup>For the best single summary of this research, get a copy of *The Balanced Scorecard* by Robert S. Kaplan & David P. Norton (Boston: Harvard Business School Press).

<sup>2</sup>The words "measures" and "metrics" are often used interchangeably, but technically they aren't synonyms. A measure is a basic quantitative or qualitative evaluative label, derived through a specified process, and assigned to a fundamental attribute of a concept that you're trying to characterize. A metric is a derivation or combination of one or more primary measures. For example, a category 3 hurricane earns its designation by being in a certain spot on the earth and having winds that rotate in a particular direction with speeds over a predetermined threshold. For the hurricane, the category designation is a *metric*; the location, wind direction, and wind speed are primary *measures*.

### Resources

Dixon, Greta Kmarie, "Evaluating Nonprofit Programs: Now It's Essential," *Nonprofit World*, Vol. 12, No. 3.

Minnis, William C., "Four Steps to Evaluation Success," *Nonprofit World*, Vol. 23, No. 2.

Stout, William, "A New Way to Evaluate Your Organization's Performance: Measure Your Use of Time," *Nonprofit World*, Vol. 19, No. 4.

Tom, Baldwin & Bill Frentzel, "Performance-Based Management Builds Support & Funding," *Nonprofit World*, Vol. 23, No. 6

Vogt, Jean, "Using Your Outcome Measurement System," *Nonprofit World*, Vol. 18, No. 1.

These resources are available from the Society's Resource Center, [www.snpo.org/members](http://www.snpo.org/members). Also see Learning Institute programs on-line: Outcome Measurement ([www.snpo.org/lino](http://www.snpo.org/lino)).

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