The Not-So-Grand Grant: When the Best Response May Be "No Thanks" Why you should always look a gift horse in the mouth, and how to do it

By Terry L. Applebaum

The awarding of a grant, with its promise of new support, renews optimism and warrants a celebration.[1] This happy scenario can turn sour, however, if you don't take into account the grant's full ramifications. To keep your organization on an even keel, view the grant through these five lenses:

1. Focus on the Mission

A nonprofit's board, staff, donors, and volunteers share a common bond: a passion for what the organization does — its mission. Mission goes to the heart of an organization's purpose. Nonprofits convey their missions through programming, publications, and fundraising materials. Highly successful nonprofits go even further: They live their missions.

For a nonprofit to retain its integrity and the commitment of its people, the mission must pervade the entire organization. This principle embodies two tenets of nonprofit management: Mission drives the budget, and mission drives fundraising. Unless severe financial pressures move fiscal issues to the forefront, most nonprofits do a good job of establishing budget priorities that reflect their missions. Less clear is how effectively they rely on mission to guide fundraising. Two common scenarios cause difficulties:

- **A board member, staff member, or donor wants your organization to adopt a project and see it to fruition. The project has merit but fits only marginally under your organization's umbrella. Thus the dissonance.** You can resolve this problem by framing the issue in the broader context of what course best supports your mission.
- **Funding is available to meet your goals. Unfortunately, your organization doesn't have the same priorities as the funder.** You must resist the temptation to reshape your priorities to meet funding guidelines. This situation challenges you to hold firm to your commitment to the mission.

Pursuing grants that are only marginally linked to your mission is a risky road. Such grants may lead to short-term financial relief or meet the wishes of a few influential people. However, that path can erode your organization's commitment to its core purpose.

If this practice continues, you can find your organization's energies dispersed, trying to be all things to all people. Long-time supporters, sensing a lack of direction, will pull back or leave the fold entirely.

2. Know Your Actual Costs

Initiating a new program or expanding an existing one without knowing actual program costs sets the stage for massive losses — a harsh dose of reality, especially if you believed your organization was proceeding on a secure financial footing. Prevent such financial surprises by allocating costs, using two classifications:

- **Direct costs.** These are costs that you can easily trace to a particular activity. They may include staff, materials, or services, so long as they specifically benefit the activity.
- **Indirect costs.** These are the routine expenses of providing systems and equipment for your organization as a whole. Indirect costs include utilities, administrative salaries, maintenance on your building, and payroll services.

Sometimes an indirect cost benefits a specific program as well. How do you decide how much to allocate to a program? The best way is to discuss the issue with your staff, financial professionals, and managers with direct program responsibility.

Identifying relevant costs and allocating them to a program can be complicated. But it's well worth the effort.[2]

Regrettably, many donors restrict the use of their gifts to direct costs. Yet your organization must pay for rent, lights, heat, insurance, and salaries. Indirect costs can add up to a sizeable share of program expenditures. You should make every effort to present indirect costs as an integral part of your proposed program budget. Their inclusion serves an educational purpose: It draws attention to the true cost of running the program.

3. Control Your Budget

Budgeting is a dynamic process. Periodic adjustments are necessary to respond to special opportunities, unanticipated expenses, or changes in the competitive environment. But these adjustments mustn't throw a budget out of balance.

When building your annual operating budget, you work and rework projected expenses and revenues until budgeted revenues at least equal the amount budgeted for anticipated expenses. Contributed income typically makes up a large portion of total revenue, so receipt of a grant check brings a sigh of relief. The money will help reach the amount needed to pay for people, programs, and overhead on the expense side of the budget. Maybe.

When the budgeted grant revenue matches all corresponding expenses, that portion of the program places no additional financial burdens on your organization. To that extent, budget control remains intact. The arrival of a new grant, one not yet included in your budget, represents good news if some or all the funds can bring relief to the expense side. In this case, allocating indirect costs to the new grant takes some pressure off your overall operating budget.

Take care, however, that you don't double-count the new revenue. Suppose, for example, that a new $10,000 grant arrives with two restrictions. First, the donor wants the money used in the current fiscal year. Second, the terms preclude using grant funds to cover any previously budgeted expenses, including overhead. You must be sure you don't consider the new $10,000 as part of your originally

[1] In this article the following pairs of terms are used interchangeably: gift and grant, donor and funder, project and program.

[2] For more details on cost accounting for decision-making, see Cutt, McLaughlin, and Solloway in "Selected References."

budgeted annual fundraising goal. That dollar goal, derived as part of the budget building process, is already committed to cover originally budgeted expenses. Yet by year-end, your organization will have incurred $10,000 in new expenses. If you treat the gift incorrectly, your organization will inadvertently create a $10,000 operating deficit.

Mistakes can also happen when dealing with multi-year grants. For example, in the case of a $30,000 grant paid in three annual installments, the full $30,000 is posted as revenue in year one. If the remaining payments are again counted as revenue in years two and three, a $20,000 fundraising discrepancy results. In this instance, good financial management dictates establishing a three-year budget consistent with the three-year grant.

Single occurrences of such errors may have a relatively small effect on a larger nonprofit. For a small organization, the impact can be disastrous. Whatever your organization's size, repeated occurrences over time will result in trailing deficits that limit your ability to move swiftly in an ever-changing environment. Periodic budget reviews and ongoing conversations among those with executive, development, and financial responsibility can go a long way toward catching mistakes and dealing with them effectively.

4. Be Alert to Lost Opportunities

The decision to move forward with a project involves tradeoffs. Implicit in each decision is the lost opportunity to do something else. The loss of resources for the *next most valuable alternative* is what economists call "opportunity cost."

At first blush, opportunity costs may seem unimportant. After all, vendors don't bill for them, and customers don't pay cash in exchange for them. Be assured, while opportunity costs may seem illusive, their impact is real. Opportunity costs hinder resources for other projects, and the chance to invest those resources in a more compelling activity is forever lost. Benefits that might have accrued remain unrealized.

5. Guard Your Reputation

> ***Reputation is only a candle, of wavering and uncertain flame, and easily blown out, but is the light by which the world looks for and finds merit.***
>
> — James Lowell

A solid reputation is among your organization's most valuable assets. Committing to a project with a weak relationship to your mission, inadequate funding, unanticipated shortfalls, a drain on organizational capacity, and high opportunity costs is a surefire recipe for a diminished reputation.

If your staff, board, and supporters sense that a project has any of these problems, they'll move toward other activities. Program performance will suffer.

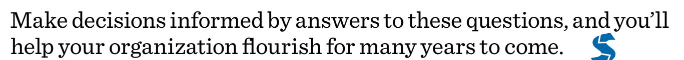
Word travels fast through philanthropic circles, and memories hold long. Years may pass before people are willing to support your organization again. On the other hand, a solid reputation will pay enormous dividends.

Make the Best Decision

A vast literature exists about how organizations make decisions. Assessing various courses requires study, thought, and time. As a start, test the viability of each possible path against four measures:

- **To what extent does this project support** your core mission?
- **Do you have the necessary resources** — people, time, energy, space, expertise, and money — to achieve successful results?
- **How will the project build capacity** vis-a-vis your programming, finances, and infrastructure?
- **What future benefits** — such as cash flow, staff morale, and reputation — will you give up if you invest in this project?

Make decisions informed by answers to these questions, and you'll help your organization flourish for many years to come.



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Should You Answer "Yes" or "No"?

Before committing to a new grant, ask yourself these questions:

Does it enhance your organization's mission?

Will it put pressure on your organization's capacity?

Does it take away resources from more promising activities?

Is it in line with your organization's top priorities?

Will it strengthen your organization's reputation?

Are the funds adequate to support the program in the long term?

Are you bearing in mind the program's indirect as well as direct costs?

Have you identified all restrictions that apply to the gift?

Have you included all costs associated with the project?

Are there better things you could do with your time and energy?

Selected References

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*Starred resources are available free at NonprofitWorld.org/members. Also see Learning Institute programs on-line: Resource Development and O for Opportunity: Exploring New Revenue Opportunities for Nonprofits (NonprofitWorld.org/LearningInstitute).