What You Need to Know about Your Finances

Safeguard your fiscal future with these guideposts.

By Ed Levin

No successful organization can exist without financial backing and good record-keeping for accountability. Consider the following to assure you have the funds and financial foundation you need to further your mission for the long term.

Keys to Financial Success

Establish good financial practices at the outset. Although a nonprofit may start small, the importance of setting up good record-keeping and governance policies can't be overstated. An essential first step for nonprofit leaders is to set up and work with a finance committee immediately, to make sure that they're fiscally responsible and recording expenses properly. Nothing can bring an abrupt end to a nonprofit faster than mismanagement of financial resources.

Nonprofit leaders also need to work closely with their governance group to maintain guidelines for ethics, policies, and procedures. For example, while it might be easy for a committee leader to suggest taking the board out to dinner instead of holding a meeting in the nonprofit offices, is that an appropriate way to spend the money? As your organization grows and increasingly becomes a steward of other people's money, you must consider adding financial policies that will endure scrutiny. One simple question to ask: Am I okay with the news of this decision being on the front page of the local paper?

It's also vital to establish an audit committee or hire an auditor – or perhaps, do both. You might consider bringing in outside expertise to move from a simple bookkeeping system to a more robust process as your organization grows.

These multiple layers of financial guidance and oversight help to safeguard your finances by showing that donations are properly accounted for and money is being spent appropriately. If you want your organization to last, you'll also need to consider longer-term strategies such as endowments, asset allocation, and rebalancing, especially if you want to attract donors likely to give larger amounts of funding year after year.

Assess cash flow needs and spending rate for both the short and long term. In the short term, examine your

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organization's needs for the next two to three years. You might ask: How much does the organization need to have, every year, in order to keep its doors open and fulfill its mission? What are overhead, staffing, and event expenses estimated to be for the foreseeable future? Once you have this information, it will be easier to identify how much money you must raise annually and how much establishing an endowment might help.

Simultaneously, consider your organization's longer-term needs. This gaze into the future should include looking at growth expenses, additional locations, research, and marketing, while also taking into consideration potential economic downturns.

If an organization fundraises, every year, only as much as is needed for its entire budget, it's doomed to fail in bad years. A good example is 2022-2023. At the end of 2022, the stock market was down, the bond market was changing, and donors didn't feel as wealthy as they did in the prior year. Organizations that didn't build the possibility of downturns into their planning were caught flatfooted, without the funding they'd planned to receive. It's critical to know what the baseline is and to try to raise that amount earlier in the year, as well as to know how an endowment can help.

Create an endowment fund, working with an attorney and financial advisor. An endowment fund is invested money that grows over time. It can help cover spending during those years when fundraising is more difficult.

For every organization, the percentage going into an endowment fund may be a little bit different. But the more that's endowed – maybe even 33 to 50% each year – the more it's going to assist with longevity. Leadership will worry less about the markets and current economy because they know the funding is there, generating interest that will help support the mission.

An endowment may cover some annual costs as well as some fundraising expenses, and it allows board members to think longer term and more strategically by knowing they have funding beyond the current year. In many cases, this fact changes the board from a management board to one that can leave day-to-day operations to the staff while it focuses on the future. Good planning far in advance can lead to longer-term success.

Assess allocation rates. For a nonprofit that's expecting to continue for the long term, what happens in the market today isn't as important as what happens over the next 10 and 20 years. Both investment allocations and asset allocations must be appropriate based on the amount of risk the organization can handle. Risk and allocations should be reviewed on a regular basis (quarterly, semi-annually, or annually, not every week).

> "An endowment allows board members to think longer term."

Be transparent. This requirement falls to the audit and finance committees. People who donate, especially those who donate large amounts of money or leave bequests, want to be able to see the nonprofit's financial records, and they care about ratings on Charity Navigator and Charity Watch. If the nonprofit has no audited records and doesn't disclose amounts on IRS Tax Form 990, financial advisors won't recommend it to their clients for funding.

Strategic Philanthropy Insights

Wealthy philanthropists have become much more strategic in how they choose to support nonprofits. Wealth is now being galvanized with the goal of contributing significantly to societal improvements or disruptions to the status quo, and philanthropists are looking far into the future, seeking the betterment of the environment, of healthcare, and of humanity itself. To attract these donors, you must show them the impact your organization can make.

Strategic philanthropists have four defining characteristics:

Innovation: Such philanthropists take risks that other types of funders might not support.

Evidence: They require evidence that the problem can be solved and that the nonprofit's plan is meeting milestones.

Collaboration: They look to see if other philanthropists, specialists, and institutional funders are joining, thus prioritizing the ability to achieve maximum scale and impact.

Scale: Their ambitions extend to solving larger, more complex challenges of a regional, national, or global nature.

Strategic philanthropy is designed to tackle the root cause of a problem. In doing so, the impact can be greater and certain problems may even be eradicated. The strategic approach may require much larger sums of philanthropic capital. Therefore, this movement by donors uses innovative financing vehicles for philanthropic purposes that incorporate pay-for-performance, results-based financing, and accountability measures.

Social finance is an impact-inspired category within philanthropy, whereby private capital is introduced into the equation to address substantial and pressing societal and environmental issues. Donors are "investors" in these models and look for the organizations they support to generate a measurable social (and sometimes financial) return.

Some philanthropists have a personal connection to a specific topic, issue, or geography. Others hope to create a change that will have a lasting, positive impact for their family or society. And others seek to embed topics that matter – to themselves, to other people, to the planet, and, perhaps, to their portfolios – into how all their capital is deployed to minimize risks and maximize opportunities. Ultimately, all of them are thinking about their legacy and how they want to leave the world or society in a better condition.

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Ensure Your Financial Longevity

If you stay fiscally responsible, you have a much better chance of gaining funds, managing your resources, and accomplishing your mission for the long term. You can gain further insights in these articles at NonprofitWorld.org:

Do Your Board Members Know Their Fiduciary Responsibilities? (Vol. 33, No. 1)

Avoid an Unwanted Auditor's Letter (Vol. 33, No. 3)

Investment Strategies for a Smooth Financial Future (Vol. 35, No. 3)

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Risk Management: How to Protect Your Assets (Vol. 26, No. 1)

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