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River Voices

Budgeting: A Plan For All Seasons

By Susan Schwartz, Director of Finance, River Network

Annual income twenty pounds, annual expenditure nineteen…result happiness. Annual income twenty pounds, annual expenditure twenty pounds ought and six…result misery.

— Charles Dickens

Budgets, simply speaking, are operating plans expressed in financial terms. Budgeting is a systematic way of allocating the financial and human resources necessary to achieve your strategic goals. The income statement describes the past. The balance sheet describes the present. The budget, however, is all about your future: it projects the costs of your programs and predicts the income necessary to finance those costs. In a volatile world, a sound budget is a pathway through uncertainty and may mean the difference between barely surviving and thriving.

Budgets have four important organizational purposes:

(1) To **quantify the necessary resources** to reach your goals and objectives.

(2) To help **predict cash flow** for better financial management.

(3) To **serve as an internal control** to alert you to unexpected variances.

(4) To help **identify operational strengths and weaknesses.**

Using budgets, the staff and the board can see problems in the making and develop thoughtful solutions. Budgets, as well as the budgeting process itself, is a critical tool for better programmatic and financial management and can help your organization achieve its mission with fewer unpleasant surprises and financial crises.

Types of Budgets

Organizations may use many different formats and models for budgeting. The budget for an organization with annual revenues of $50,000 will be different from that of one with $5 million. But while they may look different, all budgets have the same purpose: to help your organization avoid unpleasant financial surprises and ensure resources to fulfill your mission.

There are at least four (4) types of budgets relevant to nonprofits:

- The **cash flow budget** identifies periods of cash surplus and shortfall. If the organization receives its money at a different time of the year than when it pays out its expenses, it must know and plan accordingly for that timing difference *(pg. 12)*.
- The **operating budget** outlines your major sources (revenues) and uses (expenses) of funding *(pg. 13)*.
- The **grant budget** is a sub-budget or section of the overall operating budget, usually designed to meet the information and evaluation needs of a particular funder or program *(pg. 15)*.
- The **capital budget** details the cash needed to purchase large equipment and those major assets that will be depreciated over time rather than expensed in just one fiscal year *(pg. 17)*.

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River Network

Connecting People, Saving Rivers

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River Network is a national, nonprofit organization whose mission is to help people understand, protect and restore rivers and their watersheds.

From the President

credit: © River Network Collection

Most of us think about organizational budgets like we think about trips to the dentist. We know we should make them at least once a year, and we know it's a good idea to have a mid-year checkup. Even though we know we need them, we expect them to be painful at least some of the time, so we don't ever really look forward to them.

That's understandable, but there's a much better way to think about budgets. We should think of them as some of our most important tools for building healthy, effective, long-lasting organizations.

Building an annual budget forces us to think hard about resources—about how many we have, and about whether and how we can acquire more. That's reason enough in and of itself to develop good budget habits.

However, a good budget process does much more. It helps us connect our long-term goals to short-term actions and the money they require. It prompts us to talk about options, establish priorities and make choices. Sometimes the decisions it forces are important and difficult. Those tend to be the very ones we put off too long otherwise.

A good budget is more than just numbers on a page. It includes documentation of projections, decisions and the rationale behind them. Once built, a good budget gives us resources, goals, boundaries and guidance we need to perform well and manage responsibly on a day to day basis. Monitoring it regularly helps us measure our progress, giving us assurance that we are on track. It also helps us identify small problems and take corrective action before they become big problems.

Watershed protection is long-term work. It requires good planning, fiscal discipline and sound management, year after year and day after day. Organizations that succeed over the long term build good budgets and use them. We hope this issue of *River Voices* will help you build better, more useful budgets for your organization—and enjoy doing it!

Budgeting A Plan For All Seasons, cont.

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Roles and Responsibilities in Budgeting

Budgeting is unique to each organization in response to the specific staffing and volunteer patterns, organization history and cultural precedents. One formative factor in how the process looks is whether your organization is board-driven, staff-driven or a combination of both. In younger and smaller groups especially, the board treasurer often prepares the entire budget. In some, the treasurer works with volunteer committee chairs. In others, an executive director may work with the treasurer and/or committee chairs. When there is executive, program and development staff, they often will work collaboratively to prepare the budget to be presented to the finance/budget committee or to the board.

In order to produce an accurate financial plan, an organization should use a participatory approach to budgeting with the active involvement of many different people in the organization. This ensures the inclusion of more information and broader insights. At a minimum, board or staff should participate in any part of the budgeting process that impacts activities and materials for which they will be operationally responsible.

Both program and financial volunteers or staff should be involved from the beginning. Program planning is often viewed as the domain of the executive director or program staff. Fiscal management, meanwhile, is assigned to the finance director or the board treasurer. Consequently, each may not be aware of the importance of the other's approach to budget issues. Program planning may be seen as failing to reflect the economic realities, while fiscal decisions may be viewed as insensitive to the mission work of the organization.

To avoid last-minute ad hoc decisions, all key board members or staff should work together in the process to discuss plans and anticipated problems and co-develop budgets. Only with the necessary programmatic and financial expertise will the budget truly reflect joint priorities and be a useable guide for employing the resources of the organization.

Recommended Timeframe for Preparing a Budget

Since every organization will have different preparers and process, it is best to start by knowing the date of the board meeting at which the budget must be approved and count backwards, allowing enough time for thorough discussion and the necessary research for any new initiatives you are planning. One group, for example, planned to move to a new office and to hire a new program manager. That required both a survey of the commercial space market to identify average office rents and at the same time a small compensation survey to determine a competitive market rate of salary for the new staff position.

Month-by-Month Operating Budgets

If your accounting software permits, and you have sufficient information, it is very helpful to prepare monthly budgets that reflect the real timing of revenue and expense rather than simply dividing the annual budget into twelve equal parts. Your December special fundraiser should be included in that month, while expenses for that large May conference should be in May. If your insurance is due twice a year, the two premium payments should be reflected in those months, rather than in each of twelve months in your budget. By preparing monthly budget breakdowns and comparing them with actual dollars spent and received, you can far more accurately see problems and revise your planning

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THE ROLE OF THE BOARD

William Botzow, Treasurer
River Network

As board members, we are naturally most excited by what our organizations do to make the world better and by contributing to plans to restore our waterways and keep them that way for the benefit of all.

We also have another role. We safeguard the reputation and integrity of our organization. Those that fund our work put their trust in us, and we are legally responsible for the financial probity of our organization. This responsibility lies at the heart of what it means to be a trustee and a board member. The central instrument for carrying out that responsibility is the budget. We approve the budget, then monitor finances throughout the year and finally account for expenditures at year's end.

Most nonprofits have, or should have, a finance committee. Finance committees make sure that the budget supports the organization's mission and its tax-exempt purposes, and that donated and earned dollars directly connect to organizational goals and objectives.

Asking good questions during budget approval ensures realistic (not hopeful) revenue and expense projections and that dollars will be available throughout the budget cycle to support activities. We need to ask if initiatives have the resources necessary for success and will be sustainable. We need to ask if risks can be managed and not undermine essential operations.

Looking at budget changes from year to year in the specific areas we track such as salaries, travel, communications, etc. on the expense side or individual, corporate and foundation donations on the revenue side guide the realism of a budget. Carefully monitoring revenue and expense variances from budget as the year progresses stabilizes our organizations and prepares us for inevitable corrections.

Ideally, we strive for balanced budgets with surpluses. The ability to manage and protect those surpluses carries organizations through times when we need to approve deficit budgets in order to transform our organizations. If you approve a deficit budget, ask if you have the reserves in the bank to back them up. Ask if you have a plan to turn a temporary deficit into a sustainable surplus.

The assumptions we make when we write, approve and monitor budgets will ultimately be accounted for in our IRS reports and audits. Board members must be sure sensible policies are in place for handling and recording dollars in and out, for using reserves and ultimately for professional oversight at year end.

Prudent realistic financial management gives stability and certainty so we can continually evolve our work and build credibility for our organization.

Budgeting A Plan For All Seasons, cont.

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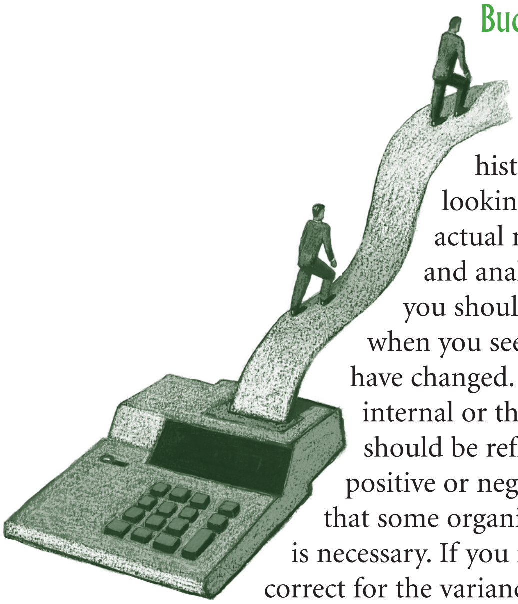
accordingly. Such monthly budgets are also the major step toward creating your cash flow budget, which is essential to prepare for any cash shortfalls.

Budget Adjustments



To be useful, a budget must be a living document and not an historical relic. If you are looking at your budget verses actual numbers each month and analyzing the variance, you should reforecast the budget when you see that circumstances have changed. Changes in the internal or the external environment should be reflected. Variances—positive or negative—may also signal that some organizational intervention is necessary. If you must change courses to correct for the variances, you want the budget to reflect new programmatic or administrative plans. If these factors are not considered and the numbers adjusted accordingly, the document will no longer reflect your organizational reality and will not provide a meaningful tool for evaluating your operational efficiency. Worse still, you may miss the opportunity to correct errors and deficiencies. Revision on a semi-annual basis is, therefore, highly recommended. Be certain that the revision process is as carefully controlled and structured as the original in order to maintain accuracy and accountability.

Other Considerations

As with all organizational initiatives, communicate, communicate, communicate. Present your plan—the budget—in a clear and thoughtful written document for board, staff and volunteers. Be certain they really understand what it says.

- What story does your budget tell the external world about you?
- Does your budget look almost the same as last year's? Different? Why? Why not?
- Should your budget be revised and updated?

Final Considerations

Does it all add up correctly? This is probably stating the obvious but it should be rechecked. Take the time to be sure that 2+2 equals 4 and not 3 on your budget. If using software like Excel, it is easy to omit a cell in a spreadsheet, which will impact one or more totals. Or, if you use your good old-fashioned calculator, add the numbers again to be sure that you get the same sub-totals and totals the second time around.

Do your numbers pass the "sanity test"? Take a moment to ask yourself if your numbers make sense overall. Are new activities or staff included? Are operational changes reflected? Do your total income and expense costs in total seem reasonable in light of what you know about the organization?

Explain your budget. Always include a thoughtful narrative that gives a summary overview of your budget. At the very least, your budget narrative should discuss any significant increases or decreases compared with last year's budget and any other material numbers. For example, if your $500,000 organization has a $20,000 increase in office rental, explain that change. A rule of thumb is to explain any difference in excess of 10%. The more information and footnotes provided, the easier it will be to review and evaluate any variances that occur during the year.

Top-down verses Bottom-up

Budget Process Models

Organizations with more than one program utilize a variety of models for developing budgets. Four common models are described below. Your board and staff may want to consider trying a new method, or using a combination of methods.

Bottom Up: Program Manager Driven

Program Managers develop budget proposals for all program costs. Fiscal Manager supplies information on proposed administrative cost share and all share costs (occupancy, phone, etc.).

Fiscal Manager reviews Program Manager's proposals for consistency with agency policies and prior years' experience. Fiscal Manager combines program proposals with administration budget proposals and works closely with Development Director or Executive Director to project revenue.

Fiscal Manager and Executive Director prepare recommendations regarding revenue and expense options for discussion by Board Finance Committee which then makes recommendations to the full board.

Top Down: Fiscal Manager Driven

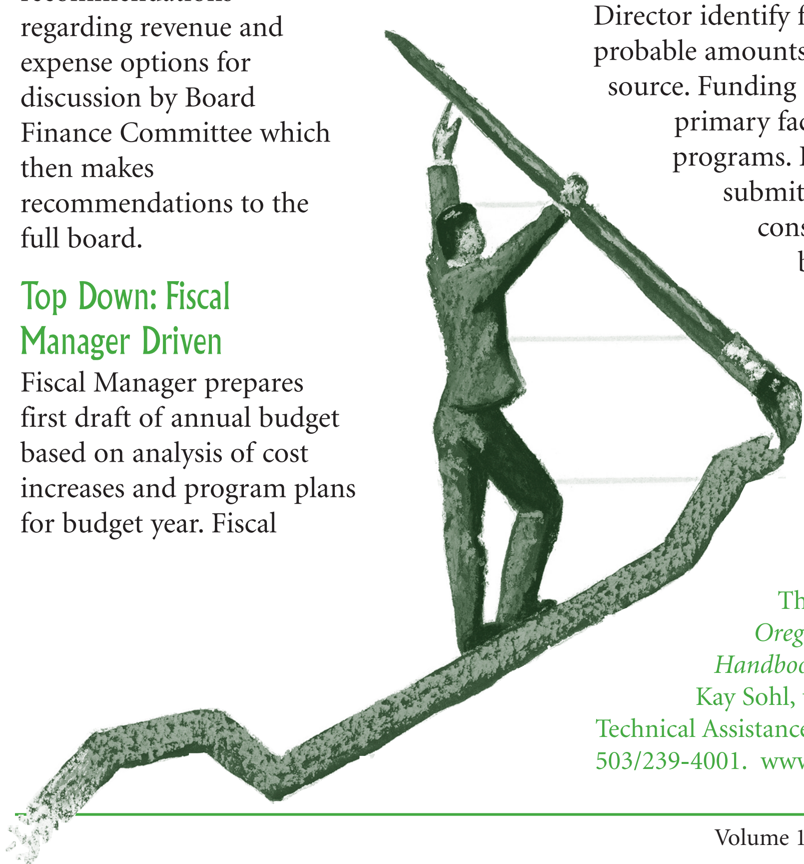
Fiscal Manager prepares first draft of annual budget based on analysis of cost increases and program plans for budget year. Fiscal Manager circulates draft budget among Program Managers for feedback and input. Fiscal Manager proposes revenue projections based on committed funds, prior years' experience and input from Development Director and Executive Director. Fiscal Manager presents proposed budget to Executive Director who presents draft to Finance Committee for review and recommendation to the board.

Board Driven

Board planning process identifies service priorities and revenue generation strategy for coming year. Fiscal Manager develops cost proposals reflecting board priorities after seeking input from Program Managers and Executive Directors on implementation plans for board identified priorities. Fiscal Manager and Executive Director develop options or key choices for Board Finance Committee.

Development Driven

Development Director and Executive Director identify funding strategy and probable amounts to be raised from each source. Funding availability becomes primary factor in design of programs. Program budgets already submitted to funders are consolidated to create agency budget. Board Finance Committee review budget prepared by staff and recommends board approval.



This information is from the *Oregon Nonprofit Corporation Handbook* by Cynthia Cumfer and Kay Sohl, used by permission of Technical Assistance for Community Services, 503/239-4001. www.tacs.org.

Realistic Income Analysis

Projecting Revenues

by Don Elder
President
River Network

Confidence in ability to produce is a virtue shared by most good fundraisers. But fundraising confidence is a virtue only up to a point. In excess—especially when not tempered by budgeting procedures that require reality checks—it can lead an organization to disaster.

Clearly, overly ambitious revenue forecasts can lead an organization to ruin. On the other hand, so can overly *cautious* forecasts that force unnecessary cutbacks in people and programs. How then can those building budgets find a responsible middle of the road? While there is no simple, cut-and-dried answer, there are some principles upon which better budgets can be built.

1 **Establish a financial reserve.** Because no revenue forecasting system will ever be perfect, the first rule has as much to do with financial management as fundraising. Some margin for error needs to exist. I recommend about six months' operating expenses—more if the organization is very dependent on highly restrictive, irregular sources of funding such as government contracts and foundation grants. If the reserve must be tapped, the first priority for the following year should be to restore it.

2 **Begin revenue projection work early in the budget process.** It's hard to think clearly and objectively about revenues for the coming year once an expense figure is already developed. By then, it's almost impossible *not* to start generating revenue numbers based on wishful thinking. Given a specific number—say, $300K—to hit, many boards and fundraisers will immediately begin thinking backwards: "Let's see, that means we just need $200K from foundations and $60K from individuals and $40K from our annual bake sale and we'll be all set. Let's get to work!" If only it were that simple and easy.

Long before you generate an overall organizational expense figure, develop the rationale, procedures, documentation and workplans to support the initial revenue projections for the coming year. They can be further developed as the budget process continues, and they *must* be further developed if the revenue projections are increased. But the foundation should be laid very early in the budget process, as independently of expense considerations as possible. I recommend beginning the revenue projection process at least one month earlier than the rest of the budget work.

3 **Consider the unique characteristics of different types of funding sources.** Some revenue streams are far more reliable than others. For example, if you already have 2,000 individual members averaging $30 each per year, you may project at least $50,000 from them with a high degree of confidence. But if you are hoping for renewal from two foundations and one major donor that together gave $60,000 this year, be much more cautious about putting $50K from those three sources in next year's budget.

4 **Look at revenue potential from several different angles.** All fundraising projection methods are simply models. Like all models, they have their limitations. Consider running your numbers for the coming year using two or even three quite different methods. For example, you might look at projections for foundations or major donors in terms of *likelihood of a gift of a certain size for each prospect* (i.e., 60% chance of a renewal of $10K = $6K projection for a particular donor); *a pyramid of most likely to least likely gifts* (i.e., $100K from two donors who have made firm $50K pledges, at least $50K from 12 highly likely donors who

have averaged $5K apiece in recent years, and at least $15K from 75 brand-new prospects for $1K gifts); and *historical performance* (i.e., no increase from foundations as compared to last fiscal year, and no more than a 10% increases from all other sources.) Each of these methods is legitimate (if based on reasonable assumptions and good data), but they can generate very different results. Don't bet the farm on one method whose results are much higher than the others. Also, keep in mind that the more donors you have, the more the odds tend to even out. If you have just a few donors in a given category, and if even one of those is a big wild card in your projections, be especially cautious.

5 **Be clear about the assumptions upon which each projection rests.** Whatever method or methods you choose, write down the assumptions behind them. Share them with board and staff. Refer to them often as the year progresses. Each time a major assumption is proven true, celebrate! If a major one proves to be false, step back immediately and reassess. Don't wait until the end of the year to do so. Quick corrective action—some supplemental fundraising strategy, some expense-cutting measures or both—may be in order.

6 **Don't rely on windfalls—and when they come, use them differently**. A well-rounded, well-run fundraising program tends to generate some nice surprises most years. Don't count on them. For example, if an individual donor has been speaking with you about the possibility of a major one-time gift, don't include it in your annual budget projections. Even if it arrives in the amount and at the time expected, you will be better off if you weren't counting on it to meet this year's budget, because it will not come again next year. As long as doing so is consistent with donor intent, it's far better to use windfalls for special purposes, such as building reserves or endowment, that will enhance your organization's efforts for many years to come.

7 **Plan to exceed projections.** While relatively cautious projections usually make sense, they should be accompanied by the most aggressive fundraising plans possible. Fundraising goals should be greater than, not equal to, your budget revenue figures. Aim to exceed budget figures nine years out of ten. When revenues are almost always greater than budget projections, it is much easier for fundraisers and everyone else to do their jobs well. Why then do so many organizations set budget figures that they believe they have only a 50% chance of exceeding?

8 **Decide in advance what major events will trigger what expense management decisions.** This reassessment will be faster and easier if you have decided in advance what events (or non-events) will trigger what actions. For example, a 20% shortfall in individual giving during the holiday season might be reason to scale back some program activities. Non-renewal of a major corporate donor might be reason to modify or eliminate the program it funded. On the other hand, receipt of a pending grant that wasn't assumed in the budget might allow specific, predetermined expansion to take place. In addition to providing clarity for program staff and board, advance decisions of these kinds help fundraisers prioritize their efforts.

Adopting these principles will not remove all uncertainty from revenue projections. Nothing will. But it can help move an organization from guesswork, boom-and-bust cycles and crisis management toward a much steadier, more productive and more sustainable long-term path.

Understanding Your Costs

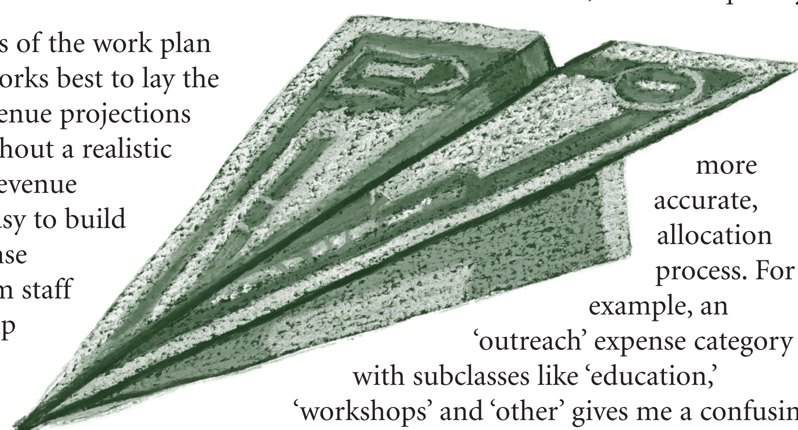
Estimating Expenses

by Rob Buirgy

Executive Director
Big Thompson
Watershed Forum
& River Network
Board Member

The art of estimating expenses exists in close relationship to the challenge of predicting revenues. These are the yin and yang of a balanced budget, and maintaining a harmony between the two is a key ingredient to building the productive planning tool we all desire.

As with any relationship, our budgets will function best when directed toward a common purpose. By having our organization's mission clearly in mind and a realistic work plan established, we'll have a framework that can support the inevitable 'squabbles' that surface between revenues and expenses.



Once the key ingredients of the work plan are in place, it usually works best to lay the foundations of your revenue projections early in the process. Without a realistic assessment of top-line revenue estimates, it's way too easy to build the pie-in-the-sky expense budgets that get program staff and boards all worked up about unrealistic goals, and end up with equally unrealistic expectations for fundraising. We all know the best chance for a successful marriage is to start with realistic expectations; I think of this as the pre-nuptial agreement between the two halves of our budget, and it helps us go into the process with confidence.

Ahhh—now for the fun part. In a conscientious organization, we have quite a bit of control over our own activities, and estimating expenses comes a little more naturally. This part of the process often engenders more confidence than what we get from reading the tea leaves of our funding sources. Also, as our expense budgets develop some established traits, they can hold their own in the relationship and give us a clear indication of where we need to go with our revenue projections.

As a starting point, it's worthwhile to consider the basic categories to which expenses are allocated. Reporting expectations for nonprofits will require at least 3 general expense categories, which gives rise to the typical classes seen in most budgets: Administration, Fundraising, and one or more Programs. This is where our work plan objectives dovetail with the budget, and often where program staff gets the opportunity to build their part of the budget. A little creativity, with an eye toward descriptive labels, makes for a more natural, and consequently more accurate, allocation process. For example, an 'outreach' expense category with subclasses like 'education,' 'workshops' and 'other' gives me a confusing variety of options when I'm trying to figure out where to allocate the cost of this year's State of the Watershed report. In a case like this, eliminating subclasses can pay off big dividends—especially early in the budgeting process. A single 'education' class will make the allocation decision obvious and keeps the process moving forward. Subclasses will naturally evolve in a working program budget, but I recommend rolling them up into major categories during the early stages of budget planning.

Expense categories will share the same list of 'line items' such as salaries, rent, insurance, materials, mileage, etc. We all have regular expense items that can't be ignored—paying our own salary and renting office space don't usually slip peoples' minds. However, there is one regular expense item that belongs front and center, but is so commonly overlooked that it demands special attention. In true top-down fashion, the Board of Directors must set a goal for an annual financial reserve and ensure that the overall budget has 'cash remaining' in the final analysis. Just as a business would never overlook their bottom line profits, a sustainable nonprofit must have a realistic operating reserve that is endorsed by everyone in the organization. Enough said. This is also the time to take a careful look at line item categories to determine if adding, eliminating or renaming lines is in order. A stale, out-dated budget is a real burden, and this is a good opportunity to breathe new life into the organization on an annual basis.

When it comes to actually estimating expenses, there are at least three common methods:

- $ **The "Mark-Up Method"** estimates future expenses based on my organization's historic spending patterns. We usually use the most current expense records available and factor in an increase or decrease based on our recent experiences. This method is widely used, so it makes sense that the inherent problems with this method are some of the most commonly encountered. For example, when using this approach, we often assume that our current year's costs are reasonable, when they may be quite the opposite. This would cause a problem, for example, if we need to rehire for a departing administrative assistant whose loyalty kept them working for years at minimum wage, but that pay rate won't attract the quality of applicants we need. Conversely, perpetuating inflated expenses is just as common—how long has it been since you solicited bids for your organizations' internet services or technology hardware? Computer and IT services have shown dramatic price decreases in the past few years and may be good candidates for decreased expense allocations in next year's budget.
- $ **The "Percentage Method"** compares the current year's percentage of each expense relative to revenue and applies these percentages to projected revenues for next year. This method often works well when allocating fixed costs across several expense categories, as long as we are on the lookout for the same pitfalls we encounter with the mark-up method.
- $ Last, but not least, **the "Zero-Based Method"** is all we have to work with when we are starting a new organization or a new program—or in lean times, this strategy takes us right back to the base assumptions we have in running our organization, and may be the only way to create a budget that allows us to keep the doors open. With this approach, current or previous years' figures are ignored or don't exist, and each expense must be justified on its own merit. I imagine this is a favorite tool of evil corporate types who want to torture their managers, but it is truly the only option in many young or developing organizations. Be sure to allow for the extra time and effort this method requires, and inform the process with as much organizational knowledge you can muster through a team approach that includes experienced program staff.

At the end of the day, our success as an organization must be measured by our results, not by our efforts—and a balanced budget that allows for a dynamic relationship between expenses and revenues is one of the most efficient planning tools we can have.

Touring Friendly Watershed Council's Budgets...

Budgets, Budgets, Budgets

$AMPLE BUDGET$

Cash Flow Budgets:

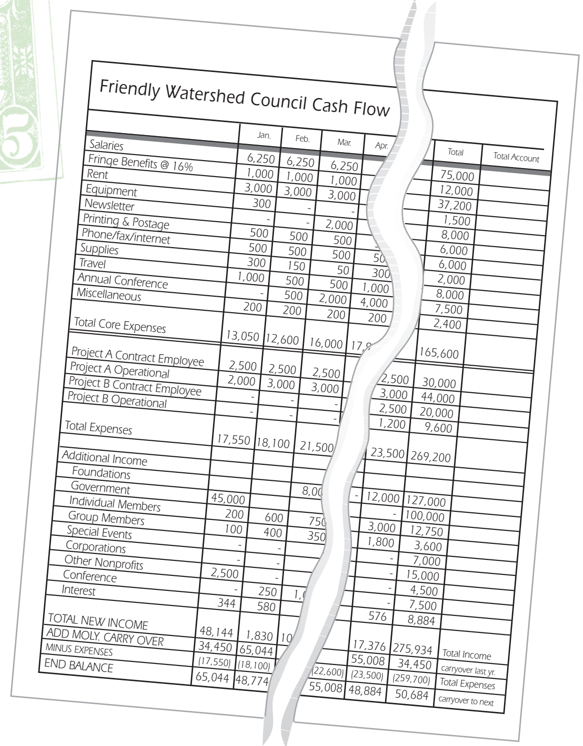
by Suzi Wilkins Berl

Forewarned is forearmed! A cash flow budget set up in an Excel spreadsheet allows an organization to determine how various expenses and income will balance throughout a fiscal year. With this information, an organization can foresee shortfalls and can take steps ahead of time to ward off a cash shortfall.

Basically, a cash flow budget takes the projected numbers from your overall operating and capital budgets and adds timing to the mix. By estimating when the actual cash from the various income items is expected and when the expenditures must be made, a cash flow budget has been created. Cash and the demands for cash will ebb and flow throughout the year.

Projecting the likely timing on expense items, of course, is the easier task. The payroll must be at regular intervals by law, and the accounts payable tends to be steady except for start-up and one-time only outlays. There is also some control that may be exercised over the timing of outgoing funds.

The timing for revenues, however, requires communication and coordination with whoever will execute the fundraising plan and development calendar and depends to a greater extent on factors external to the organization. Do be realistic and consistent about the probable receipt of payments. Even if the budgeted revenue is realized, the cash may not be paid in accordance with the terms originally specified. This is particularly true of corporate contributions and fee-for-service income.



Friendly Watershed Council Cash Flow

	Jan.	Feb.	Mar.	Apr.		Total	Total Account
Salaries	6,250	6,250	6,250			75,000	
Fringe Benefits @ 16%	1,000	1,000	1,000			12,000	
Rent	3,000	3,000	3,000			37,200	
Equipment	300	-	-			1,500	
Newsletter	-	-	2,000			8,000	
Printing & Postage	500	500	500			6,000	
Phone/fax/internet	500	500	500	50		6,000	
Supplies	300	150	50	300		2,000	
Travel	1,000	500	500	1,000		8,000	
Annual Conference	-	500	2,000	4,000		7,500	
Miscellaneous	200	200	200	200		2,400	
Total Core Expenses	13,050	12,600	16,000	17,[illegible]		165,600	
Project A Contract Employee	2,500	2,500	2,500		2,500	30,000	
Project A Operational	2,000	3,000	3,000		3,000	44,000	
Project B Contract Employee	-	-	-		2,500	20,000	
Project B Operational	-	-	-		1,200	9,600	
Total Expenses	17,550	18,100	21,500		23,500	269,200	
Additional Income							
Foundations							
Government	45,000		8,00[illegible]	-	12,000	127,000	
Individual Members	200	600	750		-	100,000	
Group Members	100	400	350		3,000	12,750	
Special Events	-	-			1,800	3,600	
Corporations	-	-			-	7,000	
Other Nonprofits	2,500	-			-	15,000	
Conference	-	250	1,[illegible]		-	4,500	
Interest	344	580			-	7,500	
					576	8,884	
TOTAL NEW INCOME	48,144	1,830	10[illegible]		17,376	275,934	Total Income
ADD MOLY. CARRY OVER	34,450	65,044			55,008	34,450	carryover last yr.
MINUS EXPENSES	(17,550)	(18,100)		(22,600)	(23,500)	(259,700)	Total Expenses
END BALANCE	65,044	48,774		55,008	48,884	50,684	carryover to next

Facing short-term financing problems is not uncommon in nonprofit. If the organization needs a bank line-of-credit or another type of loan, the cash flow budget will be an essential part of the documentation for making that lending possible. One of the first questions that a lender will ask is: "When will the organization be able to repay any loan?"

Here in the example, we show the new income for each month plus the cash carry over from the previous month minus the monthly expenses, with that total then carrying over to the next month. Using regular spreadsheet formulas throughout, the organization can determine what might happen if, for example, the $75,000 foundation income anticipated in April comes in at a lower level, doesn't come in at all or is delayed 6 months. This "what-if" planning is crucial for the cash forecasting that will help stabilize the financial management of an organization.

Operating Budgets:

A wise man will have money in his head but not in his heart.

— Jonathan Swift

$AMPLE BUDGET$

by Susan Schwartz, River Network

The initial step in the operating budget process is a careful review of the organization's achievements and fiscal performance of the prior year. This includes, but is not limited to, reviewing programmatic goals and objectives accomplished and comparing past years' budgeted revenues and expenses to the actual financial experience of the organization. If it is possible, it may be helpful to look at the number of people trained or groups served or activities evaluated—whatever the appropriate outcome statistic is for your programs. Based on this review, goals and objectives might be reevaluated and redesigned. The budget can be the connector between your goals and objectives, and your strategic, long-range plans.

In many organizations, the budget preparers begin with what was spent last year and add the amounts anticipated for contractual increases, predicted inflationary trends and projected new programs or services. The budget should estimate the total costs required to achieve program objectives, including staff, supplies, equipment, space, insurance and all other resources. In a staff-driven model, both program and administrative staff should be involved in discussions of programmatic costs to be sure that all the resources required by your programs are considered.

You can certainly rely on past experience, as reflected in budget to actual financial reports, to determine some of the information for continuing programs. Do make sure to account sufficiently for anticipated changes, though, especially in areas such as fringe benefits and insurance, which are often subject to double-digit increases in cost. Also review other expense line items for normal cost-of-living adjustments like annual rent increases. It's axiomatic but still good advice not to project expenses to the last penny, but to allow some room for the unexpected.

Since personnel costs typically account for by far the largest share of a nonprofit's total expense budget, be sure to plan carefully for these line items. There can be a lot of hidden costs associated with staffing new programs beyond the addition to salaries and benefits. For example, new employees entail recruitment advertising; interviewing applicants and hiring the chosen candidate; training and evaluating a new person through an introductory period; providing additional office space, furniture, equipment and supplies; and supporting additional staff through added supervision, coordination and meeting time.

Of course, you must budget for income, as well as, expenses. Even though entirely unpredictable events may influence grants, contributions and fee-for-service income, you can estimate revenues with some degree of accuracy based on past experience. As with any budgeting based on the past, it is important to make adjustments for changes and anticipated trends. Grants from foundations, corporations and government agencies are usually much more difficult to predict than membership income or paid consulting work. Both the financial and fundraising volunteers or staff, in collaboration with the board chair or executive director, have to make a conservatively realistic assessment. In some cases, it may be necessary to develop three (3) contingency budgets: most likely, best case and worst case scenarios for the revenue projections. Some foundation

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Operating Budgets, cont.

$AMPLE BUDGET$

revenue forecasts use a method of discounting the grant requests for both likelihood and amount of award. A proposal for $50K, for example, may be budgeted for $30K after being discounted 25% for yes/no on the funding decision and then again 20% for the amount granted. There are many methods for projecting revenue, and each organization will need to find the methodology that works best for its circumstances.

Finally, carefully compare revenue and expense projections. At different times organizations will choose to incur a small deficit, realize a surplus or simply break even. No rule says that budgets must balance in each budget period. However, a surplus is the most desirable outcome under all circumstances. Your organization should plan for financial success and sustainability. That means a surplus year after year. If you anticipate a deficit, are you investing monies in new programs? Deficits can lead to insecurity in program delivery, staffing and funding, and even eventually bankruptcy. Large surpluses may mean that the organization is not investing enough in serving the public interest. However, for any given budget period, revenue and expenses should be in the relationship that the organization deliberately and strategically chooses.

Friendly Watershed Council Operating Budget

Revenue and Support:	Annual Budget
Foundation	$75,000
River Festival	55,000
Corp Giving/Sponsorships	40,000
Individual & Workplace Giving	40,000
Government Contract	34,000
Fees for Service	10,000
Board Contributions	10,000
Sale of Materials	5,500
Interest Income	1,000
In-kind Donations	5,000
Other	4,000
Total Revenue:	**$275,500**
Costs and expenses:	
Salaries	$108,275
Taxes & Fringe Benefits	26,550
Consultants	15,500
Workshops/Trainings	12,000
Printing	12,750
Staff Travel	4,000
River Festival	29,750
Telecommunications	8,500
Postage & Shipping	8,500
Materials & Supplies	13,125
Occupancy	11,000
Insurance	3,500
Donor Recognition	1,200
In-kind Expense	5,000
Total Expenses:	**$259,650**
Net Surplus (deficit)	**$15,850**

If the first draft of your budget does not indicate that revenue and expenses are in the desired relationship, all the organizational activities must be reevaluated and adjustments must be made. Nonprofits often find that their initial projections for income and expenses create an unacceptable deficit, and so either additional revenue must be generated or activities must be reduced. When reviewing the revenue budget, it is important to avoid the temptation of raising the estimate without changing the plans for generating revenue. The budget must be based on reasonable assumptions, or you are only postponing a crisis.

If expenses need to be reduced, it is helpful to determine what each program would cost at different capacity and service levels. A fixed percent cut across all expense lines is usually not the most effective way to reduce expenses. It is often not true that program benefits and costs will move together in the same direction with each additional dollar spent resulting in an additional dollar of results.

Once you have changed your plans and updated your budget so that revenues and expenses are expected to be in the proper relationship, the full board, in its governance role, will approve the budget. From that point, staff and volunteers put the plan into action and should prepare monthly reports comparing actual income and expenses to the budgeted amounts.

$AMPLE BUDGET$

Grant Budgets:

by Sarah F. Moore, River Network

Even though your grant budget will likely be attached to the end of your proposal, sometimes it's the first item foundation staff will read. **Your budget should tell the same story as the narrative you write.** It should show where the project money will come from and where it will go, and it should be in line with the priorities of your organization.

The detail of your grant budget demonstrates your credibility and your ability to effectively carry out the work or project in your proposal. Does your budget provide enough capital to complete the work professionally? Funders do want to know you're cost conscientious, but they usually won't fund a project that doesn't have enough resources to accomplish the tasks outlined in the proposal. Be realistic about your goals, how long it will take, and how much money you'll need to do the job.

Your grant budget also reveals your understanding of the funder's guidelines. Be clear what you are asking the foundation to fund. Don't ask them to pay for travel, if their guidelines state that they don't. (If possible, identify that another funding source will cover those expenses, or that they will be covered by unrestricted general funding.) Is the amount of your request in line with the average amount this funder routinely awards? For instance, asking for $20,000 from a funder with average grant awards of $2,000 – $5,000 may disqualify your proposal from even being considered. Similarly, if you need only about $5,000, a foundation that typically funds projects at the $50,000 – $100,000 range isn't the right fit for your proposal.

Keep the content simple, unless more detail is requested by the funder.

Always double-check your numbers and your math. Check it again just before mailing to be sure any changes/editing to your narrative is reflected in the budget and vice versa.

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$AMPLE BUDGET$

Grant Budgets, cont.

List all sources of revenue for the project and indicate if they are confirmed or pending. Be sure to highlight how much of the project funding is already secured.* Put the name of the funder to whom you are applying on the first line to demonstrate that they are a critical part of the success of the project.

Save this budget template to be sure all other proposals for this project have a consistent look. (Funders do compare notes.) Work with your financial officer or bookkeeper to develop a budget format that is flexible enough to meet the budget requirements of different funders, but still easy for your bookkeeper to report expenses within. This will make reporting on how your spent the funds simple, defendable and professional.

Finally, save your budget template to modify and re-use for other projects in the future. Take a bit more time to create a "wheel" that can really go the distance.

**If you receive confirmation of additional funding sources after you've submitted your proposal, use it as an opportunity to send an update to all other funders with whom you have pending proposals (for the relevant project). This keeps your name current in their mind and demonstrates that your project was considered a good investment by another foundation.*

Friendly Watershed Council Proposal to ABC Foundation

Project: Volunteer Monitoring Training Workshop - Spring 2005 (Mar-June '05)

Revenue	Amount	Status
Blue Water Foundation	$18,000	Received
Fish Family Fund	10,000	Committed
ABC Foundation	8,000	*Pending*
Flyfisherman Corporation	2,000	*Pending*
Unrestricted contributions	1,500	Received
Participant workshop fees	400	$10 x 40 participants
Total received/committed	29,500	
Total pending	*10,400*	
TOTAL	**$39,900**	

Expenses	Amount	Description
Project Coordinator (including benefits)	$22,320	60% of FTE for 2005
Development/Volunteer Coordinator	4,500	20% FTE for 2005
Outreach brochure & newsletter	300	Design & printing
Mailing & postage	120	
Training workshop space rental	1,000	$250 x 4 workshops
Transportation to riverside	800	$200 x 4 workshops
Workshop training materials	200	
Monitoring training kits	2,400	$60 x 40 participants
Refreshments & lunches	600	$150 x 4 workshops
Subtotal	32,240	
Administration & overhead	4,836	@ 15%
TOTAL	**$37,076**	

Capital Expenditures Budgets:

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Capital expenditures are those that acquire assets whose useful lives are greater than the current period. Many times a small organization will borrow assets, or members will use personal assets for the needs of the organization. Assets that are given to the organization should be treated as both income (a contribution) and outgo (the purchase of an asset). Donors of non-cash items will need to help provide a solid estimate of the value of the items, both for the organization's records and for the donor's records for tax and other purposes.

Some donated items, such as stock or a vehicle, require a transfer of title, which is recorded with local or federal authorities. Make sure this transfer of title is carried through in an orderly and timely manner.

Some gifts bring new responsibilities to the organization. Can you safeguard this asset? Does it need to be insured? Do you need a safe deposit box? If an asset is housed on premises that do not belong to the organization, then a master list of such assets and their whereabouts should be prepared and maintained in a safe and central location.

CAPITAL BUDGET

Rank	Item	Quantity	Department	Organization Code	Cost	(E) Essential (N) New (U) Upgrade (R) Replacement	Justification / Notes
1	Copy Machine	1	Admin	9000	$5,500.00	R	old copy machine does not work
2	Telephone System Update	1	All	9000	$3,000.00	U	add voice mail
3	Computer Upgrade	1	Develop	8000	$2,000.00	E	upgrade necessary
4							

Example by Andrea Korsen

There are other gifts that need accounting and budgeting. One is the forgiveness of rent for space. The fair market value of the rent should be recognized on both the budget and actual financial information as income and expense.

This type of recognition gives a better picture of the true state of affairs for the organization. If you lose the free rent, can you make up the difference in cash donations and afford to pay the rent? This question is best answered when the value of the prior gift is recorded.

Capital budgets can be achieved over a period of years when a sinking fund is established to collect money for a future capital expense.

SAMPLE BUDGETS

CASE STUDY

Cahaba River Society ~ Alabama

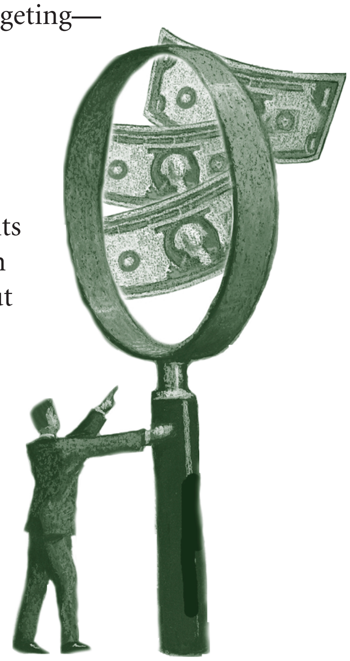
Healthy Budgets – Healthy Organizations

by Beth K. Stewart

Executive Director
Cahaba River Society

www.cahabariversociety.org

In the late 1990s, the Mary Reynolds Babcock Foundation selected the Cahaba River Society (CRS) to participate in an organizational development program. Several of the participating executive directors felt a need for financial management training, a common concern of environmental executive directors who come up from advocacy work. The training opened my eyes about the need to be able to do cash flow budgeting—to be able to plan/predict revenues and expenses on a monthly basis—because nonprofits have such uneven revenue flows, but have regular expenses. You can't do good fundraising planning unless you can make sure the timing of the revenues match expenses.



Out With the Old, In With the New

CRS used to have only an annual budget with projected total revenues and expenses for the entire year. The whole budget was on two pages. We couldn't predict whether our reserves would dip way too low at one point in the year because expenses took the money out faster than the revenues came in. We did not have as effective a system for tracking whether we were actually receiving projected revenues each month, thus we were less aware of missed opportunities that we had to redouble our efforts on. It was hard to coordinate our budget with fundraising planning. Our updated financial management system marries tight monthly budgeting and cash flow projections with a monthly fundraising plan. The system provides greater accountability and fewer surprises for both staff and board.

It took several years to build the system, so groups need to start putting the data and systems in place well before the tight times come. Because we had this system in place, we were able to weather nearly two years of very tight finances without having to cut back on staff or programs.

A Closer Look

The pieces of the system are:

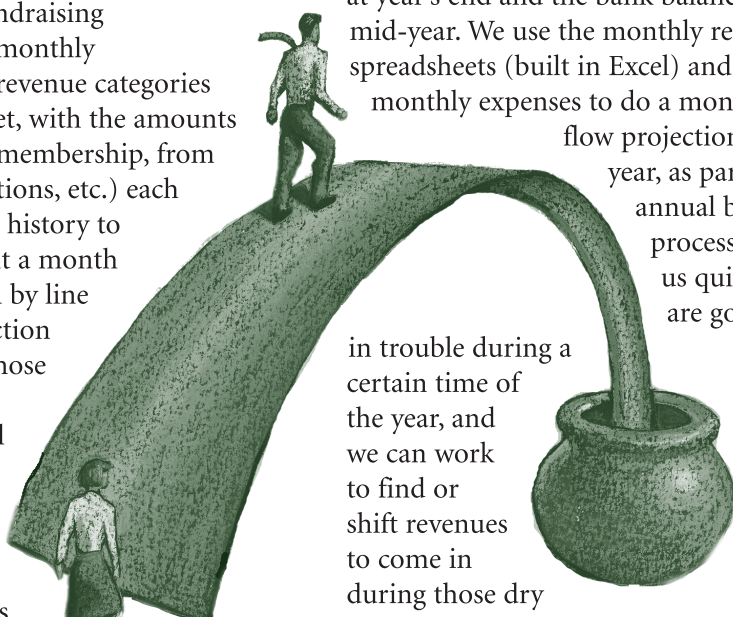
- $ Annual Budget
- $ Detailed fundraising plan based on actual past revenues, in monthly spreadsheets showing all revenue prospects
- $ Cash flow projections for coming year, by month, updated through the year based on actual cash flows
- $ Fundraising calendar
- $ Diverse revenue sources, with foundation grant reliance at only about 1/3 of total revenues.

ANNUAL BUDGET

Our budget is structured with flexibility. We have a "Basic" and Target" budget amount for each expense and revenue line item. For revenues, "basic" includes what we are very certain will come in—regular grants, membership similar to last year's, etc. "Target" includes grants we are less certain about and the more aggressive expectations for membership, special events, etc. For expenses, "basic" is the authorized budget, and in tight years it's the bare minimum we need to get by, equal to our basic revenues. "Target" expenses include special programs or people funded by anticipated grants and the more aggressive revenue expectations. Staff can spend the "basic" budget without special authorization. Spending from the "Target" budget requires the executive director to authorize it, which is done only when special revenues are received.

DETAILED FUNDRAISING PLAN

We track revenues on a monthly basis going back several years, and these form the basis for our monthly fundraising spreadsheets. Each monthly spreadsheet has all revenue categories similar to the budget, with the amounts received (e.g. from membership, from donors and foundations, etc.) each month. We use that history to build and document a month by month, line item by line item revenue projection for the next year. Those solid projections underlie our annual projected budget that the board adopts—it's not just a wish list, there are real figures behind all of it. As we go through the year, we use the monthly sheets going forward several months, as the basis for planning—what must we do in July, for instance, to make those revenues happen by September? The spreadsheet also tracks what we actually receive each month compared to projections. This helps us not leave money on the table: if something doesn't come in, we're reminded to stay after it. Sometimes we amend future month spreadsheets to carry those missed revenues forward and keep them on the front burner. The spreadsheets are also a great way to quickly show board what sources we are pursuing and engage them in helping, and they help to keep the whole fundraising team accountable.



CASH FLOW PROJECTIONS

The cash flow projections are essential to our budget process. Nonprofits typically have similar monthly expenses but feast or famine monthly revenues. When the money is tight, it won't matter that the annual budget balances, if most of the revenues are at year's end and the bank balance crashes mid-year. We use the monthly revenue spreadsheets (built in Excel) and averaged monthly expenses to do a monthly cash flow projection for the year, as part of the annual budgeting process. That tells us quickly if we are going to get in trouble during a certain time of the year, and we can work to find or shift revenues to come in during those dry months. As we go through the year, we update each month with actual revenues and expenses, which automatically recalculates the rest of the year. That way we can see the future impact of unanticipated expenses or lost revenues, and can have several months to avoid having the bank balance dip too low.

Organizational development folks recommend that nonprofits have about six months operating revenue in the bank at all times. Your goal is that you don't fall below that, even in your leanest months. Foundation reps (program officers) have agreed that is a reasonable amount and shows good financial management. Building those reserves either takes many years of slowly building them—budgeting for it each year—or a leap forward from

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Cahaba River Society ~ Alabama, cont.

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undesignated revenues, such as a planned gift. That cash-in-hand cushion is absolutely necessary, not only to protect against the unexpected, but to give you flexibility and strength to pursue your mission. Sometimes you have to take a tough stand, even if you lose revenue because of it. Ideally, you don't want financial survival to be a factor when you decide what stands the organization must take.

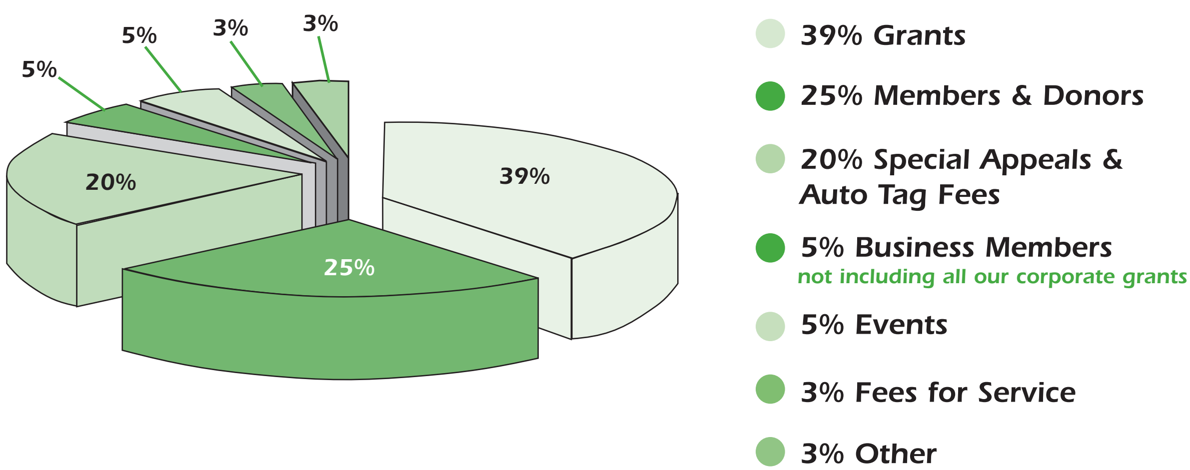
Our system helps us understand the "cushion" of cash we need in the bank to make sure we are in good position throughout the year, even in lean revenue months. It makes us budget to build that cushion. We are now close to accomplishing the 6 months goal.

FUNDRAISING CALENDAR

We maintain a list of all grant deadlines, with a computer prompt system. This helps us submit both timely proposals and required reports. Additionally, it allows us to budget our time appropriately. One staff member is responsible to check the calendar monthly and remind responsible staff to write those grants or reports.

DIVERSE REVENUE SOURCES

A key to survival is diverse sources of revenue. For Fiscal Year 2004, our revenue included:

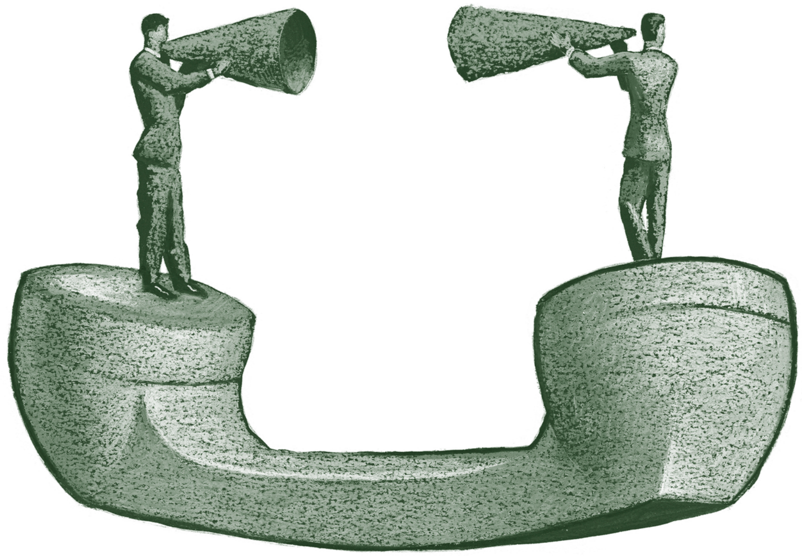


With this level of diversity, about 60% of our revenues are what we call "sustainable" — constituent-based, renewable and unrestricted revenues rather than grants.

Words of Advice

The one most important thing I can say to organizations struggling financially is **tell your board and staff**. Sometimes the executive director may want to gloss over the situation to the board or staff. You need your board and staff to be full partners in strengthening the organization, understanding why cost-cutting measures are necessary, and having input on how to do it. Board and staff will greatly multiply the ideas for strategies. A hallmark of our system is great reporting to our board—in addition to the monthly financial reports, they see actual and projected cash flow monthly, as well as the monthly fundraising plans. This ensures that the board is a full partner in financial management and fundraising.

As one example, when times were at their tightest, the board asked our landlord to reduce the rent temporarily as a donation, and he did. The staff decided we would all rather take a minor temporary pay cut then have to lay someone off. Board and staff worked double hard at raising revenues. All these things helped us through it.



Forms for the Taking

The Cahaba River Society has generously provided two of their forms for use by other groups. River Network Partners can access both a Cash Flow Projection and a sample Montly Fundraising Plan on River Network's Partner webpage: www.rivernetwork.org/Partners. Simply log on to the page using your User Name and Password and then click on "templates and examples."

Both forms are available as Excel documents and can be modified to suit your needs. As always, River Network highly recommends that you double-check all formulas used in the form.

Monthly Fundraising Plan

	Rec'd Jan 05	Basic Budget	Actual Jan 04	Actual Jan 03
Donors above $1,000				
new/renewals*	$0	$0	$0	$0
Total	**$0**	**$0**	**$0**	**$0**
Business Members				
new/renewals*	$0	$0	$0	$0
Total	**$0**	**$0**	**$0**	**$0**
CLEAN Education Program				
CLEAN Corporate Sponsors	$0	$0	$0	$0
CLEAN Contracts	$0	$0	$0	$0
CLEAN trip fees	$0	$0	$0	$0
Total	**$0**	**$0**	**$0**	**$0**
Other Sources				
Memberships	$0	$0	$0	$0
Board of Director Contributions*	$0	$0	$0	$0
Appeals	$0	$0	$0	$0
Events	$0	$0		$0
Auto Tags	$0			$0
Special Contribution				$0
				$0
				$0
				$0
				$0
				$0
				$0

ACTUAL CASH FLOW PROJECTION

Cash Position June 30, 2004 $0

	July	Aug	Sept	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	June	Projected Total
Revenues	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	**$0**
Expenses	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	**$0**
Cash Position Month End	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	

ORIGINAL CASH FLOW PROJECTION

Cash Position June 30, 2004 $0

	July	Aug	Sept	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	June	Projected Total
Revenues	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	**$0**
Expenses	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	**$0**
Cash Position Month End	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	

NOTES: On first chart, replace projected numbers with actual figures as each month occurs, and recalculate "cash position" projections for each month in the future based on those actual figures. Keep 2nd "Original Cash Flow Projection" chart as a comparison to know if you are meeting your original projections.

Resources & References

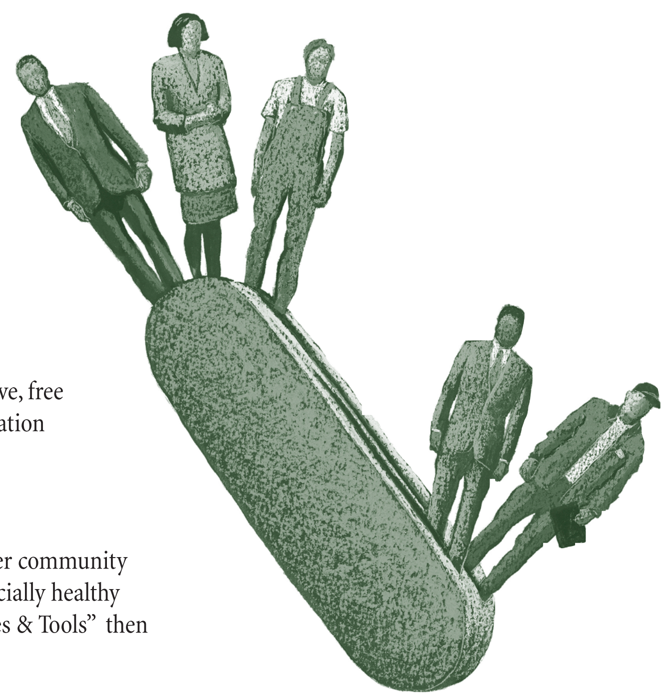
The Alliance for Nonprofit Management is the professional association of individuals and organizations devoted to improving the management and governance capacity of nonprofits—to assist nonprofits in fulfilling their mission. The Alliance is a learning community that promotes quality in nonprofit capacity building. Type "Budget" into their search engine for information on the budget process.
www.allianceonline.org

Innovation Network is a nonprofit organization that provides evaluation consulting, training and online tools. Our organization and our website are dedicated to developing and sharing evaluation tools and know-how with nonprofits and funders, so you can do your work more effectively. Free registration allows you access to the "Nonprofit Workstation" that allows you to build a blueprint for designing, evaluating and implementing a successful program. Workstations are included for budget plans, program plans, evaluation plans and grant applications.
www.innonet.org/

The Internet Nonprofit Center is home to the Nonprofit FAQ. The FAQ is based on "frequently asked questions" and answers drawn from an email discussion forum.
www.nonprofits.org/npofaq/

The Management Assistance Program (MAP) for Nonprofits' *Basic Guide to Non-Profit Financial Management Library* is a free community resource. The overall goal of the library is to provide leaders and managers (especially those with very limited resources) basic and practical information about personal, professional and organizational development. Resources include how to design a budget, manage cash flow, prepare financial statements and more.
www.mapfornonprofits.org/

Non-profit guides are free web-based grant-writing tools for nonprofit organizations, charitable, educational, public organizations and other community-minded groups. Guides are designed to assist established nonprofits through the grantwriting process and include sample budgets.
npguides.org/index.html



NonprofitExpert.com provides an extensive, free site on the web for nonprofits. View information about budget basics and much more.
www.nonprofitexpert.com/

Nonprofits Assistance Fund seeks to foster community development and vitality by building financially healthy nonprofit organizations. Click on "Resources & Tools" then "Financial Foundations."
www.nonprofitsassistancefund.org

Budgeting: A Guide for Small Nonprofit Organizations is a publication of the **Virginia Society of Certified Public Accountants**, researched and written by Frances C. Taylor, CPA. This online publication includes chapters on selecting a budget committee, setting budget priorities, when to prepare a budget and more. To view, visit their website and enter the title into the search function.
www.vscpa.com