



# Building a Beautiful & Bountiful Budget

Benjamin D. Bullock  
Director of Operations  
Together SC

# The Board's Levers to Govern The Org.

- Bylaws
- Board Policies
- Strategic Plan
- Executive's Performance Evaluation

AND

- THE BUDGET!

# Basic Terms for Financial Management

- Accounting Exists to Create Two Documents:
  - Statement of Financial Position (Balance Sheet)
    - $\text{Assets} = \text{Net Assets (Equity)} + \text{Liabilities}$
  - Statement of Activities (Profit & Loss)
    - $\text{Revenue} - \text{Expenses} = \text{Change in Net Assets}$
- Budgets are Plans or Projections for Statement of Activities
  - Also, Board-Approved Budgets are authorization to raise and spend money!
- Both are dependent on the Chart of Accounts.

# Example Chart of Accounts

#	Account Name	Type
1100	Wells Fargo Checking	Asset – Cash
1200	Wells Fargo Savings	Asset – Cash
1300	Accounts Receivable	Asset
2200	Accounts Payable	Liabilities
3200	Unrestricted Net Assets	Equity
3300	Temporarily Restricted Net Assets	Equity
4100	Donations	Income
4200	Gala Sponsorships	Income
5200	Salaries	Expense
5300	Gala Expenses	Expense
5400	Program Expenses	Expense

<b>Revenue</b>	<b>Amount</b>	
General donations	\$2,500	
Appeals	\$1,500	
Monthly giving	\$1,200	
Fall gala	\$4,500	
Program fees	\$15,000	
In-kind donations	\$5,000	
	<b>Total revenue</b>	<b>\$29,700</b>
<b>Expenses</b>	<b>Amount</b>	
Salaries	\$17,000	
Payroll taxes	\$5,000	
Insurance	\$500	
Marketing & PR	\$500	
Office supplies	\$350	
Postage & Printing	\$400	
Professional services	\$1,500	
Program supplies	\$2,050	
Technology & Phone	\$1,500	
Travel & Mileage	\$900	
	<b>Total expenses</b>	<b>\$29,700</b>
	<b>Net gain/loss</b>	<b>\$0</b>

Is this  
Your  
Budget?

# Budgeting with Intention

- **Simple, one-column Budgets:**
  - Hide the organization's meaningful work behind "Program Expenses"
  - Overemphasize "Salary" and "Overhead" as if they aren't programmatic
  - Say nothing about which donor or grantor's dollars are going to which program, and don't recognize donor restrictions on funding.
  - Require reinventing the wheel when writing grants and grant reports.

But Mostly:

**THEY DON'T ALLOW FOR REAL, STRATEGIC, INTENTIONAL PLANNING!**

# Plan Better with Class Accounting

- Each Program/Project/Initiative, etc. gets its own Class
- Example:
  - 01 – Governance / Administrative
  - 02 – Fundraising
  - 03 – Program 1
  - 04 – Program 2
  - 05 – Grant Funded Initiative 1
  - 06 – Grant Funded Initiative 2
  - Etc.

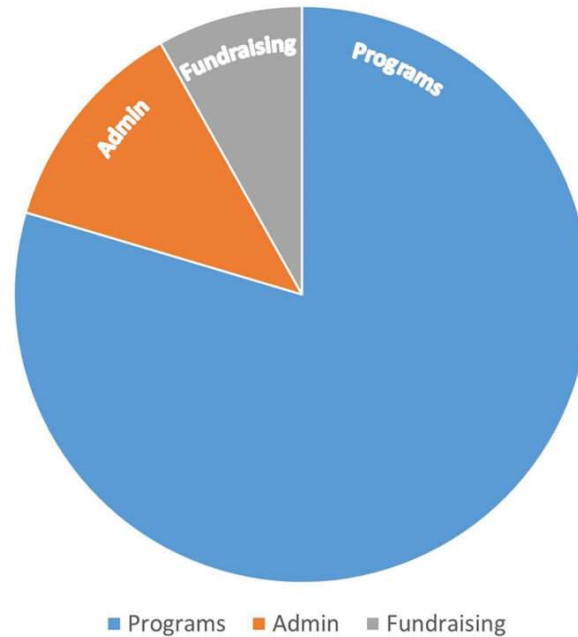
**FINANCIAL MANAGEMENT IN TWO DIMENSIONS!**





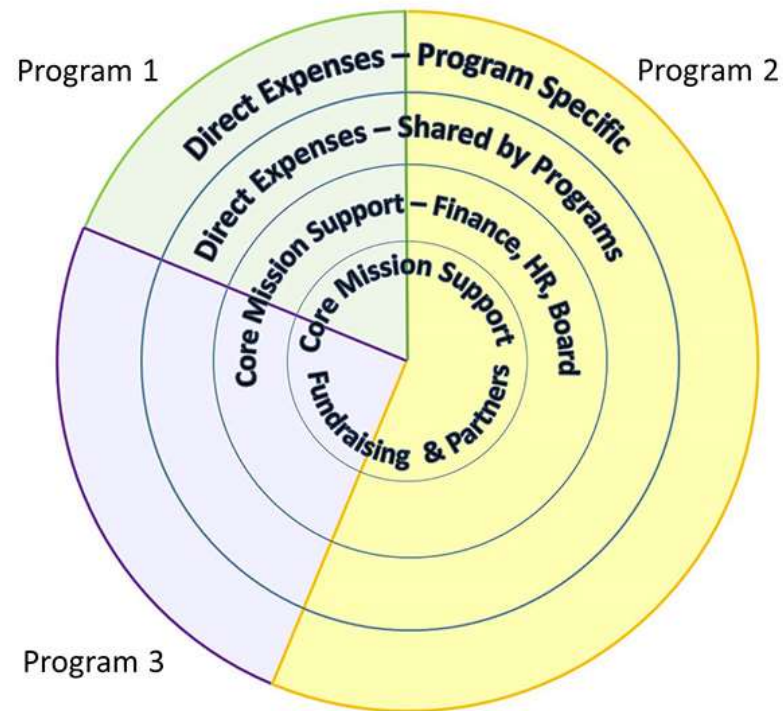
# Re-visioning Nonprofit Overhead

A Tired Old View of Our Organization



<https://nonprofitquarterly.org/graphic-re-visioning-nonprofit-overhead/>

# Re-visioning Nonprofit Overhead



<https://nonprofitquarterly.org/graphic-re-visioning-nonprofit-overhead/>

# Re-allocating “Overhead”

**Exhibit 2**  
**Statement of Functional Expenses by Nature with Supporting Services Allocated to Program Activities**

	Program Activities				Supporting Services			
	A	B	C	Programs Subtotal	Management and General	Fundraising	Supporting Subtotal	Total Expenses
Salaries and benefits	\$7,400	\$3,900	\$1,725	\$13,025	\$1,130	\$960	\$2,090	\$15,115
Grants to other organizations	2,075	750	1,925	4,750	–	–	–	4,750
Supplies and travel	890	1,013	499	2,402	213	540	753	3,155
Services and professional fees	160	1,490	600	2,250	200	390	590	2,840
Office and occupancy	1,160	600	450	2,210	218	100	318	2,528
Depreciation	1,440	800	570	2,810	250	140	390	3,200
Interest	171	96	68	335	27	20	47	382
<b>Total Expenses</b>	<b>\$13,296</b>	<b>\$8,649</b>	<b>\$5,837</b>	<b>\$27,782</b>	<b>\$2,038</b>	<b>\$2,150</b>	<b>\$4,188</b>	<b>\$31,970</b>
Allocation of Management & General	1,079	568	251	1,898	(2,038)	140	(1,898)	–
Allocation of Fundraising	1,124	633	533	2,290	–	(2,290)	(2,290)	–
<b>Total Expenses after Allocation</b>	<b>\$15,499</b>	<b>\$9,850</b>	<b>\$6,621</b>	<b>\$31,970</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>\$31,970</b>

<https://www.cpajournal.com/2019/05/17/functional-expenses-by-nature-and-the-overhead-debate/>

# Acknowledgements

Klotz, C. (2016, August 16). A Graphic Re-Visioning of Nonprofit Overhead. *Nonprofit Quarterly*. Retrieved from <https://nonprofitquarterly.org/graphic-re-visioning-nonprofit-overhead/>

Klotz, C. (2019, May 17). Functional Expenses by Nature and the Overhead Debate: Crafting an Alternative Approach to ASU 2016-14. *The CPA Journal*. Retrieved from <https://www.cpajournal.com/2019/05/17/functional-expenses-by-nature-and-the-overhead-debate/>

## A Graphic Re-visioning of Nonprofit Overhead



"We can work together for a better world with men and women of goodwill, those who radiate the intrinsic goodness of humankind." / [Kate Ter Haar](#)

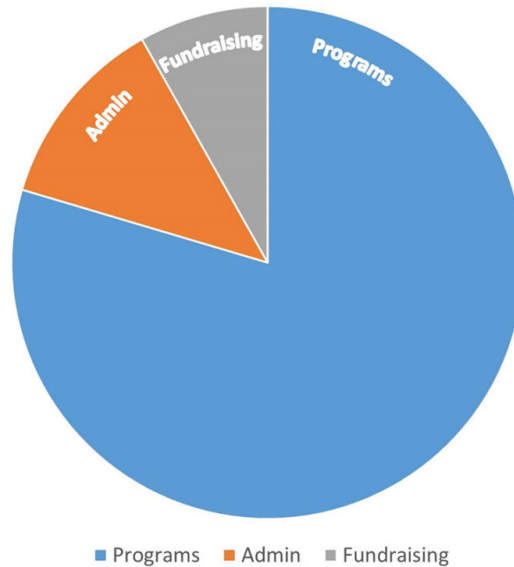
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Most nonprofit leaders agree that we need a new way to communicate about the true costs of our programs and the vital importance of strong organizational infrastructure. But we have not yet developed a simple, consistent message when sharing our view with potential supporters and investors. We are stuck with old terms and old images.

The following series of images and descriptions is really a blog in pictures. How we visualize our understanding of nonprofit structure and programs shapes the overhead debate. It's time to get graphic about our new ideas—to deploy fresh images to help educate the public, our funders, and ourselves.

# It's Time to Retire This Pie Chart

A Tired Old View of Our Organization

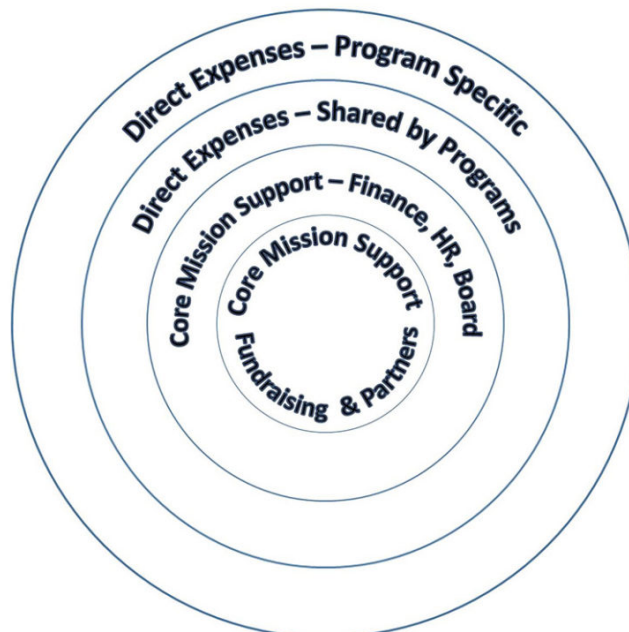


When nonprofits are viewed this way, no matter how hard we try to think differently, we imagine important infrastructure of our organization as taking a slice out of the pie—as diminishing the “real” work of our mission.

Strategic financial functions, good governance, and the development of key funding partnerships are vital to strong organizations. We need a new way to communicate this truth.

## We Need a New Image

Rather than thinking of our investment in key infrastructure as diminishing our programs, it should be seen as valuable **Core Mission Support**.

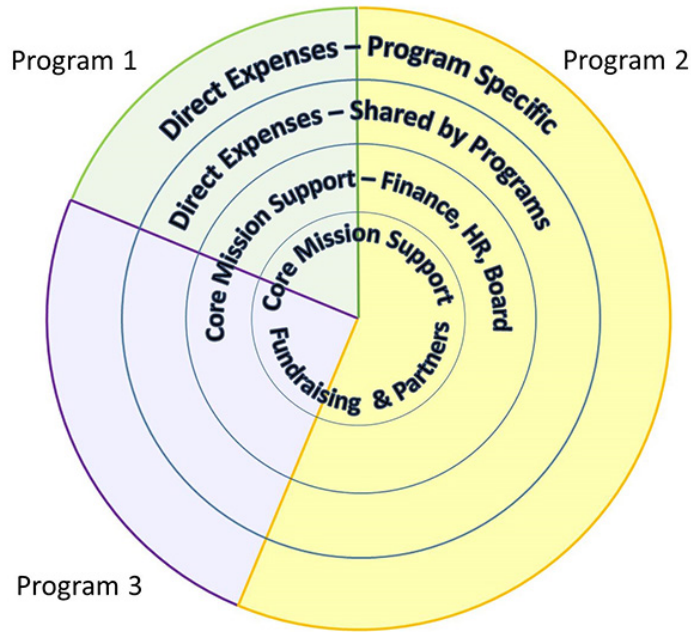


Core Mission Support functions are necessary, vital, and integral.

- Strong, strategic finance and accounting
- Progressive human resources practices
- Capable, responsive board governance
- Talented and engaged development staff

## Whole Organizations and True Program Costs

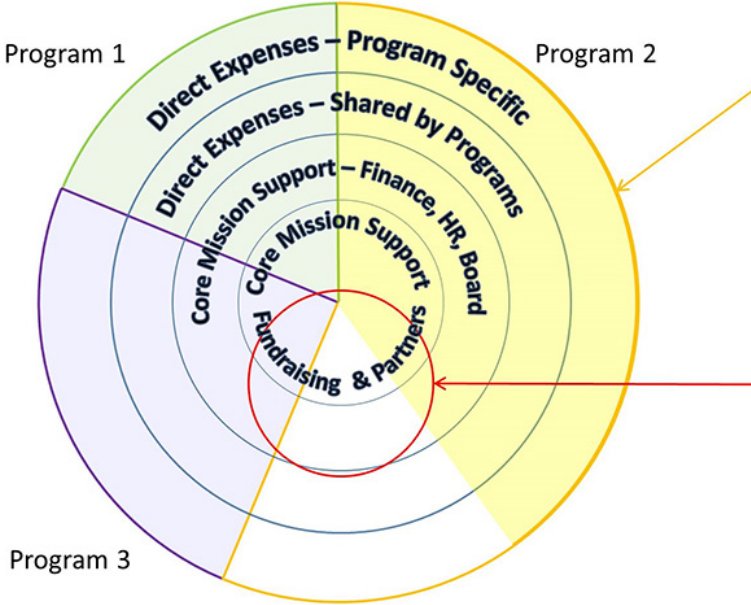
Each of our programs is built around, is supported by, and shares responsibility for **Core Mission Support**.



All of the resources we need to accomplish our programs are the **True Program Costs**, which include four types of expenses:

- Direct Expenses: Program-Specific
- Direct Expenses: Shared by Programs
- Core Mission Support: Finance, HR, and Board
- Core Mission Support: Fundraising & Partners

# Underfunded Programs Create a Gap at the Core

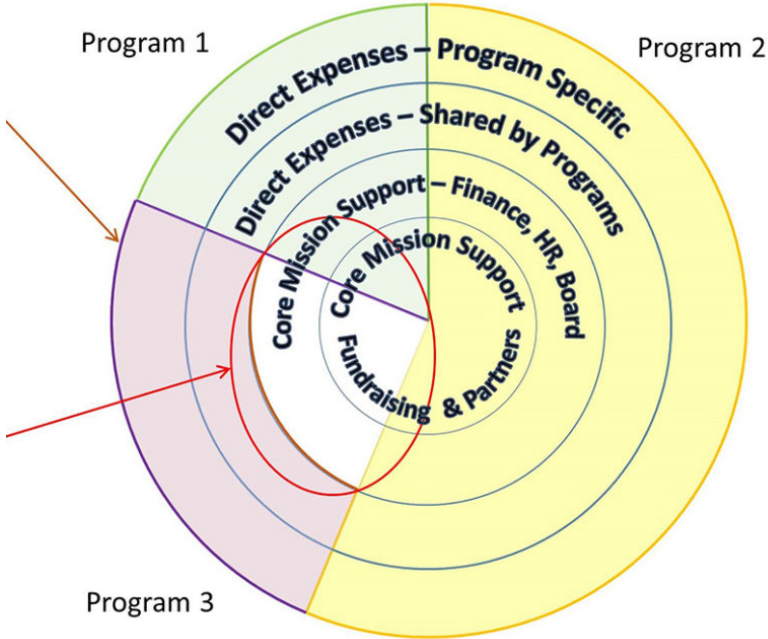


Some programs are only partially funded by contributions or by earned revenue.

When a program is only partially funded, the expenses not covered include a proportionate share of the Core Mission Support. This creates a **Gap** in funding for the finance, human resources, governance, and fundraising infrastructure that support the entire organization.

# Line-Item Funding Creates a Gap at the Core

Some funders limit their support to only the direct expenses of program.

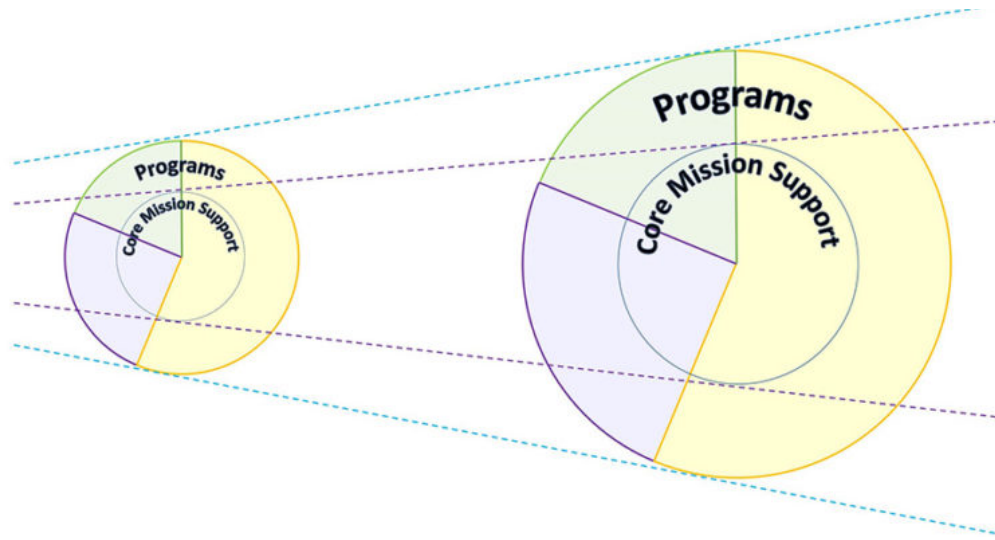


When funders support only direct expenses, they deny funding for Core Mission Support. This leaves a **Gap** at the



center of our organization. Not only is one program affected, but the health of the entire organization is at risk.

## Invest in the Core to Grow the Mission



The growth and effectiveness of our mission work depend on having a solid core at the center of our organizations. Investing in our infrastructure is savvy, prudent, and absolutely necessary.

## Go Visual With Our New Thinking

Once we have a new way of understanding and communicating about the Core Mission Support needed by our organizations, it is our job to share our thinking with others. Our funders, supporters and investors all want us to succeed. They are partners in accomplishing our mission work. But like us, they may need help reimagining the role strong infrastructure plays in amplifying program effectiveness. By providing a simple visual guide, we can help transform the way we talk about, picture, and ultimately fund the Core Mission Support that is at the center of all great nonprofits.

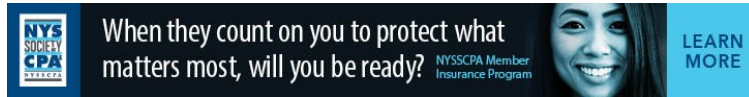
*This article was [published in its original form](#) at the blog of [Propel Nonprofits](#). It debuted on August 16, 2016.*

### ABOUT THE AUTHOR



[Curtis Klotz](#)

Curtis Klotz is the CFO and Vice President of Finance at Propel Nonprofits, a certified Community Development Financial Institution in Minneapolis with the mission of fueling the impact and effectiveness of nonprofits. In his current role, he also provides financial management advice and support to a variety of nonprofits, is a frequent presenter at conferences and workshops on nonprofit finance topics, and is a frequent contributor to Propel Nonprofits' Balancing the Mission Checkbook blog.



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# Functional Expenses by Nature and the Overhead Debate

## Crafting an Alternative Approach to ASU 2016-14

Feedback



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By Curtis Klotz, CPA (https://www.cpajournal.com/author/curtis-klotz/)

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FASB ASU 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*, is in full effect with the close of the December 31, 2018, fiscal year. As implementation progresses, a key provision of the new standard is likely to stir up the ongoing overhead debate. The standard's requirement that audited financials present a statement of functional expenses by nature is a stark reminder to nonprofits that—regardless of their own positions and practices where it concerns overhead—accounting convention is once again putting the numbers that fuel the debate front and center.

Fortunately, there is a way to both satisfy the new standard and go beyond it to present functional expenses in a manner more consistent with contemporary strategy and practice for nonprofit entities. This is an opportunity for CPAs to become advocates, helping nonprofits use the new standard to produce even more useful financial information for users.

### How the Statement of Functional Expenses Fuels the Debate

At the center of the debate is the longstanding reliance on the overhead ratio (alternately known as the program efficiency ratio or the functional expense ratio) as a measure of nonprofit effectiveness and efficiency. This view values keeping overhead costs (i.e., the cost of

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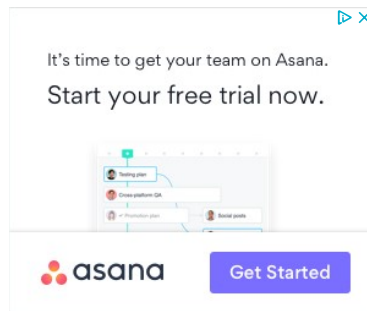
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core infrastructure) low. The assumption is that those nonprofits spending a higher percentage of their resources on what is broadly defined as overhead are less efficient than those that spend a lower percentage. Without a broader understanding of the financial strategies used by truly successful nonprofits, the presumption is that low overhead rates point to the best-run organizations.

What is concerning about the new FASB standard is that it refocuses attention on functional expenses. By requiring nonprofits to show functional expenses by nature (i.e., line item), there is an implicit assumption that the functional expense breakout is even more important. Focusing too narrowly on the statement of functional expenses could lead financial statement readers to misguided conclusions about whether a particular nonprofit is successfully carrying out its mission.



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Feedback

## An Alternative Viewpoint Requires an Alternative Presentation

Fortunately, many nonprofit leaders and their supporters understand the importance of investing in and strengthening their core administrative, HR, IT, governance, and fundraising functions, and are rightly questioning the efficacy of the overhead ratio as a measure of organizational efficiency. Recent research out of North Carolina State University caught the attention of the *Wall Street Journal* for suggesting that, instead of providing a measure of nonprofit efficiency, the ratio actually correlates negatively to nonprofit financial and programmatic success (Jason Coupet and Jessica Berrett, "When It Comes to Evaluating Nonprofits, It Isn't All About the Overhead," *Wall Street Journal*, Dec. 16, 2018, <https://on.wsj.com/2Y71MW0> (<https://on.wsj.com/2Y71MW0>)). For years, many in the nonprofit sector, including the author, have advocated for an alternative view of overhead that encourages strong investment in core organizational needs rather than discourages it (Curtis Klotz, "A Graphic Re-visioning of Nonprofit Overhead," *Nonprofit Quarterly*, Aug. 16, 2016, <http://bit.ly/2FeaZ3x> (<https://bit.ly/2FeaZ3x>)).

CPAs should do their part to help nonprofits navigate the new reporting requirement. The challenge is finding a way to display functional expenses while remaining true to nonprofit values where it concerns overhead. Using an alternative display is a powerful way to offer a different point of view.

## Satisfying the Minimum Requirements

The guidance provided in ASU 2016-14 is meant to establish a minimum threshold of practice and presentation. But once that minimum is met, nonprofits have the opportunity to use their audited financials to more fully share their financial stories.

**Exhibit 1** (<https://www.nysscpa.org/news/publications/the-cpa-journal/article-detail?ArticleID=13102#T1>) comes from ASU 2016-14 and is an example of a statement of functional expenses by nature. Showing expenses by nature translates into displaying those expenses by line items, which meets the minimum requirements of the standard.

### Exhibit 1

Statement of Functional Expenses by Nature



## Telling a More Complete Story

No one ratio or financial statement can tell the full story of a nonprofit business model. FASB makes clear that its model disclosures and statement mock-ups are meant to provide guidance and should not be seen as the only proper way to display information.

These illustrations are intended as examples only; they present only a few of the permissible formats. Other formats or levels of detail may be appropriate for certain circumstances. ... Not-for-profit entities (NFPs) are encouraged to provide information in ways that are most relevant and understandable to donors, creditors, and other external users of financial statements. (ASU 2016-14, 958-202-55-2, page 39)

Where it concerns the statement of functional expenses and the overhead debate, nonprofits can use this flexibility to tell a more sophisticated story.

One way to counter the overreliance on the functional expense ratio is to show that supporting services (e.g., management and general, fundraising) do indeed support the program activities and should not be seen as separate from, or diminishing of, program effectiveness. Of course, this requires that nonprofits actually allocate these expenses back to programs using an appropriate basis. For nonprofits that allocate administrative and fundraising costs to programs, the result is a more complete understanding of the true program costs or full costs of each program area. This is a powerful tool for measuring the actual program performance and is more in line with the reality of nonprofit business models.

Program work—that is, the mission—cannot get done without the benefit of and expense of core supporting services. *Exhibit 2* (<https://www.nysscpa.org/news/publications/the-cpa-journal/article-detail?ArticleID=13102#T2>) takes the sample ASU statement of functional expenses one step further by displaying the allocation of supporting services to program activities.

### Exhibit 2

Statement of Functional Expenses by Nature with Supporting Services Allocated to Program Activities



## CPAs as Advocates

Regardless of what one thinks of the overhead ratio and its usefulness, CPAs can advocate for nonprofit clients and employers to display their financial information in a way that counters overreliance on that single measure. For some nonprofits, this means boldly displaying the allocation methods they already use in the statement of functional expenses; others may first need to rethink and redesign their accounting systems to capture the data needed to accurately make these allocations. In either case, CPAs can help nonprofits move toward a more effective financial strategy that takes into account the true, full cost of program activities.

*Curtis Klotz, CPA serves as director of nonprofit innovation at CLA (CliftonLarsonAllen), Minneapolis, Minn., and is primary author of the CLA Innovation in Nonprofit Finance blog.*

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