

# PROJECT BUDGETING

(adapted from *Building Stronger Nonprofits Through Better Financial Management* by Lauren J. Kotloff with Nancy Burd)

Developing realistic budgets is one of the core project management functions. Nonprofits often seek to maximize the programmatic parts of budgets and try to meet ever stricter funders' expectations on very low administrative or overhead expenses, not tied directly to programs.

Failing to include reasonable allocations of overhead expenses into project budgets results in nonprofits having no cash reserves and facing difficulties in managing day-to-day cash flow as well as proper capacity building of the organization.

Accurate and realistic project budgets result from close cooperation between finance office staff and project managers. Sadly, all too often, neither group is capable of strategically viewing the organizations overall financial picture. Often the financial department is much better at performing common operational tasks than at big-picture analysis or long-term program planning.

## **What are then key points to keep in mind in project budgeting?**

1. Develop sufficient **procedures** (e.g. using appropriate software) **to automatically and accurately identify overhead costs** and assign them to individual project budgets.
2. Ensure that **project managers understand the financial information** received from the financial department by building up their capacity.
3. Make it standard practice for financial staff to monitor and discuss **variances between budget and actual program costs** with project managers so the project managers may plan how to use remaining project funds.
4. Without sufficient financial management capacity organizationally, financial management of individual projects will suffer. The case should be made to funders to **invest sufficient support into developing organization-wide financial procedures**, implementing software and training finance staff to be able to set the proper indicators and **do broader-picture analysis** rather than perform just routine day-to-day financial tasks.

# **FINANCIAL ANALYSIS – WHAT IT CAN TELL US ABOUT POSSIBLE UPCOMING CHALLENGES**

Financial management often involves keeping certain financial indicators in right proportion. Significant departure from a ratio which was shown previously to work well might indicate upcoming difficulties. Some of the “red flags” in financial analysis include:

## **Declining ratio of unrestricted to restricted income**

This indicates the organization is less flexible in planning for its fundraising and institutional capacity development. It may be using restricted income to pay for its current bills – only running into cash flow problems later on.

## **Increase in short-term liabilities**

This indicates the organization postpones paying its bills as much as possible, possibly facing the situation when it is forced to apply for a short term “bridge loan” from a bank or a private lender to keep it from insolvency in the period before it receives planned income.

## **Reduction in administrative or project expenses**

Efforts to save money by scaling down administrative or programmatic functions are understandable when faced with decreasing income from grants or individuals or company fundraising. It may signal a return to core values of the organization but it may also signal its inability to formulate a vision appealing to donors and therefore a need to reposition the organization to meet new challenges in the society.

## **Declining surplus of income over expenses**

This indicates a problem with fundraising/income generation or with overspending. In any case it signals a future need to either intensify fundraising or scale down in order to cut expenses. In this situation, an accurate analysis of what is happening helps determine the right course of action.

# INTERNAL CONTROLS (AS PART OF FINANCIAL MANAGEMENT)

(adapted from *Financial Management For Nonprofits* by Corporation for Supportive Housing)

Enthusiasm within nonprofits is no guarantee against poor quality of financial information or possibility of error, fraud or mismanagement.

To safeguard the organization from the resulting impact and from associated reputation damage, internal controls are needed to:

- **To ensure the accuracy and reliability of financial records:** Leadership of the organization makes strategic decisions on its future in terms of human resources, programs, target groups, and sustainability partly on the basis of financial data as prepared by the finance office.
- **To protect assets of the organization:** Assets of the organization (whether money or physical assets) need to be protected from mishandling, whether wilful or resulting from negligence. A problem in this area is especially challenging to handle well if it must be communicated to organization's stakeholders such as its institutional donors or individual supporters.
- **To promote operational efficiency:** Internal controls help ensure that any lack of communication between the finance office and program managers or between the finance office and leadership of the organization does not create a situation when resources are spent ineffectively.
- **To encourage compliance with organizational policies and/or requirements set forth by funders.** Internal controls lead to a higher rate of compliance with organizational policies (e.g. regarding travel expenditure reporting) and less problems with financial reporting to funders who have special requirements (e.g. concerning exchange rates, acceptability of expenses).

The *Support for Training, Advocacy, and Networking in Developing Democracies (STAND)* project is funded through the U.S. Department of State, Bureau of Near Eastern Affairs, Office of the Middle East Partnership Initiative (MEPI). MEPI is a unique program designed to engage directly with and invest in the peoples of the Middle East and North Africa (MENA). MEPI works to create vibrant partnerships with citizens to foster the development of pluralistic, participatory, and prosperous societies throughout the MENA region. To do this, MEPI partners with local, regional and international nongovernmental organizations, the private sector, academic institutions, and governments. More information about MEPI can be found at [www.mepi.state.gov](http://www.mepi.state.gov).

