

Financial Management of Not-for-Profit Organizations

Introduction

Financial management of not-for-profits is similar to financial management in the commercial sector in many respects; however, certain key differences shift the focus of a not-for-profit financial manager. A for-profit enterprise focuses on profitability and maximizing shareholder value. A not-for-profit organization's primary goal is not to increase shareholder value; rather it is to provide some socially desirable need on an ongoing basis. A not-for-profit generally lacks the financial flexibility of a commercial enterprise because it depends on resource providers that are not engaging in an exchange transaction. The resources provided are directed towards providing goods or services to a client other than the actual resource provider. Thus the not-for-profit must demonstrate its stewardship of donated resources — money donated for a specific purpose must be used for that purpose. That purpose is either specified by the donor or implied in the not-for-profit's stated mission. The management and reporting activities of a not-for-profit must emphasize stewardship for these donated resources. The staff must be able to demonstrate that the dollars were used as directed by the donor. The shift to an emphasis in external financial reports on donor restriction has made the use of fund accounting systems even more critical.

Budgeting and cash management are two areas of financial management that are extremely important exercises for not-for-profit organizations. The organization must pay close attention to whether it has enough cash reserves to continue to provide services to its clientele. Cash flow can be extremely challenging to predict, because an organization relies on revenue from resource providers that do not expect to receive the service provided. In fact, an increase in demand for a not-for-profit's services can lead to a management crisis. It is difficult to forecast contribution revenue in a reliable manner from year to year. For that reason, the control of expenses is an area of increased emphasis. Budgeting therefore becomes a critical activity for a not-for-profit.

Budgets

Budgets are the organization's operating plan for a fiscal period. They express, in monetary terms, the board's and staff's decisions regarding how the organization will fulfill its stated purpose. The board

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