



Feature Article

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Stay True to Your Cost

By Andrea T. Mills, CPA, MBA

For many nonprofits, contracts that fund key programs carry a double-edged sword. While the contracts provide important program dollars, they often bring costly administrative demands and call for a reporting system that puts funder needs before your organization's. As a result, administering contracts may make it difficult for senior management to keep pace with the true cost of their programming.

These issues become magnified for nonprofits who oversee a mix of various programming. Often, in these scenarios, instead of determining the true cost of a program, expenses are defined by what the contract covers. Finance departments that use the contract-revenue line as the driver in determining budgets produce financial reports with expense amounts that balance perfectly - a clear sign that something is not right.

**There's a simple rule for financial reporting that I'd like to share:
"If your financials are balancing to zero, they're probably wrong!"**

Financial reports that do not accurately reflect reality are harmful. They prevent management from making informed decisions and could result in a programming mix based on contract needs, rather than the organization's mission. When working with our clients, we always emphasize the need for "True Cost Accounting."

The key to determining the true cost of your programs comes down to allocation of indirect costs. The administrative burden of management, overhead and fundraising should be reflective of what staff and resources those programs actually spend. Such allocations are most often identified through a mix of time studies, square footage, or supply usage. The key is to *allocate indirect costs consistently*, regardless of what the contracts may say. By using the true



cost of all programs, you can then identify to what degree each program contributes support towards the entity as a whole.

Organizations that identify true cost of programming garner access to a number of tools. They can identify operating margin (program-specific Surplus or Deficit divided by Revenue) to compare how much they gain or lose for every dollar of program revenue. They can conduct a per-unit cost analysis, which allows them to compare their services to market prices while also returning to funders with earnest data on what programs actually cost. Finally, organizations that know the true cost of programs have an easier time deciding whether to pursue RFP opportunities or, at the minimum, fully understand the risks they are taking with a submission.

Facing the truth can be uncomfortable sometimes, and for organizations that adhere to “True Cost” accounting, they must wrestle with some hard realities. But only through this process can a nonprofit make informed decisions that ensure they stay in the driver’s seat.

Andrea Mills is FMA’s Director of Outsourcing. For more information on how your organization may utilize true cost accounting tools, contact Andrea at AMills@fmaonline.net

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