Monitoring Return on Strategy

Can you link strategy, budget, and outcomes? You can. Here's how and why to integrate planning and financial management at a higher level.

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FINANCIAL SCANDALS HAVE ROCKED THE FOR-PROFIT AND NONPROFIT sectors, resulting in a demand for greater transparency and reliability in the fiscal operations of public organizations. For-profit organizations are invading the turf of nonprofits. Association boards are demanding that associations demonstrate that they've followed their strategic plans, and members are demanding that strategies be sensitive to current and anticipated reality, results oriented, informed, coherent throughout the organization, measurable, nimble, and adjustable.

To cope with the current environment, nonprofit organizations need to upgrade the way they do business. Most nonprofits today manage to the budget, which involves developing a plan for producing programs and services and earning revenue. They also devote resources to creating a strategic plan. Unfortunately, in the vast majority of associations, the budget and strategic plan are not integrated. Rather, they exist in insufficiently linked universes—the budget being an annual affair approving programs and estimated revenue most often for a single year, and the strategic plan setting multiyear objectives and often only revised every two or three years. In most nonprofit organizations, both documents have objectives—one is measured regularly, one is hardly ever measured. With two sets of objectives, what is the staff to do?

To best serve members—and respond to growing pressure for greater accountability and transparency—associations need to link the budget and the strategic plan. In today's 24/7 world, a 12-month cycle for adjusting strategy and asset allocation is often too little too late. Without timely financial measurements of strategic efforts, the reputation of an organization as relevant can be diminished, the usefulness of the association's program of work can decline, and trust in staff and volunteer leadership can be eroded. To operate successfully, this system should regularly measure receipts and disbursements, as well as monitor attained strategic goals and their associated costs.

To tie together operations and strategies, your organization will likely have to change, which can be discomforting and may be resisted. Your job will be to explain to your staff and board what they will gain. Staff members will have the chance to work on a new methodology that will allow them to focus closely on achieving what leaders identify as needing to be done. Board members, in consultation with staff, will be able to clarify with specificity the relative value and allocation priority of the outcomes they want to achieve. The leadership partnership will be able to assess the outcome—and the costs—of those efforts.

The existing accounting structure

If your association is like most, you probably use a standard income-and-expense accounting system designed to measure receipts, disbursements, and adjustments for noncash items, such as depreciation and amortization. This system, which is generally set up in a hierarchical fashion, includes a separate section for each department or division and further subdivisions for programs or projects. If you have a particularly large organization, you may have three or more tiers, depending on the complexity of your operations and the detail you wish to track.

This system helps you meet current reporting requirements because it allows for tracking and summarizing the various *natural* classifications of receipts (dues, interest income, etc.) and expenses (salary, travel, etc.) while simultaneously aggregating expenses by *function*—that is, by department or program. All of these aggregations are necessary for correct reporting, either to management, to the board, to the Internal Revenue Service, or in audited financial statements.

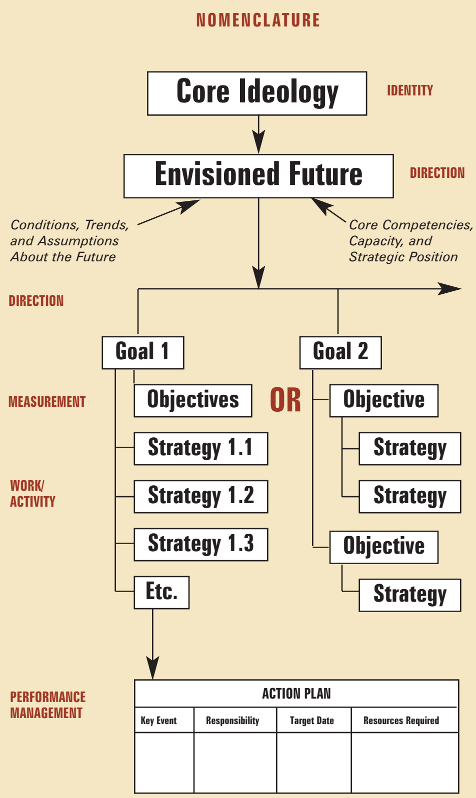
The chart of accounts drives this system. The chart, which generally differs from one association to the next, contains a string of numbers identifying the item to be accounted for. For multiple entities, such as your association and its foundation, the first one or two digits in the string will identify which entity the item relates to. If one or both of the entities is departmental, the next figures in the string will identify the department, and if multiple projects exist within that department, their identifier will come next.

For instance, if your association is 1, and your meetings department is 02,

Let's Be Clear About Your Goals

To determine the cost of any single element of your association's strategic plan, you must appropriately charge costs and related revenue. Unfortunately, the wide variety of terms used in strategic planning can cause confusion. The nomenclature you use, however, is not significant so long as you are consistent.

This article uses the following hierarchy: The highest level of desired results are *goals*, which are then subdivided into a series of *objectives*; each or all of which can be achieved by implementing its related *strategy*. The strategies are then divided further into *activities.* Put another way, if you successfully undertake your activities, you will succeed in your strategies (thereby achieving their related objectives), and if you succeed in your strategies, you can expect to accomplish your goals.



and your big annual meeting is 112, then the beginning of any income or expense related to your annual meeting will be 1-02-112. The next set of figures in the string usually identifies the type of revenue or expense that has been earned or incurred. For instance, if travel is 642, a travel expense chargeable to the annual meeting is 1-02-112-642.

Done by hand, this type of system would be tedious, but using software designed for the task, these strings of digits allow for rapid rollups of important data. For instance, you can find out at a glance what you have spent on travel on an associationwide basis, or for a single department by requesting a departmental and consolidated *natural* financial statement. Alternatively, you can ask that a *functional* statement be printed out and find out what has been received and spent on each project, program, or department being tracked. In effect, you can slice and dice the numbers in two different dimensions.

Adding a third dimension

How can you tie your strategic plan—and its outcomes—into your current accounting system? By assigning an additional set of digits to tag each receipt and disbursement to the activity it relates to in the strategic plan. For instance, all the activities involved in accomplishing the second strategy of the fourth goal could begin 42XX, and those for the third strategy of the fourth goal could begin 43XX.

This mechanism for tracking expenditures against accomplishments can work regardless of the current budgeting approach you use. It doesn't matter if you have a functional budget, a program-based budget, or a zero-based budget. Traditionally, none of these budgeting approaches have a mechanism for tracking expenditures against the specific strategic value you're trying to attain.

Before you do this, of course, you will need to take three steps:

1. Make sure that your software can manage yet another group of digits (perhaps three or four) to each string.

2. Reduce your goals to their individual strategies and each strategy to its component activities.

3. Develop a methodology that systematically numbers each of the activities. You will want to ensure the system is logical so that staff can easily learn and effectively use it.

Using this methodology, as the staff members record the income and expense items using the basic chart of accounts, they would also be keeping in mind what part of the strategic plan is being achieved and would charge that activity. The result would be the ability to print a report isolating the receipts and disbursements of a specific goal, or each or any of its strategies, or each or any of its particular activities. For a not unreasonable amount of effort, your association's strategy would be firmly linked to everyday endeavors.

How difficult will it be to start using this system? Much depends on your association's current budgeting process. For example, imagine that budgeting for expenses can be divided into four evolutionary steps:

1. Having a natural budget.

2. Having a functional budget so that you know how much you're paying for various products and services for each program.

3. Having an integrated budget that allows you to track expenses as in one and two above, in addition to rolling up all costs at a program, department, and entity level.

4. Having an integrated budget that lets you track expenditures in terms of strategic outcomes.

Associations that can already roll out their integrated budgets by function and by program will have a third way to roll out their budgets: by strategic outcome. Associations that do not already have integrated budgets may, in fact, need to have two budgets—their existing budget and a parallel strategic budget.

Make your plan measurable

To gain maximum use of the system, first develop a strategy plan and then develop the strategic budget, which will indicate precisely how much is to be spent on each activity, and thus on each strategy, and thus on each goal. As you create your strategy, keep the following principles in mind:

- *Identify what your organization hopes to accomplish* in the foreseeable future in six or fewer goals. The goals of the plan should represent outcomes, conditions, or attributes the association wishes to achieve.
- *Frame each desired outcome in terms of the value* that will accrue to those served by the organization, once the goal is achieved.
- *Ensure that each goal has objectives that represent changes* in significant conditions—and the direction of the change—related to a given goal. Direct or indirect measures related to the objective can be tracked across time to determine whether progress is being made toward the desired outcome.
- *Prioritize strategies,* which describe the nature of the work required to accomplish the goal and its companion objectives. Each strategy should include an action plan.
- *Create detailed action plans,* which link your association's strategic plan to its everyday activities. Plans should include who will do what, by when, using what resources to execute the strategy, and must have companion strategic budget worksheets. You can use your existing chart of accounts to build the worksheet.

Strategic budget adds value

Practically speaking, it might make more sense for you to determine the relative value of goals and allocate to each the sum you wish to expend on it as compared to the others. Once the largest split is done, allocations can be made within each goal's budget to undertake each strategy, and so on down into the activities.

For example, suppose your association has two goals:

1. Members will have instant access to the information and insight they require to effectively make decisions on a daily basis.
2. The value of members' contributions will be fully appreciated and members will be compensated accordingly.

Assume that after many conversations with members and market research, you find out that the first goal should be the priority. Consequently, you dedicate 60 percent of your $1 million budget to the first goal and 40 percent to the second goal. Also assume that the first goal has three objectives, and you have selected seven strategies to achieve those three objectives. You can now determine the relative importance or value of each of the strategies and dedicate X amount of the $600,000 to each of the strategies. Here's the wrinkle: You cannot do that in a knowledgeable fashion until you have an action plan for each strategy. Until you get to action planning, you cannot determine the cost of each strategy, which you need before you decide how much to allocate to it. You may discover that one strategy will only cost $10 and decide to proceed. You may also discover that a high-priority strategy will cost $650,000, which you don't have, and have to rethink it.

Allocating funds in this manner takes what is often an emotional or political decision and makes it more rational. The answers to two critical questions—"How important is the outcome we're trying to achieve?" and "To achieve that outcome, how much will the work cost?"—will determine how much you allocate.

The result: Across time the strategic budget can be compared to the actual activity. Nearly instant information can be gained as to where your organization stands in its efforts to fund its drive toward fulfilling its goals. When these figures are then compared to the outcomes achieved to date, your organization can demonstrate its unique value to members. In addition to the usual natural and functional financial statements, you can create strategic reporting statements as well. Whenever you wish, you can measure your success in achieving your objectives and thus achieving your goals and compare that to their related costs and revenues, if any.

This will allow your staff and leaders to accurately assess return on investment and demonstrate in a trackable and transparent fashion how your organization has spent its resources. Although it will allow you to make knowledgeable decisions with confidence, this system will not replace good judgment.

Accurately measuring costs

Although your association may have well-developed methods for tracking costs, before taking your organization to the level of strategic reporting statements, you should make sure that you correctly apply costs in two critical areas:

1. Employee costs. To avoid serious errors in accounting for costs, you must keep track of staff time. This means timesheets. There is simply no other alternative. Readily available software makes it easy for staff members to allocate and track their time. Individuals who are involved in a variety of strategic activities each day should update timesheets daily. Studies of professional firms, where many matters are worked on each day, find that waiting even one day to record time translates into a substantial loss in accuracy.

2. Indirect costs. Failing to correctly apply indirect costs frequently creates errors in accounting. For example, it would be hard for you to miss the fact that the cost of 10 airplane tickets to attend a meeting is directly related to that meeting. But what of the time it took for your administrative staff person to order those tickets, or the cost of the space in which that administrator was sitting? These indirect costs, which should be allocated to various activities, are often lumped into an administrative category instead of being reasonably allocated to whatever was being made possible by them.

These costs, while small in and of themselves, add up. The best method for handling these various indirect costs is to pool them by like kind and then allocate them to the various programs or activities based on a reasonable, consistently applied method. (For a more detailed discussion of issues related to program-based budgeting, see the February 2003 issue of ASSOCIATION MANAGEMENT.)

A process for determining success

Because identifying objectives and measures can be daunting, strive for utility rather than perfection, particularly in the learning curve. The validity of the measures as indicators of direction and progress is more important than quantifying an arbitrary degree of achievement. The process involves three basic steps:

1. Identify an existing condition or trend that made you think you needed a goal to address it to effectively fulfill the organization's purpose.

2. Determine what you want to have happen with that condition. In what direction do you want the condition to move? For example, do you want the condition to increase, decrease, become universal, or never occur?

3. Develop a measurement related to the objective. What is it you will be able to know or observe across time to judge achievement?

Getting started

How you manage the change strategy is just as critical as how you implement the technique. There is no one best way or order. Your implementation should build on the strengths of your current accounting system. Customize the details of the approach to your organization, remembering that the results could alter the culture of your associa-

Measuring Outcomes

In 1998, the American Compensation Association (now World at Work) began to measure outcomes, in addition to outputs, for two reasons: to produce new program, structure, process, and cultural strategy for the organization and to institutionalize an informed process of continuous strategy development, monitoring, and adjustment.

The following example may be a helpful model as your association moves to outcome-oriented measurement.

GOAL 1 (of four): Individuals and organizations with an interest in total rewards management, or any of its four facets, will have easy access to a quality knowledge base that will enable them to more confidently make informed decisions about policy and practices.

OBJECTIVE 1.1 (one of several): Increase the size and value of knowledge base of total rewards management.

Measure 1.1.1 (output; one of several): Knowledge assets available in the compensation database will increase 20 percent each year until 2005.

Measure 1.1.2 (outcome; one of several): Survey conducted in accordance with the Marketing Research Plan [2.2.2.5] will demonstrate increased customer perception that the four-dimensional database meets their needs each year until 2005.

Measure 1.1.3 (output): The number of knowledge creators and providers contributing to the rewards management knowledge base will increase by 20 percent each year until 2005.

Measure 1.1.4 (outcome; one of several): Ratings of the value to the members' company of application of knowledge obtained, reported by 85 percent or more respondents in a stratified random sampling of database users, will achieve a rating of "8" or better on a 10-point scale by 2005.

tion in terms of what the association is willing to be held accountable for and what staff views as important.

During your first year of measuring strategic outcomes, you will need to take a number of actions:

- Ensure that the goals and objectives that comprise the results or outcomes to be pursued are identified.
- Determine strategic choices and decide which strategies and activities will be required.
- Identify the relevant conditions that will be tracked and the mechanisms for measurement. This will be a challenge. It is far easier to measure inputs and outputs than to measure outcomes. It's the difference between declaring an annual conference a success because attendance increased 20 percent or being able to recognize that increased size negatively affected the quality of experience and program and more people went home dissatisfied with less useful knowledge than ever before.
- To be fair to all parties, treat the initial year's cost estimates for the activities in the strategic plan as exploratory. After all, the cost estimates will have no historical precedent your first year.
- Complete the strategic budget before the financial budget. Once you have determined how you will fund your strategic activities, you will have a clearer understanding of what is available to spend on new and existing programs. This is a key step so allot adequate time for this exercise.
- Set reporting dates, likely no more frequently than quarterly, for the creation of strategic reporting statements.
- Once the year is under way, share the data with the staff members responsible for the various activities.
- Report successful achievement of outcomes and assess the value of the return on the investment to the board. With this information in hand, board members can see that the association is investing its efforts as they directed, compare expenditures by activity to date with the strategic budgets they approved, analyze trends, and make decisions on how to allocate the association's efforts in the future.

Why you should try it

Why spend money to tie purchases to value, value to purpose, and expenditures to desired outcomes? Because of increasing demands for value-based accountability, exemplified in the influence of Sarbanes-Oxley and proposals for similar legislation specific to nonprofits in several states.

Why allocate time and human resources to an early-warning system that enables you to monitor whether strategy is working and investments in change are paying off? Because technology has increased members' expectations. What used to take years now takes weeks, and what used to take hours is now accomplished in seconds. Members demand access to actionable information in compressed time, and they expect more value than ever before.

Members want to optimize the investment of both their time and money in their associations. By using this measurement and early-warning system, your association will allow members, elected leaders, and staff to track strategic outcomes and costs and to monitor returns on investment. In the process, you will create a culture of transparency, demonstrate value to members, and nimbly monitor and adjust strategy based on evidence, rather than the opinion of the moment. AM

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