Who holds the keys to change?

Getting change to occur in any organisation is difficult. Often it seems even more so in the NFP/charity sector. We explore some of the reasons why and seek to answer the question; "Who holds the most effective keys to facilitating change."

Background

We all know the truism that "change is constant". And it is. However in many organisations, being able to instigate change, or effectively respond to change, is often very difficult. Generally the barrier to change is not the nature of the changes needed, but rather the emotional or human barriers to accepting the need and then moving to doing something about it.

Interestingly this situation is usually more pronounced in NFP organisations than it is in For-Profit organisations. This is understandable when you consider some of the key differences between the two types of organisations. This includes that most For-Profit organisations are generally more command and control in operational style, and more binary in their decision making, i.e. the driver for most decisions are: Will this make us more money - yes or no?

NFPs by contrast are commonly much softer in governance and management style because they often involve elements of volunteering and social motivation, as well as being driven more by service delivery rather than a single minded financial profit driver like the majority of For-Profit businesses.

Sadly however this can translate into NFPs being much more inefficient in how they do what they do, and much more resistant to change. By not being forced to innovate as much as many For-Profit entities they can become flabby and inefficient. Conversely, some NFPs are too lean, such that innovation is unable to flourish through lack of skills, time and resources.

Ironically though given the above, in times of financial crises or stress it is usually NFPs that will survive, or survive longer than many For-Profits. Even though they don't have the same single minded focus on their financial bottom line and financial sustainability, when times get tough their key stakeholders will generally support them "just enough" so they can struggle on. Whereas by contrast, the situation for companies is much more binary; they either make enough money to stay in business or they go out of business.

Related to the above is the concept that; starvation often forces innovation. And those that don't innovate generally decline.

As an audit firm we commonly get called in to NFP organisations to investigate messy financial situations. Equally common is that by the time we get called in, either by the organisation in desperation, or by a key stakeholder, the NFP is usually at or near financial crisis stage. As the finances of any organisation are just a symptom of other factors we usually end up looking not only at the financial mess but also the root causes of the mess. Once you get your head out of the numbers the reasons for the financial crisis are most commonly traced back ultimately to governance, and the decisions and structure that flow from that.

This repeated experience over many years has got me increasingly interested in the drivers for change and more importantly, the barriers to change.

So why do organisations change?

While completely unscientific, our anecdotal experience has shown that there is a clear pecking order of reasons that change in NFPs happen. In reverse order we have found the following to be the 8 main drivers of change:

8. It's the logical rational thing to do and a result of a desire for best practice
7. It's the advice of expert advisors

6. Combatting the threat of competition
5. Changed operating model
4. National body requires the change
3. Financial crisis forces change
2. Legislation forces change
1. The funding body requires the change for continued funding

Hence this list goes from the least common reason being "It's the right thing to do"; to the most common being "Those holding the funding are the most powerful motivators of change". While it may seem hard to accept that rational logical reasoning is a poor motivator for change, it reinforces the emotional barrier - quite simply humans are hardwired to avoid pain and change presents the threat of pain.

Funders hold the keys - and a significant opportunity

So if funders recognise and accept that they are the most powerful motivator for change, this presents them with a real opportunity to help to both facilitate positive change and to reduce pain in the NFP sector.

Here are some ways where we believe innovative funders can best assist using their position of significant influence:

1. **Encouraging Collaboration & Efficiency**

   Funder Opportunities

   - Funders can encourage collaboration or even combinations of entities to help create more efficient and effective service delivery. The main barrier is usually sovereignty concerns. Influence from funders can help organisations overcome this.
   - Encouraging hubbing or shared service models – utilising specialist expertise and technology to leverage highly efficient administration across a range of entities that individually would never be able to afford that level of specialist skill, systems, and expertise. Funders can help educate, assist with facilitating and even fund establishment of shared service operations.

2. **Financial Reporting Change to Performance Reporting**

We are currently faced in New Zealand with the biggest change in financial reporting legislation in the past 20 years. In relation to financial reporting for charities and NFPs it is possibly the biggest change ever! Registered charities are now required by law to follow Public Benefit Entity (PBE) accounting standards, which are themselves effectively legal instruments. Other NFPs such as incorporated societies are expected to be required by legislation to do similar with the overhaul of the Incorporated Societies Act. In addition, the removal of the former accounting standards effective 1 April 2015, along with the need to compete for funding will likely see other NFPs follow these new accounting standards as there won't be any other standard form of reporting. Hence our prediction is that they will become the defacto standard even for those not required by law to follow them.

The new PBE standards also require a move to mandatory service performance reporting. This is an excellent innovation for the sector and will help move the focus to the important metrics of performance against entity purpose, rather than just financial performance. The fact that service performance reporting is mandated by PBE standards should eventually result in better clarity and consistency of reporting to stakeholders.

Funder Opportunities

→ Funders can assist with education of NFP/Charitable entities to help raise awareness, understanding of and adoption of the new mandatory PBE reporting standards. Consistent compliance with the new standards will greatly assist funders in an improved level and consistency of reporting to them. Funder assistance may be direct, or by facilitating others to deliver this.

→ Service performance reporting, once understood and adopted, will provide much greater consistency and quality of reporting. It should also help funders receive more information they require from one place. i.e. they will get this from the mandatory annual performance report. This presents policy opportunities to ensure that, as much as possible, funders are aligning their information requirements to the mandatory performance reporting and not imposing a variety of other information demands on

NFP/Charitable entities. The increasing variety of funder information demands on NFP/Charitable entities is a significant drain on their available capacity to actually deliver on their purpose. Funder consistency and alignment on this could have significant sector benefits.

→ Technology is a great enabler. Innovative technology providers, such as the accounting software provider Xero, have been encouraged and are responding to the opportunities of aligning their software with the new PBE performance reporting requirements. This has significant potential benefits for sector entities in terms of not only successfully changing to the new reporting requirements, but also in the efficiency and effectiveness of how they are accounting. This example is also an enabler of other innovations like shared service hubs, as finance is one of the most logical shared services to begin with. Funders could assist by encouraging adoption perhaps via partial funding initiatives.

Requiring Independent Assurance

Traditionally most NFP/Charitable entities in New Zealand have been audited. Very often this requirement is at the request of funders. However audit standards and expectations of auditors have increased significantly over the past 2 decades. This has reduced the number of specialist auditors and increased audit costs.

An audit of financial statements also does not, of itself, guarantee that funding has been used for the desired purpose or that there has not been any fraud. This means that requesting an audit may not be achieving the most cost-effective result for funders.

The Government has also legislated the levels at which they believe it is appropriate for registered charities to have to obtain independent assurance. This sets an interesting “bright-line” level that may be of interest for funders to reconsider their levels. The legislated levels are:

- → a mandatory audit for registered charities with annual operating expenditure over $1m per annum
- → the choice of either a review or an audit if annual operating expenditure is over $500,000 but below $1m;
- → no mandatory requirement below annual operating expenditure of $500,000 per annum.

Funder Opportunities

Funders can revisit their independent assurance requirements and ensure appropriate to the level of funding and risk. Aligning their policies to the Government–set levels above will eliminate undue additional requirements on funded entities. If the Government levels are seen as too high then at least aligning assurance requirement policies amongst significant funders would be an improvement.

For smaller entities there may be much greater funder benefit in assisting the NFP/Charitable entity to comply with the new PBE reporting standards rather than imposing an audit.

Summary

Funders hold much more power in their hands and actions than they may realise. This power presents a significant opportunity to help the NFP/charity sector, themselves and New Zealand Inc. It will however require funders to take some different actions as well as to work together to really leverage this great opportunity.

By embracing some of the opportunities above, funders can turn the keys and indeed be in the driver’s seat to help remove some potential pain and to make the NFP/charity sector a faster, higher performance vehicle!

About the Author

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