

# An appraisal framework for the sustainability of non-governmental organisations

**Rozenda Hendrickse**

Department of Public Management  
Cape Peninsula University of Technology

## **ABSTRACT**

This article supports an appraisal framework for the sustainability of non-governmental organisations (NGOs). A theoretical analysis of existing literature on governance and the financial sustainability of NGOs have revealed that there is no generally agreed upon appraisal framework for assessing the long-term sustainability of NGOs. However, a number of NGO stakeholders would benefit from this type of framework. Research has revealed that, in terms of sustainability, it is particularly necessary to assess an NGO's legal status, its leadership capacity, the roles and responsibilities of the executive management, the role the NGO board plays in its governance processes, as well as the extent to which principles of good governance are practiced within the organisation. These key criteria have proven to be the most important in the governance endeavours of NGOs. Therefore, it has become evident that fundraising strategies, good practices in financial management, sources of NGO funding and financial control mechanisms should be assessed, as these key aspects have proven to impact on the organisation's financial sustainability. In the article, theoretical assessment and case experiences are used to develop an appraisal instrument. This appraisal instrument was custom-designed for the South African NGO sector in particular.

## **INTRODUCTION**

A theoretical analysis of existing literature on governance and the financial sustainability of NGOs revealed that there is no generally agreed upon appraisal

framework for assessing the long-term sustainability of NGOs. However, it was found that a number of NGO stakeholders would benefit from a type of framework as an appraisal instrument that is custom-designed for the South African NGO sector in particular.

The purpose of the appraisal instrument proposed in this article is to provide a framework for assessing the governance and financial sustainability of NGOs. During this research investigation, many NGO stakeholders noted that a standardised appraisal system would be particularly useful to NGO bodies such as community-based organisations (CBOs), civil society organisations (CSOs), statutory bodies that exist to regulate NGOs, network organisations, organisations providing funding, as well as NGO managers. This instrument does not negate the importance of the NGO's output or impact on its constituents. Whilst the latter is imperative to the survival of an NGO, this research focuses on NGO's compliance with good governance and financial management practices.

## **THE APPRAISAL FRAMEWORK**

The purpose of this appraisal instrument is to provide a framework for assessing the governance and financial sustainability of NGOs. During this research investigation, many NGO stakeholders noted that a standardised appraisal system would be particularly useful to NGO bodies such as community-based organisations (CBOs), civil society organisations (CSOs), statutory bodies that exist to regulate NGOs, network organisations, organisations providing funding, as well as NGO managers. This instrument does not negate the importance of the NGO's output or impact on its constituents. Whilst the latter is imperative to the survival of an NGO, the focus of this research focuses on an NGO's compliance with good governance and financial management practices.

The governance and financial sustainability appraisal framework for NGOs consists of systematically developed appraisal criteria based on theoretical assumptions and empirical evidence explored by this research. Its purpose is to assess and to make explicit recommendations with a definite intention of influencing how NGOs are governed and financially sustained.

The appraisal framework is intended for the following groups (Hendrickse 2008:200). This includes:

- Policy makers in South Africa with specific reference to: The South African Revenue Service (SARS); The Master of the High Court; The Minister for Social Development; The Director-General of Social Development and The Registrar of Companies with regard to Section 21 companies. The framework will to help them decide which guidelines could be recommended for NGOs in relation to their governance and financial sustainability. In this

instance, the instrument should be part of a formal assessment process. This instrument should not be used to the detriment of civil society organisations that are lobbying government to change/reformulate certain public policies, nor should NGOs calling for new legislation on certain issues be penalised.

- NGOs/CBOs/CSOs, as a self-assessment tool to ensure sound governance and financial sustainability practices.
- Government, donors, private sector social responsibility funders, the National Development Agency (NDA) and development banks that wish to undertake their own assessment of an NGO/CBO/CSO before committing any resources.
- NGO/CBO/CSO staff should help identify critical skills that the organisation requires.

An appraisal form has been formulated and consists of a governance section and a financial sustainability section. Each section consists of assessment criteria against which scores are assigned. A practical cumulative scoring system has been devised. An assessor with extensive experience in the area of NGOs should facilitate this system.

The theoretical assumptions forwarded by the study form the basis of the assessment criteria utilised in the appraisal framework. In particular, evidence suggests that an NGO's legal status proves imperative to its legitimacy and its receipt of funding. NGO managers, in turn, influence the organisation's longevity – particularly where subordinates are groomed to take up leadership. The form of leadership the organisation practises – whether autocratic or participatory – is an essential component of NGO governance. An NGO's executive management should understand its roles and responsibilities. Furthermore, theorists suggest that diversity in terms of the NGO board's composition and skills is of utmost importance to ensure the NGO's sustainability. Lastly, the extent to which principles of good governance is applied will influence the organisation's sustainability (Hendrickse 2008:201).

An organisation's financial sustainability depends on the sources of NGO funding, the management of a funding strategy, as well as sound financial management and control. Self-financing strategies that an NGO employ are proposed as key contributors to its long-term prospects. The research suggests that it is imperative for NGOs to apply good financial management practices and financial control. Most NGOs do not have clearly defined fundraising strategies or personnel responsible for fundraising. In many instances this has led to the organisation's early demise. Williams<sup>1</sup> (2008:2) contends that:

“Donors have the upper hand in terms of determining what aspects of an NGO they would fund. Generally they want to focus on programme

delivery and often sets limits to the overhead/organisational/administrative costs of the organisation, including governance costs. In this context it would be unlikely that donors would provide resources for a fundraising capacity. In addition, if an NGO appoints an external fundraiser the donor may argue that if they do not have the capacity to develop funding proposals and liaise with donors what internal capacity exists to manage their funds and the programme? Furthermore, most external fundraisers require a percentage payment out of the funds they raised. Most donors would not agree to pay such a commission and this puts the NGO in a difficult position if it receives funds through the efforts of an external fundraiser. Do they misappropriate funds from the donor to cover the costs of the fundraiser or do they take on contract work to cover this cost. In so doing their focus is shifted away from the programme that the funder originally intended for them to work on”.

The above suggests that it is important to consider each of the criteria in this assessment instrument before any score is assigned. The user should follow the various steps to ensure that this framework is utilised properly.

In concluding the appraisal process, score categories have been developed to help indicate whether the NGO is sustainable, or whether particular areas require improvement. The NGO’s total score should be measured against one of the following score categories:

**Diagram 1: Sustainability indicator**

| Score Category  | Final Score | Sustainability Indicator   |
|-----------------|-------------|--|
| Green Category  | 60% +       | Sustainable  |
| Orange Category | 41% – 59%   | Strengthen governance and financial management practices                             |
| Red Category    | 0% – 40%    | Drastic action required with regard to governance and financial management practices |

This study’s theoretical and empirical research formed the basis of the following appraisal framework. The key categories includes the NGO’s legal status, standards of accountability and transparency, the leadership, roles and responsibilities of the executive management, the board, the extent to which

## Appraisal Form 1: Appraisal instrument for the sustainability of NGOs

|                          | Appraisal criteria   | Maximum Score | Score attained |
|--------------------------|--|---------------|----------------|
| Governance               | NGO legal status.  | 10            |                |
|                          | NGO leadership (Chief Executive Officer/Director/Manager).       | 10            |                |
|                          | Roles and responsibilities of the executive management.          | 10            |                |
|                          | NGO Board.   | 10            |                |
|                          | The extent to which principles of good governance are practiced. | 10            |                |
|                          | <b>Score: Sub-Total</b>  | <b>50</b>     |                |
| Financial sustainability | Sources of ngo funding.  | 10            |                |
|                          | Self-financing strategies.                                       | 10            |                |
|                          | Good practices in financial management.                          | 10            |                |
|                          | Financial control measures.                                      | 10            |                |
|                          | Fundraising strategies.  | 10            |                |
|                          | <b>Score: Sub-Total</b>  | <b>50</b>     |                |
| <b>Total Score:</b>      |  | <b>100</b>    |                |
| <b>Percentage Score:</b> |  |               | %              |

principles of good governance are practiced, sources of funding, self-financing strategies, good practices in financial management, financial control measures and fundraising strategies. These areas will be discussed in detail in the following sections.

The user should note that the criteria and weighting of scores are relative. Weighting (how many points are allocated to each criterion) can be adjusted depending on the value placed on particular criteria, within acceptable parameters and particularly by facilitating agreement between stakeholders of a particular NGO being appraised. In this context, where a particular criterion may require an adjustment, an acceptable parameter will be an adjustment of not more or less than two points in the score column in question

The next section will explain the theoretical relevance of the assessment criteria. It will also provide perspectives on the reasoning for the assessment scores pertaining to each criterion.

## NGO legal status

In the South African context, the *Nonprofit Organisations Act* (Act 71 of 1997) (hereafter *NPO Act*) has been enacted to provide an environment in which non-profit organisations can flourish. Furthermore, it establishes an administrative and regulatory framework within which non-profit organisations can conduct their affairs.

The *NPO Act* encourages and supports non-profit organisations in their contribution to meeting the diverse needs of the South African population. In particular, these organisations are encouraged to maintain and improve adequate standards of governance, transparency and accountability. The *Act* provides that the minister responsible for non-profit organisations prescribes benefits and allowances to **registered** non-profit organisations. This is done after consultation with the committees of the two Houses of Parliament responsible for welfare and with the concurrence of every minister whose department is affected by a particular benefit or allowance (*Nonprofit Organisation Act of 1997* (Act 71 of 1997)).

The South African Government encourages the registration of non-profit organisations. Moreover, research has shown that local and international donors are also increasingly demanding that their grantees are registered as non-profit organisations, as evidence of compliance with basic criteria of authenticity as a *bona fide* organisation.

As the legal status of NGOs has proven to be an important aspect of good governance, the criteria of: the existence of a legal entity; an NGO registered as a non-profit organisation under the *NPO Act 1997*; an NGO registered as a PBO; a non-profit trust registered under the *Trust Property Control Act 1998*; an NGO registered as a Section 21 not-for-profit gain organisation under the *Companies Act 1973* as well as an NGO registered for value added tax (VAT) are suggested for determining the status of an NGO in this respect (See Appraisal Diagram 1.1).

## NGO leadership

Leadership is the process of establishing direction and influencing others to follow that direction. Often the leadership style adopted, for example, autocratic, people-orientated, participatory, democratic or *laissez faire*, depends on the circumstances that prevail and the NGO's life cycle (Centre for African Family Studies 2001:7, Odiorne 1969:81-90, Greenberg and Baron 1997:437).

As corporate governance is essentially about leadership, it is imperative for this concept to be assessed within an NGO. Williams<sup>2</sup> (2008) contends that one of the key problems in many NGOs, "...is the confusion between governance

## Appraisal Diagram 1.1

| GOVERNANCE APPRAISAL  |                   |                   |
|---|-------------------|-------------------|
| NGO LEGAL STATUS<br>Assessment Criteria   | Possible<br>Score | Score<br>Assigned |
| Existence of a legal entity.  | /5                |                   |
| Registered as one of the following: <ul style="list-style-type: none"> <li>• NGO registered as a non-profit organisation under the <i>NPO Act of 1997</i>.</li> <li>• Registered as a PBO.</li> <li>• Non-profit trust registered under the <i>Trust Property Control Act 1998</i>.</li> <li>• Section 21 not-for-profit gain organisation as per the <i>Companies Act of 1973</i></li> </ul>   | /4                |                   |
| Registered for value added tax (VAT).   | /1                |                   |
| <b>Sub-total</b>  | <b>/10</b>        |                   |
| <b>How to assign scores</b> <ul style="list-style-type: none"> <li>• Insert a score in each column. Where the organisation does not meet the specified criteria, assign a zero (0). Where the organisation has partially met the assessment criteria, where appropriate and at the discretion of the assessor, assign a score of between five (5) and zero point five (0.5).</li> <li>• Transfer sub-total of score attained under Appraisal Diagram 1.1 to the appropriate block in Appraisal Form 1.</li> </ul> |                   |                   |

and management. By grouping all in terms of leadership, this confusion is exacerbated.” It is therefore important to clarify the hierarchical relationship between the governing board and the chief executive officer (CEO). To eliminate such confusion, NGO leadership in the context of this appraisal instrument refers to the operational arm of the NGO – chief executive officer, director, manager or management,.

With regard to NGO leadership, some commentators refer to charisma as a key attribute. According to Indian, Kenyan and South African commentators, in the NGO context, a charismatic leader is able to attract funding, which in turn impacts on the organisation’s financial sustainability. A charismatic leader exhibits confidence, dominance, a sense of purpose and the ability to articulate goals. Furthermore, this type of leader is considered an exceptional person. And, his/her sheer presence and personality helps shape and influence the future of an organisation (Bass 1990; Raelin 2003).

In the above context, the following assessment criteria have been devised under the heading “NGO leadership”. Scores can be assigned, as indicated in Appraisal Diagram 1.2.

## Appraisal Diagram 1.2

| GOVERNANCE APPRAISAL  |                   |                   |
|---|-------------------|-------------------|
| NGO LEADERSHIP<br>Assessment Criteria   | Possible<br>Score | Score<br>Assigned |
| The NGO displays ALL of the following leadership criteria.  | /3                |                   |
| NGO manager/director displays transparent and accountable leadership in line with the organisation's constitution.  | /1                |                   |
| NGO leadership (manager/director) is not centred on a particular individual and where the manager is also the chairperson of the governing board. Clear separation of powers exists between the two entities.   | /1                |                   |
| NGO has a charismatic leader (director/manager).  | /1                |                   |
| NGO manager/director delegates the management of the organisation to senior executive staff (where subordinates exist).   | /1                |                   |
| NGO manager/director served for three years or more as managing director or director.   | /1                |                   |
| NGO manager/director effectively manages the organisation's operational arm, and the chairperson of the governing board and/or governing board does not intervene in the organisation's administrative issues – except in the formulation of operational policies.  | /1                |                   |
| The chairperson of the governing board supervises the director/manager/management on a regular basis.   | /1                |                   |
| <b>Sub-total</b>  | <b>/10</b>        |                   |
| <p><b>How to assign scores</b></p> <ul style="list-style-type: none"> <li>• Insert a score in each column. Where the organisation does not meet the specified criteria, assign a zero (0). Where the organisation partially meets the assessment criteria, where appropriate and at the discretion of the assessor, assign a score of between three (3) and zero point five (0.5).</li> <li>• Transfer sub-total of score attained under Appraisal Diagram 1.2 to the appropriate block in Appraisal Form 1.</li> </ul> |                   |                   |

## Roles and responsibilities of executive management

The operational arm of an organisation should manage the NGO. This includes an executive management team, which typically includes the organisation's CEO. Ideally, this team should have clearly assigned roles, functions and responsibilities.

How these roles and responsibilities are defined and executed determine the power relations, balance of authority and the extent to which an organisation will run smoothly, effectively and professionally (Camay and Gordon 2002:3, The National Association of Non-governmental Organizations in Zimbabwe 2005:1).

Essentially, the executive management team combines human resources, material resources and financial resources into a productive system in which organisational objectives are attained (Odgers and Keeling 2000:109-110). This requires an organisational structure, policies, systems, qualified, committed staff as well as a facilitating institutional environment.

The lack of skills or insufficient management capacity to oversee and ensure the successful implementation of NGO projects and the delivery of services was quoted as a key factor contributing to the problems many NGOs face (allAfrica 2002:2). Aforementioned suggests that an organisation’s executive management structure should have clearly-defined roles and responsibilities. Within this context, the following assessment criteria have been developed.

Under the assessment criteria “Roles and responsibilities of executive management” the following scores can be assigned:

### Appraisal Diagram 1.3

| <b>GOVERNANCE APPRAISAL</b>   |                       |                       |
|---|-----------------------|-----------------------|
| <b>ROLES AND RESPONSIBILITIES OF EXECUTIVE MANAGEMENT<br/>Assessment Criteria</b>   | <b>Possible Score</b> | <b>Score Assigned</b> |
| The NGO meets ALL the assessment criteria, as stated in this diagram, pertaining to the roles and responsibilities of the executive management structure. <i>(First complete the sections below before assigning a score in this block.)</i> .  | /4                    |                       |
| The executive management team clearly understands its roles and functions.  | /1                    |                       |
| The executive management team has clearly assigned responsibilities.  | /1                    |                       |
| A cohesive management structure exists.   | /1                    |                       |
| Executive management effectively and efficiently manages the NGO’s resources.   | /1                    |                       |
| Executive management upholds the NGO’s vision, mission and strategic objectives as displayed in its constitution..  | /1                    |                       |
| A sound strategic and business plan exists. Executive management assisted in its formulation and oversees its implementation.   | /1                    |                       |
| <b>Sub-total</b>  | <b>/10</b>            |                       |
| <b>How to assign scores</b> <ul style="list-style-type: none"> <li>• Insert a score in each column. Where the organisation does not meet the specified criteria, assign a zero (0). Where the organisation partially meets the assessment criteria; where appropriate and at the discretion of the assessor, assign a score of between four (4) and zero point five (0.5).</li> <li>• Transfer the sub-total of the score attained under Appraisal Diagram 1.3 to the appropriate block in Appraisal Form 1.</li> </ul> |                       |                       |

## Composition and skills of the board

The separation of governance and management involves a division of both duties and personnel. The usual rule is that management runs the organisation from day-to-day, while the board sets policy, oversight and strategically guides the organisation (Wyatt 2004:11b-16b, Centre for African Family Studies 2001: 16 & 27, Block 2001).

The King II Report (2002) suggests that the governing board seeks to ensure an adequate mix of skills, experience and diversity in demographics to enable them to operate effectively and efficiently. NGO governing boards may delegate responsibility to others, such as paid staff. However, they must accept ultimate responsibility for the governance of the NGO. Preconditions for the recruitment of new board members include identifying NGOs' governance needs and discovering how the characteristics, qualities and skills of potential board members correspond to the organisation's needs (Block 2001; Camay and Gordon 2002:43-45).

The Centre for African Family Studies (2001:16) reports that where board members are friends and family, or are intrinsically linked to the organisation, for example, board members are also founder members of the NGO, they cannot always act independently and in an unbiased fashion. Therefore, development theorists<sup>3</sup> suggest that the governing board be composed of 50% internal membership and 50% external membership. This ensures an equitable distribution of power.

Under the assessment criteria "composition of the board", the following scores may be assigned:

### Appraisal Diagram 1.4

| GOVERNANCE APPRAISAL  |                |                |
|---|----------------|----------------|
| COMPOSITION AND SKILLS OF THE BOARD<br>Assessment Criteria  | Possible Score | Score Assigned |
| Existence of a governing board.   | /4             |                |
| Diversity of the board. The board consists of representatives from the NGO sector, community, government and private sector.  | /2             |                |
| The board consists of more than 50% of external membership.   | /2             |                |
| The board reflects diversity in terms of technical, community engagement, management, fundraising, financial and legal skills that correspond to the business the NGO.  | /2             |                |
| <b>Sub-total</b>  | <b>/10</b>     |                |
| <b>How to assign scores</b> <ul style="list-style-type: none"> <li>• Insert a score in each column. Where the organisation does not meet the specified criteria, assign a zero (0). Where the organisation partially meets the assessment criteria, where appropriate and at the discretion of the assessor, assign a score of between four (4) and zero point five (0.5).</li> <li>• Transfer the sub-total of the score attained under Appraisal Diagram 1.4 to the appropriate block in Appraisal Form 1.</li> </ul> |                |                |

## **Extent to which principles of good governance are practiced**

NGOs have the responsibility to think about governance practices. Good governance established at the outset encourages organisational stability and balanced decision-making.

Good governance consists of a number of characteristics, which forms the core of the next appraisal diagram. According to Van der Waldt (2004:10-11), these characteristics are: participation, rule-of-law, transparency, responsiveness, consensus-orientated, equity and inclusiveness, effectiveness and efficiency and accountability.

According to Van der Waldt (2004:10-11), participation within an NGO context can be direct, where staff provides feedback on the formulation and implementation of organisational policies. Furthermore, good governance requires fair organisational policy frameworks that are enforced impartially. Transparency, in turn, implies that decisions are made and are enforced according to rules and regulations. Information pertaining to the organisation should be made available and be directly accessible to stakeholders. Responsiveness requires that the organisation serves all parties (internal and external to the organisation) fairly and within an appropriate timeframe. Consensus-orientated decision-making requires that the organisation recognises community needs. Accordingly, broad and long-term perspectives should be formulated on how to address these needs and attain sustainable human development. Equity is paramount in the appointment of human resources and when services and resources are acquired externally. When it comes to accountability, civil society organisations must be accountable to the public and to their respective institutional stakeholders.

In line with the above assertions around good governance, Appraisal Diagram 1.5 has been devised.

## **Sources of NGO funding**

NGOs have generally been able to raise revenue through a variety of sources. Before 1994, South African NGOs had a multitude of funding options. The arrival of democracy saw the redirecting of funding away from NGOs to a new legitimate democratic government. Organisations such as the National Funding Agency (NDA), the National Lottery and the Umsobomvu Youth Fund were created in an attempt by government to fill the funding gap. These organisations operated with little success. As they were accustomed to traditional sources of funding, NGOs struggled to diversify their funding base (Camay and Gordon 2004: 57-97; Farouk 2002b:1).

## Appraisal Diagram 1.5

| GOVERNANCE APPRAISAL   |                |                |
|--|----------------|----------------|
| THE EXTENT TO WHICH PRINCIPLES OF GOOD GOVERNANCE ARE PRACTICED<br>Appraisal criteria  | Possible Score | Score Assigned |
| <p>ALL of the following characteristics of good governance are present within the organisation.</p> <ul style="list-style-type: none"> <li>• Staff participation in policy formulation and implementation.</li> <li>• Transparency of decisions by management.</li> <li>• Responsiveness to clients.</li> <li>• Consensus-oriented decision-making.</li> <li>• Equity with regard to human resource appointments.</li> <li>• Equity with regard to the procurement of external services and resources.</li> <li>• Effectiveness and efficiency in responding to client needs.</li> <li>• Accountability to stakeholders.</li> <li>• Legal frameworks are enforced impartially.</li> </ul> <p><i>(Hendrickse 2008: 62-67)</i></p> | /1             |                |
| Staff participation, where staff comments on the practicality of implementing policy frameworks.   | /1             |                |
| Transparency of decisions by management.   | /1             |                |
| The organisation's responsiveness to clients.  | /1             |                |
| Consensus-oriented decision-making.  | /1             |                |
| Equity with regard to human resource appointments.   | /1             |                |
| Equity with regard to the procurement of external services and resources.  | /1             |                |
| Effectiveness and efficiency in responding to client needs.  | /1             |                |
| Accountability to stakeholders.  | /1             |                |
| Legal frameworks are enforced impartially.   | /1             |                |
| <b>Sub-total</b>   | <b>/10</b>     |                |
| <p><b>How to assign a score</b></p> <ul style="list-style-type: none"> <li>• Insert a score in each column. Where the organisation does not meet the specified criteria, assign a zero (0). Where the organisation partially meets the assessment criteria, where appropriate and at the discretion of the assessor, assign a score of between one (1) and zero point five (0.5).</li> <li>• Transfer sub-total of score attained under Appraisal Diagram 1.5 to the appropriate block in Appraisal Form 1.</li> </ul>   |                |                |

Therefore, the challenge for South African NGOs is to devise a sustainable framework to attain financial resources. Within this context, the following assessment criteria become imperative.

### Appraisal Diagram 1.6

| <b>FINANCIAL SUSTAINABILITY</b>   |                           |                           |
|---|---------------------------|---------------------------|
| <b>SOURCE OF NGO FUNDING<br/>Assessment Criteria</b>  | <b>Possible<br/>Score</b> | <b>Score<br/>Assigned</b> |
| The organisation has multiple funding sources that may include Government, the private sector, other donors or several from the same category.  | /1                        |                           |
| The organisation receives funding from international foreign aid grants.  | /1                        |                           |
| The organisation receives funding from national/local Government grants.  | /1                        |                           |
| The organisation receives funding from bilateral and multilateral grant aid.  | /1                        |                           |
| The organisation receives funding from international foundation grants.   | /1                        |                           |
| The organisation receives funding from national/local foundation grants.  | /1                        |                           |
| The organisation receives funding from international, national and local corporate grants.  | /1                        |                           |
| The organisation receives funding from international charitable donations.  | /1                        |                           |
| The organisation receives funding from local individual donations.  | /1                        |                           |
| The organisation receives funding from internal self-financing strategies.  | /1                        |                           |
| <b>Sub-total</b>  | <b>/10</b>                |                           |
| <p><b>How to assign a score:</b></p> <ul style="list-style-type: none"> <li>• Insert a score in each column. Where the organisation does not meet the specified criteria, assign a zero (0). Where the organisation partially meets the assessment criteria, where appropriate and at the discretion of the assessor, assign a score of between one (1) and zero point five (0.5).</li> <li>• Transfer sub-total of score attained under Appraisal Diagram 1.6 to the appropriate block in Appraisal Form 1.</li> </ul> |                           |                           |

## Self-financing strategies

Self-financing is an alternative to the more traditional fundraising approaches non-profit organisations use. Donor agencies such as Agro Action, Enterprise Works Worldwide, the Roberts Enterprise Development Fund, the Aspen Institute and a number of other private foundations encourage NGO self-financing initiatives (Viravaidya and Hayssen 2001:4). A number of self-financing methods or strategies exist that NGOs could use to sustain themselves. These include fees-for-services, various loans and credit arrangements, membership fees and product sales (Viravaidya and Hayssen 2001:4-8).

Williams (2008) warns that South African NPOs should not generate more than 25% of their income from “service provision” in which they compete with the private sector for contracts<sup>4</sup>. TRAC, a non-profit organisation of which Williams is a director, reports in their fundraising proposal<sup>5</sup> that, in an attempt to develop capital reserves, a percentage of the income derived from the contract work. In these instances TRAC-MP undertakes contract work on behalf of the government, higher education institutions or the private sector and income is accrued to a capital reserve fund. Williams (2008) suggests that it is important for an NGO to build up capital reserves – particularly where delays in donor contributions may cripple the organisation financially.

However, contrary to Williams’ warnings, it is the researcher’s view that South African NGOs should be allowed to generate 50% of their own income. In line with this proposition, assessment criteria have been devised. See Appraisal Diagram 1.7.

The reader is cautioned that self-financing strategies may differ from country-to-country and even between different communities (Academy for Educational Development 2004).

Appraisal Diagram 1.7 has been developed to assess the presence of self-financing strategies within an NGO.

## Good practice in financial management

For NGOs to survive in a changing and competitive environment, managers need to develop the necessary understanding and confidence to make full use of financial information. While there is no single financial model that suits all NGOs, good practice in financial management is achieved by designing appropriate systems and procedures.

Organisations should be committed to practicing good governance and should in every instance adhere to the recommendations of the King Commission Report. A NGO’s management of funds should comply with the highest professional and ethical standards. Importantly, sound financial systems

## Appraisal Diagram 1.7

| FINANCIAL SUSTAINABILITY   |                   |                   |
|--|-------------------|-------------------|
| SELF-FINANCING STRATEGIES<br>Assessment Criteria   | Possible<br>Score | Score<br>Assigned |
| Self-financing strategies or methods are present and in use within the organisation.   | /5                |                   |
| Not more than 50% of the organisation's overall income is generated through: <ul style="list-style-type: none"> <li>• Membership fees</li> <li>• Fees for services</li> <li>• Product sales</li> <li>• Use of hard assets, for example, equipment rental</li> <li>• Use of soft assets, for example, patents, copyrights</li> <li>• Ancillary business ventures</li> <li>• Investment dividends</li> <li>• Gift of time (time spent by volunteers)</li> <li>• Gift of product (donations given by the public)</li> </ul> | /3                |                   |
| The organisation has capital reserves to be used at the board's discretion.  | /2                |                   |
| <b>Sub-total</b>   | <b>/10</b>        |                   |
| <p><b>How to assign a score</b></p> <ul style="list-style-type: none"> <li>• Insert a score in each column. Where the organisation does not meet the specified criteria, assign a zero (0). Where the organisation partially meets the assessment criteria, where appropriate and at the discretion of the assessor, assign a score of between five (5) and zero point five (0.5).</li> <li>• Transfer sub-total of score attained under Appraisal Diagram 1.7 to the appropriate block in Appraisal Form 1.</li> </ul>  |                   |                   |

should be in place. This will help ensure donor partners that their funding contributions are being managed and expended in an appropriate fashion within the NGO. In accordance with South African statutes, local NGOs should have their financial year-end in March. Audits should be conducted in an appropriate period of time. Furthermore, reports to donor agencies are presented based on respective agreements either quarterly, every six months, biannually or annually<sup>6</sup>.

Authors such as Narayan, Godden, Reid and Ortega (2000:3-5), Ott (2001) and Alin *et al.* (2006) have written extensively on good practice in financial management. The following assessment criterion has been devised within the context of the above discussion.

## Appraisal Diagram 1.8

| FINANCIAL SUSTAINABILITY   |                   |                   |
|--|-------------------|-------------------|
| GOOD PRACTICE IN FINANCIAL MANAGEMENT<br>Assessment Criteria   | Possible<br>Score | Score<br>Assigned |
| In terms of good practice in financial management, the organisation:<br>• Keeps an accurate record of all financial transactions ( <b>accounting records</b> ).  | /2                |                   |
| In terms of good practice in financial management, the organisation:<br>• Links the budget to its strategic and operational plan ( <b>financial planning</b> ).  | /2                |                   |
| In terms of good practice in financial management, the organisation:<br>• Produces management accounts, so that managers can compare the organisation's progress against the budget and then make decisions about the future ( <b>financial monitoring</b> ).<br>• Produces financial statements for outside scrutiny to demonstrate how funds have been applied in the past ( <b>financial monitoring</b> ).  | /2                |                   |
| In terms of good practice in financial management, the organisation:<br>• Has internal controls (checks and balances) in place to safeguard its assets and manage risk ( <b>internal controls</b> ).   | /2                |                   |
| In terms of good practice in financial management, the organisation:<br>• Has an audit committee/auditor to assist in the quality and reliability of financial and other performance information issued.   | /2                |                   |
| <b>Sub-total</b>   | <b>/10</b>        |                   |
| <p><b>How to assign a score</b></p> <ul style="list-style-type: none"> <li>• Insert a score in each column. Where the organisation does not meet the specified criteria, assign a zero (0). Where the organisation partially meets the assessment criteria, where appropriate and at the discretion of the assessor, assign a score of between two (2) and zero point five (0.5).</li> <li>• Transfer sub-total of score attained under Appraisal Diagram 1.8 to the appropriate block in Appraisal Form 1.</li> </ul> |                   |                   |

## Financial control

Financial control<sup>7</sup> is at the heart of financial management. Effective financial accounting and managerial control practices are as important to NGOs as they are to the private sector. Without properly executed financial control, the organisation's assets and resources are at risk, funds may not be spent in accordance with the organisation's strategic objectives or funders' wishes. Furthermore, managers' competence and the NGO's integrity may be called into question (Alin *et al.* 2006, Herzlinger and Nitterhouse 2001).

Designing systems and procedures to suit the particular needs of the NGO enforce financial control. Accordingly, an overall financial policy should be formulated and implemented that pertains to donors, income, budgeting, expenditure, travel, auditing, petty cash, assets, salaries, staff loans and the opening and operation of bank accounts (Shapiro n.d.).

One of the major responsibilities of a board of directors is to establish fiscal policies that protect the organisation from either intentional or unintentional misuse of funds. The board must decide how money will be handled internally to ensure that it is received, recorded, deposited and expended safely and in a manner that seems appropriate. For example, tasks such as receiving cash, preparing financial statements and the expenditure of funds should be assigned to two staff members to ensure adequate financial control. Other forms of control relates to rules around monitoring and amending budgets, writing out cheques, receiving money and insurance around financial losses (Wolf 2001).

For NGOs to survive in a changing and competitive environment, managers need to develop the necessary understanding and confidence to make full use of financial information. While there is no finance system model that suits all NGOs, good practice in financial management is achieved by designing systems and procedures around:

- *Accounting records:*  
Every organisation must keep an accurate record of all financial transactions that take place, so that it can show how the funds have been used. This is referred to as the financial accounting function.
- *Financial planning:*  
The budget is linked to the organisation's strategic and operational plans. Therefore, it forms the cornerstone of any financial management system and plays an integral part in monitoring the use of funds.
- *Financial monitoring:*  
Management accounts are internal reports produced so that managers can compare the organisation's progress against the budget and then make decisions about the future. Financial statements are produced periodically for outside scrutiny to demonstrate how funds have been applied in the past.
- *Internal controls:*  
Controls, checks and balances, collectively referred to as internal controls, are put in place to safeguard an organisation's assets and manage risk. Their purpose is to deter opportunistic theft or fraud and to detect errors and omissions in the accounting records. An effective internal control system serves to value and protect those who are responsible for handling the financial affairs of the organisation.

(Wolf 2001, Alin *et al.* 2006)

The following assessment criteria have been formulated to test the above assertions.

**Appraisal Diagram 1.9**

| <b>FINANCIAL SUSTAINABILITY</b>  |                           |                           |
|--|---------------------------|---------------------------|
| <b>FINANCIAL CONTROL<br/>Assessment Criteria</b>   | <b>Possible<br/>Score</b> | <b>Score<br/>Assigned</b> |
| The organisation has fiscal policies that protect it from intentional or unintentional misuse of resources.  | /1                        |                           |
| Financial policy and implementation of procedures and systems relevant to South African company and tax law are in place. The policy also recognises the financial reporting requirements of donors/funders.   | /1                        |                           |
| Financial policy exists around staff salaries, staff loans and opening and operating bank accounts. Implementation procedures and systems around this policy are in place within the organisation  | /1                        |                           |
| Financial policy exists around how money is received and recorded. Implementation procedures and systems pertaining to this policy are in place.   | /1                        |                           |
| Financial policy, implementation procedures and systems exist around how money is spent.   | /1                        |                           |
| Tasks such as receiving cash, preparing financial statements and the expenditure of funds are assigned to more than one staff member to ensure adequate financial control.   | /1                        |                           |
| Rules exist around how the budget should be monitored and amended.   | /1                        |                           |
| Rules exist around writing out cheques.  | /1                        |                           |
| The organisation has insurance in place to cover financial losses.   | /1                        |                           |
| Auditing procedures are in place.  | /1                        |                           |
| <b>Sub-total</b>   | <b>/10</b>                |                           |
| <p><b>How to assign a score</b></p> <ul style="list-style-type: none"> <li>• Insert a score in each column. Where the organisation does not meet the specified criteria, assign a zero (0). Where the organisation partially meets the assessment criteria, where appropriate and at the discretion of the assessor, assign a score of between one (1) and zero point five (0.5).</li> <li>• Transfer sub-total of score attained under Appraisal Diagram 1.9 to the appropriate block in Appraisal Form 1.</li> </ul> |                           |                           |

## Fundraising strategies

Fundraising is proactive and should be conceptualised and designed as a long-range programme. Very few NGOs have dedicated professional fundraising human resource capacity and a coherent fundraising strategy. Building NGO fundraising capacity requires developing a fundraising policy and regulations. Furthermore, a fundraising committee with clear job descriptions and mechanisms should monitor fundraising activities (Kraak 2001, Alin *et al.* 2006). Williams (2008) notes that externally appointed fundraisers require a commission on the funds they raise on behalf of organisations. Many donors may refuse to pay such commissions. The latter commentator contends that, in many instances, funders may argue that if the NGO does not even have the internal capacity to draft a funding proposal, they may also lack the capacity to manage the organisation's financial resources. It is the researcher's view that a fundraiser is essential within an NGO. The cost to the organisation of such an incumbent should be recovered from the administrative categories of budgets of individual projects or programmes. All donor agencies have a limit to their resources and have to make decisions around what they are prepared to fund. Once a funder has decided what type of activities/programmes it plans to fund, a relationship begins to develop between the receiver-of-funding and the donor. Donor agencies emphasise the fact that this is a mutually beneficial relationship and both parties aware of the other's expectations (Ndlovu 2004). The researcher contends that the funding agency still holds the dominant power in this relationship, which inevitably proves uneven.

A well-executed fundraising strategy remains imperative within organisations and, as such, the assessment criteria in Appraisal Diagram 1.10 have been devised.

## FRAMEWORK APPLICATION GUIDELINES

The following section will forward a discussion on the structure and content of the appraisal framework. It looks at how documentation should be assimilated, who should appraise and how final scores should be calculated.

### Structure and content of the appraisal framework

This appraisal framework consists of 10 assessment criteria. Each criterion is intended to capture a separate dimension of governance and financial sustainability, as informed by theoretical and empirical evidence.

The scope and purpose of this appraisal instrument is to provide a framework for assessing the governance and financial sustainability of NGOs, as alluded to earlier in the article.

## Appraisal Diagram 1.10

| FINANCIAL SUSTAINABILITY  |                   |                   |
|---|-------------------|-------------------|
| FUNDRAISING STRATEGY<br>Assessment Criteria   | Possible<br>Score | Score<br>Attained |
| The organisation has a well-executed fundraising strategy that contains ALL of the following elements present in this diagram.  | /2                |                   |
| Diversification: Diversified fundraising means that an NGO has several sources of funding from several different types of fundraising activities.   | /2                |                   |
| Sustainability: This relates to developing self-reliance. The more self-reliant a NGO is, the more control it can maintain over its resources, as well as the decisions around resource management and use.   | /2                |                   |
| Creativity: Being creative means utilising available resources and taking advantage of opportunities as they emerge.  | /2                |                   |
| Inclusiveness: Taking an inclusive approach means finding a role for supportive people to play. In this way, the boundaries of the NGO will be expanded beyond its present scope.   | /2                |                   |
| <b>Sub-total</b>  | <b>/10</b>        |                   |
| <p><b>How to assign a score</b></p> <ul style="list-style-type: none"> <li>• Insert a score in each column. Where the organisation does not meet the specified criteria, assign a zero (0). Where the organisation partially meets the assessment criteria, where appropriate and at the discretion of the assessor, assign a score of between two (2) and zero point five (0.5).</li> <li>• Transfer sub-total of score attained under Appraisal Diagram 1.10 to the appropriate block in Appraisal Form 1.</li> </ul> |                   |                   |

## Documentation/Information

The assessor should attempt to identify all information pertaining to the organisation before starting the appraisal exercise. Information can be collated through consulting, for example, the organisation’s annual reports and other relevant documentation, or through site visits, interviews, questionnaires and focus groups.

## Who should appraise

It is recommended that an assessor with experience in the area of NGOs facilitate the appraisal instrument, in order to increase the reliability of the assessment outcomes. A moderator may assist the assessor. Furthermore, focus groups can be utilised to deliberate the outcomes of the appraisal exercise.

## **Score scale/overall assessment**

A cumulative scoring system has been devised. Each item within the assessment criteria has been awarded a possible score. The assigned score measures the extent to which a criterion has been fulfilled.

- If the assessor is confident that the criterion has been fully met, then the full possible score can be assigned.
- If the assessor is confident that the criterion has partially been fulfilled, a portion of the possible score may be assigned at the discretion of the assessor. However, if a possible score equals one, a score of zero (0) may be assigned at the discretion of the assessor.
- If the assessor is sure that a criterion has not been fulfilled, due to a lack of corroborating evidence, a score of zero (0) may be assigned.
- Sub-totals attained in each appraisal diagram should be transferred to Appraisal Form 1, where after a final score and a percentage score should be calculated.
- The percentage score should be compared to the Sustainability Indicator presented earlier in the article.

The next section will highlight the limitations of the appraisal instrument.

## **LIMITATIONS OF THE APPRAISAL INSTRUMENT**

The success and the sustainability of a particular NGO sector depend on its ability to deliver and meet the expectations of its constituency, and to retain credibility in the eyes of that constituency. This particular instrument is not results-orientated. This implies that it does not measure output or outcomes of a particular NGO, CSO or CBO. Only an assessor who is regarded as an expert in the institutional, financial and governance matters of NGOs can apply the appraisal framework.

This appraisal framework has been specifically developed for the South African context and should be revised as the economic, social, political and technological conditions of the country changes. Therefore, it is not necessarily applicable to NGOs in other developing countries in Eastern Europe or East Asia, for example.

The appraisal criteria could be revised in the future should a researcher find evidence of alternative criteria that are more applicable to the sustainability of NGOs. Assessment categories forwarded within the appraisal diagrams may also require refinement should the need arise in the future. This study attempted to develop (and test) an appraisal framework for NGOs. However,

it is recommended that research agencies may further develop this framework and test the instrument more comprehensively, so that researchers may further refine the specific categories and considerations for its measurement.

## CONCLUSION

South African NGOs undeniably have a critical role to play in providing welfare, basic and other services to individuals that were disadvantaged by the previous socio-political system. Therefore, the challenge is to create an environment in which NGOs can flourish.

In conclusion, this article has provided an opportunity to develop an appraisal framework for the sustainability of NGOs. It is the researcher's view that this appraisal framework will help create a sustainable South African NGO sector. It will prove invaluable to all stakeholders dealing with NGOs, CBOs, CSOs and non-profit organisations, testing the organisation's long-term prospects for sustainability.

## NOTES

- 1 Christopher John Williams, director: TRAC, joined TRAC-MP in 2000 after working at the DLA Provincial Office. Chris holds a BA, Honours and MSC in Development Planning and provides overall management, leadership and strategic support to TRAC-MP's programme activities. Also see <http://www.trac.org.za/context/About-US.asp>
- 2 Williams, as noted earlier, has extensive experience in NGO governance. The National Director of the Harold Wolpe Memorial Trust supports this notion.
- 3 The National Director, Harold Wolpe Memorial Trust (2008) See the writings of Loukas Spanos (2005) on governing boards in the Greek context.
- 4 A developmental theorist, who wants to remain anonymous, contends that an NGO should be allowed to generate 50% of its funding from self-financing strategies. In this way, the commentator argues, NGOs will be less dependent on funding from external sources, particularly in instances where terms and conditions are attached to the funds.
- 5 See <http://www.trac.org.za/content/Fund-Raising.asp>
- 6 See <http://www.trac.org.za/content/Fund-Raising.asp> Allan Roman, an NGO financial management expert, interviewed in May 2008, concurred with a number of the views expressed by Williams, 2008.
- 7 Allan Roman, a financial expert, asserts that, not only is the existence of financial policies in NGOs extremely crucial, he contends that the implementation and the monitoring of these policies are even more imperative. He argues that, in this way, the organisation's financial resources will be protected.

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## **AUTHORS CONTACT DETAILS**

Dr Rozenda Hendrickse  
Senior Lecturer  
Department of Public Management  
Cape Peninsula University of Technology  
P O Box 652  
Cape Town  
8000  
Tel: 021 460 3929  
Cell: 083 744 1629  
hendrickser@cput.ac.za