

WHAT MAKES A GOOD CHARITY?

NPC's guide to charity analysis

Ruth Gripper and Iona Joy September 2016

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FOREWORD

NPC's mission is to transform the charity sector, and encouraging good charity analysis is one of the key ways we achieve this. Carrying out this kind of analysis allows funders to better understand where to put their money and time to achieve maximum impact. It also helps charities themselves improve and so deliver more of the social and other outcomes that they are set up to achieve.

We published our first guide to analysing charities in 2010 and <u>The little blue book</u>¹ has proved popular ever since.¹ We shared our approach to support a greater focus on effectiveness in the charity sector and to allow others to make use of our framework.

Since then, the environment for charities has changed: we have seen the growth of new forms of finance; the shift, for many charities, from grant funding to contract delivery; ongoing demographic and societal changes; digital technology opening up new possibilities; and charities' public benefit no longer being taken as read. Recent scandals and problems have brought a renewed focus on governance. What it takes to be effective as a charity in this environment has evolved; that evolution is reflected in this guide.

NPC's thinking on many topics has also developed. We place a greater emphasis on the involvement of people using the charity, as well as on organisational culture, in supporting effectiveness. The need for organisations to be able to adapt and respond to change is greater. In our recent work we have explored how successful charities are embracing digital technology and the idea of 'systems change' as a way to tackle the root causes of complex problems. These ideas, too, have informed the development of this new guide.

This latest publication brings new insights gained through our 15 years of experience working with hundreds of charities and funders, and what we have learned about the way people have used our original guidance. We hope it will help to support effectiveness in the charity sector—a sector that, at its best, is bold, ambitious and forward-looking in making a lasting difference to people's lives and the world we live in.

Dan Corry

Chief Executive, NPC

INTRODUCTION

Why do charity analysis?

Charity analysis is central to NPC's work. It underpins our advice to charities and funders, and informs our research and our responses to topical issues in the charity sector.

We believe that analysis can help charities to improve. It can help funders to identify charities' strengths and weaknesses, and make decisions about how to allocate resources. It can help charities to assess their own performance and make improvements to their organisation.

This guide sets out clearly our approach, focusing on the key characteristics we believe are common to all good charities.

Spotlight on... improvement

We hope this guide will be used to support improvement in the sector—both by charities themselves and by those who fund them. All organisations have areas of strength and weakness. Charity leaders can use our framework to identify these areas and decide where to focus their efforts or seek external support. Funders can also play a role in supporting charities as they seek to improve. Just ceasing support in times of difficulty can unnecessarily exacerbate problems when appropriate financial or other support could be part of an effective solution.

Who is this guide for?

This guide is for anyone interested in helping charities to become better. We want it to help anyone reflecting on the effectiveness of a charity—on its areas of strength and weakness—to be as successful as possible in their efforts.

- If you are a funder or philanthropist, it can help inform your decisions about where to provide financial support and where those charities you work with may need extra help.
- If you are involved in a charity, it provides a framework to review organisational strengths and identify areas for improvement.
- If you have an interest in the charity sector, it explains where to look for information and how to make your own judgement about a charity's effectiveness.

By using a framework that can be applied to different organisations, regardless of their particular goals, this guide allows readers to review effectiveness across the charity sector. It can be applied (with some tailoring—see **page 60**) to any organisation regardless of its size, model, geography, sector and even whether it operates in the UK or overseas.

For ease, throughout this guide we use the following terms as shorthand:

- 'sector' or 'charity sector' refers to the whole voluntary, charity and social enterprise sector.
- · 'charity' or 'charities' means any organisation working in this sector.

How to use this guide

We begin by setting out what you need before you start: some key principles and sources of information. We then introduce the analysis framework, covering four areas:

- 1. Purpose
- Impact practice
- 3. People; and
- Finance and operations.

For each area we set out why it is so important, the key questions in that area, and what to look for in order to reach a judgement about the charity's effectiveness.

Throughout the guide we refer to real examples to illustrate particular points. These are not organisations we have analysed in depth and their inclusion does not constitute due diligence. We hope, however, that they help to bring some of the ideas to life.

An assessment grid on page 55 summarises our approach. It provides an idea of what 'good' looks like for each area, as well as indications for when a charity is operating below expectations. We have found this to be a useful tool to give an overall picture of a charity. If returned to over time, it can also demonstrate where a charity has made progress.

We also include a blank assessment grid on **page 64** so you can easily fill in your notes as you work through the guide. A separate template is also available to download from NPC's website so you can print more copies as you need them.

GETTING STARTED

Take a proportionate approach

Charity analysis is like the proverbial piece of string—it can take as long or as short a time as you have available. Large or complex organisations require more time; smaller or simpler ones require less. It is worth investing time to do analysis properly.

The golden rule is to be reasonable and proportionate. If analysing your own organisation, it is up to you how much detail is appropriate. You could even take a gradual approach rather than trying to deal with every aspect in one go—returning to it over time can also be useful to show progress in different areas.

For funders, use existing information as far as possible, and minimise requests for tailored information. We recommend more detailed analysis when bigger sums of money are involved. Much of the information to be discussed is confidential—it is unreasonable to expect a charity to share this unless you are thinking of making a substantial donation. For any grant under £5,000, avoid using the charity's time unless you can genuinely add value. For a grant of £50,000, on the other hand, it is sensible to ask questions and to meet people to ensure the charity can manage the grant well. Remember that the stakes for the charity may be high and this process can be stressful: being open about the scale of the potential investment and the charity's chances of success (for example, if you are looking at several other organisations) will ensure that everyone knows where they stand.

Where time is limited, there are short cuts available. You should always start with basic desk research. Talking to other funders who have worked with the charity, or other charities who have come across them in the field, can provide valuable insight too. The involvement and active endorsement of credible experts and charity peers (politicians and celebrities do not count!) can also be a sign of a charity that is doing good work.

Tailor your approach

The principles set out in this guide apply to all charities—however, the sector is diverse and you will need to tailor expectations and approach to the size, maturity and complexity of an organisation and the nature of its work. For example, campaigning organisations, local community groups and charities working overseas have varying characteristics and working environments—as do social enterprises, which can be any of these. We provide further advice on how to tailor your approach on page <u>60</u>.

Understand the context

Organisations exist within a context. Without understanding this context, it is hard to know if assumptions about the future are realistic, or if the organisation is duplicating work done effectively elsewhere. Building up expertise in an area is helpful, but not always possible. NPC's team includes specialists, and when analysing charities we also often speak to others with knowledge of the charity in question or the wider issue and sector. Many sector-specific umbrella bodies publish useful briefings that can help to inform your analysis.

The importance of judgement

Analysing a charity is an art as well as a science. This guide sets out a structured approach. However, applying it requires judgement and relies on the skills, opinions and instincts of the person doing it, all of which develop with time and experience. The conclusions are therefore a mixture of objective assessment and subjective opinion.

Information sources and advice

For funders:

- Use publicly available information. Look at the annual report and accounts filed with the <u>Charity Commission</u>, and any other information that the charity publishes on its website, such as vision statement, strategy documents and evaluation reports. The level of information publicly available is an indicator of the charity's transparency. Recent press reports and biographical information for key staff available online will add to the picture.
- Request information that is not publicly available (if appropriate). This might include management accounts, internal strategy and evaluation documents. Note these documents are sensitive, and organisations may not be willing to share them.
- Meet with key people at the charity if possible. In particular the chief executive, chair of trustees and members of the management team. Remember to be proportionate—don't expect time with the chief executive of a £5m charity if you are thinking of making a £5,000 donation. A £50,000 donation, however, would warrant a visit and detailed answers to questions.
- Talk to people who use or have recently used the charity. They will be able to speak from first-hand experience about the quality and impact of the charity's work. Other individuals and organisations that have worked with the charity—such as funders, commissioners and other charities—will also have gained an impression of the organisation's efficiency and responsiveness.
- Visit a project and talk to front-line staff and volunteers. This can give you a feel for the organisation and check whether the literature tallies with what happens on the ground. Be aware that the charity is likely to 'put on its best face' for your visit. We have, when appropriate, 'mystery shopped' (eg, by visiting a project that's open to the public) and learned a great deal. Ask yourself how accessible is it, how welcoming, how busy?

For charities:

- Think about your aims. What do you want to get out of the review? How will you use your conclusions, and how much time do you want to invest in the process?
- **Consider what information you have to hand (use the list opposite)**. You may want to think separately about what the publicly available information says about your organisation. Are you being sufficiently transparent?
- **Try to put on an 'outsider hat'.** If you were not connected to the charity, how would you answer the questions set out in this guide?
- **Seek out third-party perspectives.** Those who have used, commissioned, funded or otherwise worked with your charity.
- **Be realistic about timing.** You may want to take each area in turn rather than attempt to cover everything in one go.
- **Preparation is key.** For example, if you are bringing your board or management team together to discuss an area, make sure the conversation has structure and everyone has advance sight of relevant information.
- **Trustees have a balance to strike.** While the board should be fully acquainted with the charity and key information, it is there to serve the charity—not the other way round. So supportive information requests made with the workload of staff in mind will be more helpful than demands for more information than is needed.

NPC'S CHARITY ANALYSIS FRAMEWORK

We split our analysis of what makes a good charity into four areas: purpose, impact practice, people, and finance and operations. Within each of these areas there are a number of key questions to consider, which we cover in turn in the following sections. There is no hierarchy—it is essential to consider each area of the framework. These areas need to work together for the charity to be as effective as possible.

For example, a charity with good impact practice is more likely to have a good strategy that achieves results. This in turn can attract good people and keep them motivated, while good leadership, staff and governance underpins results and will ensure good financial and operational management. Similarly, weakness in one area can limit or undermine achievements in another. When things are working well, the different areas are mutually reinforcing, contributing to greater effectiveness overall.

1. PURPOSE

- Does the charity's vision and mission answer a need?
- Does the charity have a good strategy for achieving its goals?
- Do the charity's activities reflect the strategy?
- Does the charity achieve results?

2. IMPACT PRACTICE

- Does the charity use information to learn and improve?
- · Does the charity know what it is achieving?
- Does the charity have the right approach to evaluation?
- Is the charity open about its findings?

3. PEOPLE

- Does the charity have good leadership?
- Does the charity recruit good people and manage them well?
- How good is the charity's governance?
- Do people using the charity help to shape its work?
- Does the charity have a healthy organisational culture?

4. FINANCE AND OPERATIONS

- Is the charity financially secure?
- Does the charity have good financial management?
- Does the charity have good operational management?
- Does the charity make efficient use of all its resources?







ANALYSIS | 1. PURPOSE | 2. IMPACT | 3. PEOPLE | 4. FINANCE & ASSESSMENT FRAMEWORK | PRACTICE | OPERATIONS | GRID



The starting point when looking at any charity is to understand how it wants to change the world. A charity is defined by its social purpose—regardless of how big it is, or what area it is working in, it will be seeking to achieve some kind of change.

For some, such as heritage or nature organisations, this 'change' may involve preserving something or preventing unwanted change from happening. For others, such as campaigners for social justice, it may be about changing attitudes, policy or legislation.

Does the charity's vision and mission answer a need?

Every charity has a vision of how it wants the world to be. A charity's mission is the change the charity wants to make in contributing to this vision, and it drives the charity's actions. This may appear so obvious that it is not worth stating, but there are often practical tensions between organisational and mission interests. Everything the charity does should follow from, and be aligned with its mission—including its brand, communications and culture.

The most effective organisations use data and the views of those affected to remain informed about the issue or issues they are seeking to address. They are also aware of how other organisations are responding so they can judge where they can make the greatest difference. This is an ongoing process: if changes in the external environment affect the charity's work, or people's needs or interests change, the charity will need to adapt its response—perhaps stopping some activities or starting new ones, or working with different partners.

Spotlight on... Theory of change

A **theory of change** can be a helpful way to plan how to create change.² It can help to identify activities that are irrelevant, or areas where collaboration is required to achieve a goal. A good theory of change:

- · Is clear about who the organisation aims to reach, their needs, characteristics and the wider context: It should be clear about the long-term impact the charity wants to achieve and the shorter-term outcomes that will contribute to impact, and how the charity's work will affect these outcomes.
- Is informed by academic theory and research: The assumptions that underpin the theory of change should be clear, as should potential negative consequences and external factors that might be influential.
- Will have been co-created, with input from across the organisation: Staff, trustees, volunteers and those using the charity. Everyone should understand and work towards the theory of change, which should be published and disseminated.
- Gives people confidence that the charity understands what it is trying to achieve and how it will do this: It demonstrates that the charity is aligned with the latest thinking around what works in tackling the particular social or environmental issue.

A theory of change is often presented as a diagram, but it doesn't have to be a diagram at all. The crucial aspect is that the underlying thinking about the links between the charity's activities, outcomes and ultimate goal is sound.

The Combined Homelessness and Information Network (CHAIN) is a multiagency database, managed by the homelessness charity St Mungo's, which records information about rough sleepers and the wider homeless population in London. This provides a detailed picture of rough sleeping in the capital, allowing charities, policymakers, commissioners and other agencies to identify needs and the issues and complexities driving this need, which then informs decisions.

Making an impact often requires ambition and the courage to take risks—whether that is trying out a new approach, standing up for an unpopular cause, or making difficult choices about where to focus. Trustees and managers who look beyond the concerns of their organisation to its wider purpose will achieve the greatest impact. For example, they will ask whether collective and collaborative action may achieve more than individual action, and whether the charity is best placed to achieve its mission. They will regularly review alternatives, such as changing the organisation's activities, merging with another organisation or even winding up, even though this is difficult.

In 2013 the charities **Breast Cancer Campaign** and **Breakthrough Breast Cancer** realised their new five-year strategies had very similar goals, ambitions and approaches to tackling them. The leadership teams at both charities therefore decided to merge. This led to a number of difficult decisions, including a 25% reduction in staff. However, the resulting organisation **Breast Cancer Now** seems better equipped to meet its unifying ambition: namely, to stop women dying of breast cancer by 2050.

Ambitious charities look to achieve long-term change and tackle root causes rather than simply treating symptoms. Some charities are starting to take a 'systems change' approach—aiming to bring about lasting change by altering underlying structures and supporting mechanisms (such as policies, relationships or power structures) that make the system operate in a particular way.³

- Does the charity have a clear purpose and approach, based on evidence about the issue it seeks to address?
- Does it understand its own role and how it relates to others?
- Is it best placed to do what it does? Has it reviewed the possibilities of partnership, collaboration and merger?
- · Is it looking to solve problems or treat symptoms?

Does the charity have a good strategy for achieving its goals?

A charity's mission is long-standing, whereas strategy develops and adapts to changing circumstances. The strategy sets the direction of travel for an organisation and provides a framework for making decisions. A well-presented strategy can also be helpful in communicating to stakeholders how the charity plans to achieve its aims.

The strategy should set out why the organisation does what it does and how its activities make an impact on the problem it seeks to address, based on evidence and clear logic (theory of change can be helpful—see page 15). This might be straightforward for a small charity with a single activity, but it can be more complex for charities with multiple activities or those aiming for long-term cultural change. Strategy should be reviewed at regular intervals and approved by the board.

Spotlight on... Strategy development

Strategy development sits within a wider process of organisational learning. There is no onesize-fits-all approach, but we have developed a framework to help charities think through the strategy process. This includes our **strategy** triangle, which brings together a number of different models and frameworks.⁴



While the strategic questions will vary, the best strategies address all three corners of the triangle: the charity's core purpose, its external environment and its internal capabilities. It includes an appreciation of the distinctive role of the charity and an understanding of the actions required to achieve long-term aims. Shorter-term plans to achieve the strategy should include milestones against which progress can be assessed.

ANALYSIS 1. PURPOSE 2. IMPACT 3. PEOPLE 4. FINANCE A ASSESSMENT FRAMEWORK PRACTICE 0 OPERATIONS GRID

Learning from evidence and experience is an important part of strategy development. Look at how the charity responds to new information and its previous track record of innovation. Has it used information about its impact to learn and adapt its approach? Has it been willing to close down activities that are out of date or unsuccessful? Has it been able to take advantage of new opportunities and manage unexpected events? In complex and unpredictable situations, some charities may choose to have an 'emergent' strategy. This places a focus on learning and agility, within the context of a clear overall strategic intent against which rapid decisions can be made.

Community Links helps disadvantaged people, running a range of community projects across East London. In recent years increased demand for its services has coincided with significant cuts to legal aid and severe reductions in several other sources of statutory funding. The charity realised that to continue to help people in this new environment, it needed to adapt its strategy—from providing services to the community to empowering the community to support itself. Greater use of trained volunteers in place of paid staff not only saved costs but allowed them to tailor services to the needs of the individual communities it works with. This approach has the added benefit of increasing the agency and social capital of people living in East London.

Implementation is the real test of any strategy and a good strategy development process increases the chances of success. Involving front-line staff and people who use the charity helps to ensure a charity's strategy stays relevant, so look for evidence that their views and experiences inform any plans. Does everyone say the same thing about what the strategy is? Do staff understand and implement it? In our experience this is not always the case.

A charity's strategy process can help it to consider its appetite for risk and the likely balance of risk and reward. This will differ for different charities: those seeking to tackle the root causes of social problems may decide to take more radical or disruptive approaches. Even charities such as wildlife reserves or heritage organisations that exist to preserve rather than disrupt will still need to respond to change. The best charities balance ambition with realism and adapt and evolve rather than standing still: excessive caution can be just as damaging as excessive risk-taking. ANALYSIS FRAMEWORK

Charities with well-evidenced activities should look to increase their impact by reaching more people—whether through growing as an organisation, promoting a particular approach (eg, through training, disseminating research, or campaigning for wider adoption) or more formal methods such as licensing and franchising. Where a charity is aiming to grow, plans should be realistic, justified and mindful of the risks involved. Large charities must be careful not to undermine smaller organisations by expanding into areas where they are not best placed to work—often smaller, specialist organisations are better able to reach a specific community or have specific local knowledge to draw on.

Most charities face a choice between working at scale or working in depth; few are able to reach large numbers of people and work intensively with all of them. This trade-off is especially relevant for big organisations with the scale to reach large numbers of people if they choose. Consideration of this question should form part of the charity's strategy development and theory of change. <u>Scale</u> is not necessarily a sign of success and we are wary of organisations seeking growth for its own sake.⁵

One of the challenges in developing a strategy is to ensure that it fits with the capacity and scale of your organisation, and adds real value to the sector. Sight loss charity **<u>RNIB</u>** is aware that, as a large organisation, there are some things that it can do that other smaller charities can't. Therefore it focuses on activities that lend themselves to scale, such as printing industrial quantities of Braille or operating a nationwide helpline. The organisation tries to avoid duplicating the efforts of smaller organisations that, with their local knowledge, can deliver services especially suited to local needs.

Spotlight on... Digital transformation

Digital technology is now so commonplace that it permeates almost every aspect of our lives—disrupting and transforming industries and the way we live. While it's understandable that some charities have put thinking about a digital future on the back-burner due to more immediate challenges, digital technology can't be ignored and presents both a threat and an opportunity.

Digital technology cuts across all aspects of a charity's work—from strategy to service delivery, from communications to fundraising and engagement, and from management information to impact practice. Organisations need digitally savvy leadership to appreciate this potential, to develop the expertise required to implement it, and to lead the changes required to ensure it adds up to greater efficiency and impact for beneficiaries.

When analysing a charity, it is important to consider how technology could influence its effectiveness and help it improve. But be realistic about what to expect—the digital maturity of an organisation is likely to be constrained by its size, budget and leadership. Technology-focused projects are also often iterative and involve a level of uncertainty. We encourage collaboration and the development of collective solutions across organisations and sectors. For more on this, read <u>Tech for common good: The case for a collective approach to digital</u> <u>transformation in the social sector</u>.⁶

- Ask to see the strategy (this will usually be a standalone document). How often is it reviewed? Does the charity adapt in response to lessons learned?
- Do people at all levels understand the strategy? Do the views of staff and people using the charity influence strategy and service development?
- Is the charity equipped to respond to current trends? Is it making best use of digital technology?
- How ambitious is the strategy? What are the risks and how is the charity managing those risks?

Do the charity's activities reflect the strategy?

We want to know that the charity is doing the right thing, in the right way. Activities should reflect the strategy set to achieve the overall goals. When a charity has a number of different activities, we expect to see sensible links between them—a theory of change can help map this (see page 15). For example, a charity's insights from providing services or running a helpline could and should inform its policy-influencing activity. The best organisations also involve their service users in the design of their work.

Organisations can find themselves doing things because 'that's what we've always done'. Sometimes they come to define themselves in terms of what they do-the services or activities they deliver—rather than what they achieve. To guard against this, it should be clear how activities contribute to the charity's goal; again, a theory of change can help.

Activities should not be set in stone, but should respond to changes in demand. Charities need to be alive to new ways of doing things, such as using digital technology to reach people, or trying to push changes in the system. Conversations with staff and service users about what different activities achieve and if they can be improved will help to ensure that activities remain relevant.

Spotlight on... Effective collaboration

Sometimes collaboration—within or across sectors—can be the best way to achieve results, by providing complementary services, reducing fragmentation or allowing proven interventions to reach more people. On the downside, collaboration can also be time-consuming, difficult and expensive—and does not always lead to greater impact.⁷

At the very least, charities should understand their role within a sector and how their own actions relate to the work of others. We would look for collaboration where it is relevant and productive, and expect charities to have a clear sense of how it increases their impact. Check with other stakeholders that the charity is exhibiting collaborative behaviour. Look at how the organisation is working with others, and whether collaboration is achieving results. Could closer collaboration or a different type of collaboration help it achieve more? Charities are increasingly seeing the benefits of networks, which can be looser or more structured according to the charities' needs, and may be more responsive than formal approaches.⁸

Charities should also consider whether the way they develop and deliver activities supports what they are trying to achieve. Does the charity give the people they work with an opportunity to actively shape activities? Does it use input from staff and volunteers? Are activities based on evidence of what works? If a charity is trialling a new approach, the evidence may be limited, but a rationale for the approach and method for assessing its effectiveness will ensure innovation is tested sensibly. If the evidence for the activities is well-established, then the charity should focus on delivering them effectively. In either case, charities that learn from what they do will increase their impact.

The best charities are always looking to improve. This means assessing what they do, learning from the findings and putting that learning into practice as part of a cycle of continuous improvement. We explain the use of 'plan, do, assess, review' to support good impact practice on page 25, but this can be applied to any area of a charity's work.

- Do activities reflect the strategy? Do they contribute to the charity's goal, and are there sensible links between them?
- What is the charity's theory of change and evidence to support its approach?
- Has the charity ever closed activities or stopped doing something?
- Is the charity able to adapt its approach in response to changing circumstances?

Does the charity achieve results?

The charity may be seeking to do the right thing in the right way, but is it achieving results in practice? Evidence of results tells us whether a charity is making a difference, to what extent, and how this is improving over time. It also informs judgement of value for money.

Looking at what the charity achieves can be a terrific motivator for staff, supporters, volunteers and people using the charity. When results are as expected, a charity can make the case for doing more and share findings with others to spread good practice. Where results are below expectations, the organisation should use this information to adjust its activities or overall strategy. Sharing experience with others can ensure that mistakes are not repeated elsewhere.

What to look for:

- What do the results show and are they improving over time? Are others doing the work better?
- How do results compare with what the charity expects to achieve? Are expectations sufficiently ambitious?
- What are the risks of unintended or negative impact? What are the risks that good results will not be maintained, or disappointing ones will not be addressed?

Useful resources Creating your theory of change: NPC's practical guide Growing pains: Getting past the complexities of scaling social impact Systems change: A guide to what it is and how to do it Strategy for impact: NPC's practical approach to strategy development for charities NCVO Knowhow Nonprofit strategy resources

1. PURPOSE 2. IMPACT PRACTICE

3. PEOPLE 4. FINANCE & ASSESSMENT OPERATIONS GRID

2. IMPACT **PRACTICE**

ANALYSIS

FRAMEWORK

The best charities are driven by the impact they achieve—the lasting difference they make to the issue or the people with whom they work. Impact practice is the cycle of activities that focuses on impact: planning how to achieve it, delivering, assessing and learning for the future. Good impact practice helps charities to improve.

Many organisations launch into monitoring and evaluation without thinking about what information is already available and what would give them the most useful information about their work. Unrealistic expectations from funders can contribute to this.

However developing and implementing a relevant measurement framework is a crucial step towards being a more effective and impact-driven organisation. We outline the stages involved in our *Four pillar* approach, which this section draws on.⁹

Useful terms

Monitoring: A systematic way to collect and record information to check progress and enable evaluation.

Evaluation: The use of information from monitoring and elsewhere to judge and understand the performance of an organisation or project.

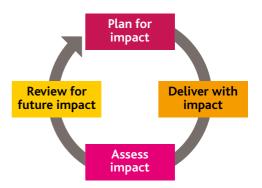
Impact measurement/impact evaluation: The set of practices through which an organisation establishes what difference its work makes.

Does the charity use information to learn and improve?

Good impact practice involves using information to understand, learn and improve—and acting on what it tells you. This is a continuous process that involves reviewing the collection of information (does it tell the charity what it needs to know?) as well as the results themselves (is there anything the charity should change as a result?).

This process is illustrated by the cycle of impact practice, which we have adapted from Inspiring Impact's <u>Code of Good</u> <u>Impact Practice</u>:¹⁰

- **Plan:** Identify the desired impact and how to deliver it, and plan an approach to impact measurement.
- **Do:** Deliver the work, and collect the necessary information.



- Assess: Make sense of the information collected, draw conclusions and compare findings.
- Review: Learn from findings and use them to improve the work.

The findings should inform planning and action within the organisation; this also shows staff, volunteers and others involved that things change as a result. Where results do not meet expectations, the charity will want to ask why and adjust its activities, assumptions or overall strategy. The best organisations use data to inform decision-making at every level and are prepared to change in response to what the evidence tells them. A record of using experience to hone activities, and being unafraid to try new techniques, are hallmarks of an organisation that is ambitious to become better.

FRAMEWORK

Empowerment, a Lancashire charity working with people affected by domestic abuse, health and social care problems, shows how smaller organisations, too, can use information to learn and improve. It uses **Insights**, the outcomes measurement programme set up by the national domestic abuse charity SafeLives, to help understand its work. Data from Insights showed that only 2–3% of Empowerment's service users are lesbian, gay, bisexual or transgender (LGBT), compared with 10% of the local population. Empowerment is now working with local community groups to understand why this may be and address the issue, thereby effectively using information to learn and improve.

- · How does the charity use results to improve performance? Has it learned from results, including mistakes, and adapted services or strategy accordingly?
- · Does the charity compare results over time?
- How do results compare with others in the sector? Has it attempted to benchmark itself against others? (This is not always feasible).

Does the charity know what it is achieving?

The starting point here is a clear articulation of the outcomes the charity wants to see and how it plans to achieve them, based on evidence. At the least we would expect a charity to have reliable information on its reach (eg, how many people it is working with, and whether it is reaching its intended audience) and whether it is delivering the right sort of quality. Where possible, indicators of change also help to show what the charity is achieving.

The charity may want to compare this information with the overall need in its sector or location, to test whether it is scratching the surface or going some way to meet the need. Estimating what the world would look like without the work of the charity-the 'counterfactual'—is helpful. Would the change have occurred regardless of the charity's involvement? Have there been unintended or even negative effects? There are a range of approaches that attempt to answer these questions, ranging from simply asking service users for their views to advanced methods like randomised control trials.¹¹ These questions are also relevant to cost-effectiveness (see page 53).

- Does the organisation know how many people it reaches and who it reaches? Can it make an informed estimate of the difference it makes? Look for numbers as well as stories: be wary of an organisation that uses only anecdotes and case studies to talk about its impact.
- Does the charity know how it is making a difference? Effective data collection (see page 29) will help to answer this.
- Does the charity understand the full impact it is having, without overstating this? Can the charity spot if anything is going wrong?

Does the charity have the right approach to evaluation?

Organisations need to identify ways of answering questions about how their services work and the difference they make with credible evidence. In an ideal world, charities and funders would have perfect clarity about the impact of different activities. The real world is more complex, so charities and funders need to be realistic about what they can expect.

There are three questions a charity should be asking:

- Is it doing the right thing? Is this model or activity an effective approach to the problem?
- Is it doing it well? Is the model or activity being delivered effectively?
- Is there a better way of doing it? Are there more effective approaches, or can the model or activity be delivered more effectively or efficiently?

The first question is more relevant when the model or activity is new or untested, or has not been used in the particular context before. In this case, in-depth evaluations will be appropriate to test whether the model works. Where the charity's theory of change is strong, and there is existing evidence to back up its model, the charity can simply focus on ensuring it is being delivered effectively and remains relevant. Real-time information that highlights whether different interventions work better with different groups, for example—or problems affecting delivery—allows the organisation to adapt.

A charity's **approach to evaluation** needs to be proportionate to its size and the stage in its development: small organisations may not have the resources for detailed impact measurement, but should be using existing evidence (where there is some) and capturing information about their reach. Very early-stage organisations would not have this information, but we would expect them to have considered questions to ask and have plans in place for how they will answer them. Large charities often use external evaluators, sometimes academics, in order to bring independent credence to their work—although the quality of this analysis can vary.

Spotlight on... Effective data collection

- Involve staff, volunteers and people using the charity. This ensures questions focus on what matters, and are asked in a way that is meaningful and accessible.
- **Minimise the burden on people using the charity.** In-depth information only needs to be collected from a sample—as long as the sample is representative, the charity can generalise from these results.
- Combine gualitative and guantitative data. Quantitative data is about numbers, for example, the number of people accessing a service or the proportion whose confidence has improved. Qualitative data aims to understand underlying reasons, opinions and motivation.
- Use off-the-shelf tools where possible. Validated approaches are more robust, and using standard approaches is more efficient and allows for comparison. Standard approaches include shared measurement, where charities working towards similar goals agree what to measure and what method to use. This helps compare and share learning.¹²
- Consider the possibility of bias and takes step to avoid it. For instance, often in the charity sector the people who participate in a programme or the related evaluation are not representative, because they are only those who volunteered or who made it to the end of a programme.

- Is the charity focusing on the right question(s)? Is its approach proportionate?
- What is the evidence behind the charity's activities? Is it credible?
- Do staff members and volunteers understand their role in data collection and analysis? Are they interested in what it tells them? If data collection is not supported by staff or volunteers, processes are not fit-for-purpose or the questions are seen as irrelevant.
- Ask to see any evaluations—often these are published on the charity's website. Does the charity talk about its approach to evaluation?

Is the charity open about its findings?

Charities are increasingly reporting on their impact in annual reports, impact reports or published evaluations. They may even share negative findings and lessons learned—something we strongly encourage. This supports genuine learning about what works (or doesn't!), within and between organisations, which can lead to improved services. By sharing their findings, charities can demonstrate accountability to beneficiaries, supporters, funders and other stakeholders, which can in turn help to increase trust. We look at two things in how a charity shares its findings: does it tell the audience what they need to know and are the findings presented accurately?

<u>Impact reports</u> should focus on results and show a good understanding of the outcomes the charity achieves, as well as a willingness to learn from evidence—be it good or bad. They should be clear about what the charity is trying to achieve and how, the results of its work and lessons learned. Impact reports should also include information about the evidence, including any weaknesses, uncertainty or limitations in the findings.¹³

With funders increasingly focusing on impact, it can be tempting for charities to over-claim their results. However, openness about the limitations of the data and accuracy in presenting any conclusions that can be drawn from it reflects integrity and transparency in an organisation, and are indicative of a learning organisation.

- Is the charity honest about whether it is achieving the results it hoped to?
- Are claims about impact backed up by credible evidence?
- Are published findings easily available and understandable? Do they include methodology and lessons learned?

Spotlight on... Inspiring Impact

Inspiring Impact is a UK-wide collaborative programme, led by NPC, that works with the charity sector to help organisations know what to measure and how to measure so that good impact practice becomes the norm. The website inspiringimpact.org offers free tools and advice to hep you improve your impact measurement practice, including:

- The Code of Good Impact Practice which presents high-level principles to follow at each stage in the cycle of impact practice.
- Measuring Up!: an online step-by-step self-assessment tool you can use to gauge your current impact practice, develop an action plan and make progress against that plan.
- The Impact Hub which is a one-stop shop for impact resources and tools which you can filter by category, sector, format or cost.



Reporting when things don't go to plan

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People—staff, volunteers, trustees—make a charity what it is. Strong leadership, sound governance and supportive management that bring out the best in staff and volunteers can make a team more than the sum of its parts.

For smaller organisations, being overly dependent on a single individual (whether volunteer or staff member) can be a particularly pressing issue, with recruitment and retention often a challenge.

Large organisations, meanwhile, face different challenges—communicating effectively between staff, ensuring a shared vision and coherent culture can be more difficult with a very large or dispersed team.

Does the charity have good leadership?

By leadership we mean articulating a clear, coherent and consistent vision, charting a path to delivering it (through the charity's strategy) and enabling others to buy into it. Good leadership articulates a coherent vision, ensures that a strategy is implemented in practice and that the organisation is able to develop and adapt as needed. Leadership is not just the job of the chief executive—the chair, board and management are all part of the leadership team. Very small or community organisations may not have a chief executive or management team—in this case, leadership sits with the trustees and often a small group of volunteers.

The leadership team must have the skills and experience to handle their brief, and communicate effectively with people both inside and outside the organisation. They should put the charity's mission first; this can lead to uncomfortable choices and decisions. Leaders do not have to be charismatic to be effective—indeed, a 'heroic' leader may be too dominant within the charity, leading to risks around succession and judgement. The best leadership teams take care to strengthen the organisation by developing leadership among staff or volunteers, and create an environment in which people can (and want to) give their best.

Different styles of leadership are more useful at different stages in an organisation's development: a start-up requires leadership that is highly adaptable and can cope with uncertainty; turnaround requires someone who is confident, who inspires confidence and is able to take difficult decisions; and when things are stable, empowering or distributed leadership can be really effective. Good leadership is particularly important during times of change and transformation.

- · Does the management team bring a range of perspectives and experience? What have they achieved in post or, if new, what did they achieve at previous organisations?
- Where do the chief executive and chair see the organisation in three years' time? Are they 'on the same page'?
- How vulnerable is the charity to a change of chief executive or other personnel? Where the chief executive is also the charity's founder, this transition is particularly important.
- Talk to external stakeholders: what is their impression of the leadership team? They may be more candid than those directly connected with the organisation.

Spotlight on... the chief executive

The chief executive is invariably the most influential person in an organisation and any in-depth analysis should involve meeting him or her. Some of the most important points to consider include:

- **Strategic vision:** The chief executive must ensure that the organisation has developed a sensible strategy and that it is in a position to implement it.
- **Relationship with the chair:** An effective chief executive–chair relationship is a key indicator for success. If the relationship is weak, both will have an uphill battle to achieve the impact they want.
- Relationship between the chief executive, board and management team: If the chief executive and management work well together, and with the chair and trustees, then the organisation is well-placed to succeed. A mix of mutual support, respect and constructive challenge is ideal.
- **Day-to-day management:** A senior team that is engaged with day-to-day activities and understands the concerns of front-line staff, volunteers and users will be able to make better decisions.
- Involvement with core functions: The chief executive is often the most important fundraiser in any organisation—we would expect him or her to have a clear understanding of the finances and fundraising activity, and to maintain key relationships.
- **External profile and relationships:** As the person most often called upon to represent the organisation externally, the chief executive needs to be an effective advocate and credible spokesperson for the charity and the issue that it represents.
- **Drive and resilience:** The ability to make things happen, take difficult decisions and implement them is an important characteristic of effective chief executives.

Does the charity recruit good people and manage them well?

Motivated, capable staff and volunteers are a vital part of any effective charity. Charities that use their human resources effectively—the right people, in the right places, doing the right things—are more likely to achieve their mission, and to do so efficiently.

Some charities comprise only staff; some are run entirely by volunteers; while many involve a combination of the two. Whether staff or volunteer, the people involved in a charity should understand how their work contributes to the organisation's mission as well as how their work relates to that of other colleagues. Their knowledge and skills should be used effectively across the organisation, including through involvement in decision-making. They must be adequately trained or qualified, with all major legal and practical issues covered: for example, Disclosure and Barring Service (DBS) checks are essential for those working with children or other vulnerable groups.

In post, staff and volunteers should be properly managed and given the opportunities and support to develop in their role—with mechanisms in place to identify and correct underperformance, at whatever level it occurs. People management practices should reinforce the direction and tone set by the leadership: supporting high standards, using resources effectively and encouraging learning, improvement and accountability.

Some charities involve highly skilled and experienced volunteers who bring additional knowledge and expertise to the organisation. Other volunteering opportunities may not be particularly highly skilled—this is fine, as long as both sides are getting something from the experience and volunteers are appropriately supervised. Volunteers can be among a charity's most committed supporters and advocates, and can bring new ideas and perspectives to an organisation. The most effective charities recognise this and invest in the relationship, involve volunteers closely and use them strategically in order to further the charity's mission. They recognise, however, that volunteers can be expensive to recruit, train and manage. Committing adequate resources to volunteers' recruitment and support will lead to better results in the long run.

FRAMEWORK

Good morale contributes to an organisation's effectiveness. Sickness absence and staff turnover over a period of time will give you some indication of staff morale within an organisation, although this needs to be taken in context. Organisations that employ more young people are likely to have higher rates of turnover, for example, as are those that employ staff by project. In charities where front-line staff do very stressful work, such as domestic violence charities, the availability of clinical supervision can help reduce staff absence and turnover. Low volunteer turnover can be a sign of a satisfying volunteer experience although again, this needs to be taken in context.

- What can you glean from the track record of key people?
- If you are able to visit sites and talk to staff and volunteers, are staff motivated and positive about what they do? Do they share the vision and enthusiasm of the top team?
- What opportunities are there for staff and volunteers to develop in their roles?
- Can you gauge staff satisfaction? If possible, check turnover and sickness absence, but remember to consider this in context.

How good is the charity's governance?

Governance is more than simply reading board papers and turning up to meetings: charity trustees have the critical role of ensuring the charity is doing what it sets out to achieve.¹⁴ They steer the direction of the organisation, appoint the top team and oversee the financial and practical aspects of running the organisation. They should be able to embrace risk as well as manage it—an overly cautious board can be just as damaging as one that takes excessive risk.

The best boards are driven by impact. They are knowledgeable and engaged, know what is going on at the charity and offer support and direction to senior staff on an ongoing basis. Trustees should be careful not to hold the executive team back and therefore need to be up to speed with areas of rapidly evolving practice, for example, in areas such as digital and **social investment**.

Look for evidence that board members understand their role and responsibilities (for example, through a good induction and a job description). The chair of trustees is a particularly important role: this varies according to the charity's size and circumstances but includes planning trustee meetings, ensuring they are properly run and recorded, that trustees comply with their duties and the charity is well governed. The chair often has a casting vote on the board. In many cases he or she will act as a spokesperson for the charity (not unique to the chair) and act as a link between trustees and staff. The chair also line manages the chief executive on behalf of the trustees, and their relationship can be crucial to the charity's success. As with the chief executive, different styles of chair can be particularly useful at different times.

The board should make a succession plan for key positions in the charity, including on the board itself. Its membership should encompass a range of relevant skills—these will vary according to the organisation's scale and activities. Many boards rely on personal networks to recruit trustees. This can be helpful in sourcing candidates, but increasingly charities see the benefit of having an open recruitment process and looking for trustees beyond their usual networks. Diversity on boards can improve effectiveness, introducing different experiences and perspectives. Some charities seek to involve those with relevant personal experience as trustees, which can work well. There should be proper processes for the induction, development and evaluation of the board, and a limit on terms—a limit of two three-year terms is about right.

- Check what the annual report has to say about governance processes. Are there any subcommittees, and if so in what areas?
- Ask about board procedures, and review board meeting papers or minutes to see if the board's focus is distributed appropriately across the different aspects of effectiveness outlined in this guide.
- How engaged is the chair? How much do they add, and how do they support the chief executive? How do the chief executive and chair interact?
- Ask about trustee roles, skill mix and governance processes. Do the areas of expertise cover all the bases? Try to gauge the level of engagement: how often does the board meet and what is the average turnout? If talking to staff, ask them about trustees' involvement in the organisation.
- · Has the board identified potential risks to the organisation and ways to mitigate them?



Do people using the charity help to shape its work?

Charities are increasingly recognising the benefits of involving people who use the charity in shaping their work, designing services or developing strategy. There is no one right way to do this—different approaches will work for different organisations and different groups.

Some charities have formal mechanisms for involvement, such as user panels or representation on the board, while others engage people on a more informal basis.

Whatever form this involvement takes, it must be purposeful, genuine (not just for appearance) and ongoing—if it doesn't make a difference to anything, then it is a waste of everyone's time. Involvement should apply both at the strategic level and on the front-line, with effective communication between the different levels. If done well, involving people in this way is likely to disrupt the power balance between management and 'service user'. This can lead to uncomfortable questions and conversations for the charity's leadership.

Thera is a charitable group of companies that supports adults with learning disabilities. Its vision is that people with a learning disability can be leaders in society and should be in control of their own lives. It therefore ensures that people using the charity have as much control over the charity as possible. This permeates the whole organisation: the name and logo were chosen by users and people with learning disabilities are employed at all levels of the organisation, including as paid directors. This holistic approach means that no element of the organisation lacks the voice of the people it supports.

- Look on the website and in published materials for a description of how the charity involves people, or ask the management.
- Look for evidence that engagement is real: what has changed as result?
- If appropriate, talk to people affected about whether and how they are involved and about what changes have happened as a result.

Does the charity have a healthy organisational culture?

Culture is intangible: you will not find it written down in an organisation's policies and procedures, and it is difficult to clearly identify and describe it. Culture is the collection of unwritten assumptions, shared beliefs and accepted norms of an organisation, and is powerful because it influences our behaviour without us being aware. A charity's culture can therefore undermine or reinforce its strategy and its ability to deliver its mission, often without the organisation realising. This leads to the famous saying, usually attributed to Peter Drucker, that 'culture eats strategy for breakfast'.¹⁵

A charity's leadership team cannot dictate culture, but they can influence it; their behaviour sets the tone of the organisation. Is the charity's culture supporting its ability to deliver, or holding it back? We look for a good 'fit' between the organisation's culture and what it is trying to achieve: if a charity is all about empowering people to take control of their lives, a 'command and control' executive culture that directs staff and stifles initiative isn't going to be convincing!

- What sort of culture does the management team want to foster, and how do they try to influence this?
- Is the management's description consistent with how staff and beneficiaries see the organisation?
- Do the values they claim match behaviour you witness?

Useful resources

The essential trustee: What you need to know, what you need to do (CC3) (Charity Commission)

Board matters: A review of charity trusteeship in the UK

Happy relations? Ensuring effective partnerships between trustees and senior management

It starts from the top: Improving governance, improving impact

Good governance: A code for the voluntary and community sector (NCVO, ACEVO, SCC, ICSA and WCVA)

Transmitting trust through governance: Charity governance review 2016 (Grant Thornton)

NCVO Knowhow Nonprofit people resources

Association of Chairs www.associationofchairs.org.uk

Association of Chief Executives of Voluntary Organisations (ACEVO) www.acevo.org.uk

NPC runs a series of trusteeship seminars supported and hosted by The Clothworkers' Company. Summary briefings from these sessions are available to download from our website **here**.

In 2015 NPC and The Clothworkers' Company also formed a partnership with Reach and Prospectus to run The Charity Governance Awards to celebrate outstanding governance in charities both small and large.

FRAMEWORK

ANALYSIS

PRACTICE

4. FINANCE AND OPERATIONS

Money is a means to an end, but it matters: financial security and sustainability allow charities to focus on their mission. We need to be realistic about the environment in which charities work: resources are scarce and money often comes with conditions.

Many funders prefer to restrict grants to a particular project, activity or post. This restriction is binding and charities are in breach of trust if they use restricted income on anything other than what it was intended for. Charities are simultaneously expected to build up reserves and to spend as much as possible on delivering activities. In such an environment, achieving financial security is a perpetual challenge and unrestricted funding, which can be spent as the charity sees fit, is like gold dust. Unrestricted funding allows charities to be more responsive, more agile, more independent and more forwardthinking, and we advise funders to provide unrestricted funding wherever possible.¹⁶

Spotlight on... Charity accounts

Donors making a smaller contribution will have to rely on careful reading of published information in the charity's annual accounts, and accept that they won't be able to answer all of the questions set out. For those looking to donate more, and with time to spend, internal management accounts, budget and cashflow forecasts give a better understanding of the charity's situation. A conversation with the chief executive and finance director (if there is one) will help to complete the picture.

More detail on analysing charity accounts, is given in NPC's Keeping account: A guide to charity financial analysis.¹⁷ Charity accounting guidance (the Statements of Recommended Practice or SORP) changes regularly—this advice is correct at the time of writing, but readers should check it remains current.

All charities must prepare annual accounts and make them available on request, although requirements vary depending on charities' legal form, income and assets.¹⁸ Most organisations also publish accounts on their own website and this is basic good practice. Different parts of the accounts provide different information:

- The auditor's report (or independent examiner's, for charities with income <fi>(£1m) tells you whether the auditor believes the picture presented to be true, complete and fair.
- The statement of financial activities (SOFA) sets out income and spending and may show whether the charity is living within its means.
- **The balance sheet** shows assets and liabilities, and is important to judge the charity's financial cushion.
- **The cashflow statement** shows the areas of the cash surplus or deficit for the year.
- Notes to the accounts provide narrative detail on the figures in the accounts.

A quirk of current charity accounting regulation means that grants are entered as soon as there is reasonable certainty that they will arrive, regardless of whether the funds are received or the work has been undertaken. A charity's accounts could show large sums received in one year (resulting in a surplus), followed by costs incurred the following years as work is delivered, with no corresponding income (resulting in deficits). Reserves that look abundant may be designated for a purpose. Audited accounts alone may not tell the reader about the terms under which big 'lumpy' grants have been received, what is to be delivered in return, and what this might cost, Explanation and interpretation will be needed to determine whether the charity is living within its means.

Most charities run management accounting systems to match costs and work to the funds received. These are not independently assessed, but may provide a better picture. Steady unrestricted income from regular donors, lots of small grants, or contract income where work is paid for in arrears, is less of an issue: the audited accounts will approximate to reality. Just as important as checking the backwards track record is looking forward: relying only on annual accounts to assess a charity's financial sustainability is akin to driving using only your rear-view mirror! Budgets, forecasts and forward cashflows tell you about the charity's future prospects.

Is the charity financially secure?

Financial security refers to whether income covers expenditure, and how predictable both are; how strong the balance sheet is, and therefore what sort of financial cushion the charity has; and its outlook for the future. An important consideration is the charity's ability to manage fluctuations in income, whether short-term or systemic. These factors affect its ability to continue its activities and plan for the future.

Income and spending

Is the charity living within its means? Income should cover expenditure and match the charity's ambitions. Continuous over-spending may be good for beneficiaries in the short term but will cause problems later. Check, too, whether a charity is spending enough—hoarding cash in the bank is unlikely to achieve social impact. The story told by the figures in the accounts should reflect the narrative in the trustees' annual report.

The charity's bottom line does not give the whole picture: a planned deficit may be a sensible use of reserves, whereas one that takes the charity by surprise could signal cause for concern. Equally, a surplus may have been inflated by the timing of grants, a one-off payment (such as a sale of assets), overly cautious spending or by the treatment of trading income. Shops report gross income and all the costs in the accounts, which inflates both items on the SOFA. A neater way of analysing trading income is to look at the net contribution of shops or trading activities so that it does not distort analysis of where income comes from.

It is sensible for charities to avoid over-reliance on a single source of income and to have a plan for dealing with those sources most at risk. Restricted income must be used appropriately, and ideally, the charity would have sufficient unrestricted income to cover any additional expenses, such as the development of new ideas and partnerships. Charities can avoid using valuable unrestricted income on restricted projects by practising full cost recovery. This means recovering all the costs of delivering a service: not just activities, but the facilities and management time supporting those activities.

Some charities are able to develop business models that help to pay for the social impact they create—for example, by packaging up a vital piece of intellectual property that others might want to buy, or selling the benefits (including cost savings) of a health intervention to a hospital trust. This can give the charity greater financial independence,

but these models rely on someone, somewhere, being willing to pay—which is not always easy. And, as ever, these activities need to align with the organisation's mission.

Balance sheet

The balance of assets and liabilities underpins a charity's financial security: the charity will need enough cash to meet immediate financial commitments and provide some flexibility in case of unexpected events. Look for an appropriate level of money in the bank—this will vary according to the charity's income and cashflow.

Reserves

Reserves are the funds held by the charity that can be spent on the charity's purpose. They are primarily held to protect the continuity of the charity's work if income falls. They are also held to provide capital for expansion or asset purchase. Trustees set the reserves policy, which should be reviewed regularly and set out in the annual report, including the desired level of reserves (either in absolute terms or relative to monthly expenses), how that was decided, why reserves are held and explaining any difference between the target and actual level of reserves. Charity Commission guidance sets out trustees' legal requirements.¹⁹

When looking at reserves, you have a choice whether or not to include restricted and designated income in the calculation. The most suitable approach will depend on the purpose for which income is set aside: if this is for activities that are part of the charity's usual business, such as salaries for staff posts, then it is reasonable to include it in the reserves calculation. This is not something you can tell from the accounts, however—so if in doubt, it is best to look at free reserves.

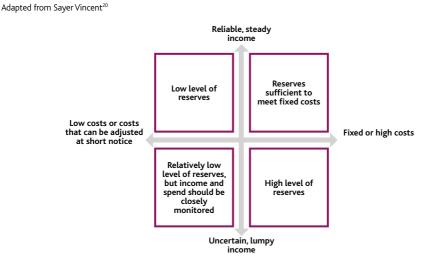
Free reserves are the unrestricted and undesignated funds available to a charity. They normally exclude endowments and restricted funds, and any unrestricted funds that are not available for spending such as assets tied up in property. To calculate free reserves, look at the total level of funds on the balance sheet and take away any restricted funds, endowments or fixed assets, or funds designated for essential future spending that is not part of the charity's usual business.

What is 'sufficient' will depend on the risks in the charity's business model: the certainty of its income, the level of costs and whether or not these can be easily adjusted (see matrix on the next page). For example, charities that get paid in arrears or on a payment by results basis would be wise to hold enough funds to cover payroll in the interim. We used to say

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that three to six months of monthly expenses were sufficient to have in reserve for the efficient running of an organisation, and anything more was inefficient. In a period of low growth, and depending on the charity's activities and vulnerability of beneficiaries, a case can be made for more generous reserve-holding policies. Charities can feel pressure not to hold 'too much' in free reserves for fear it may deter funders; this is unfortunate and counterproductive. In uncertain times a 'rainy day' fund is not just legitimate, it is desirable.

Analysing a charity's reserves



It is prudent for charities to hold some of their assets in cash (or easily realisable investments) that can be used to make immediate payments. Check that the charity can meet its short-term obligations by comparing cash and easily realisable investments to operating costs and obligations. NPC does a rough calculation on this by taking net current assets plus liquid investments, and dividing by monthly operating costs to assess how many months of liquidity is available. If current assets are all tied up in debtors, then this can affect the charity's ability to meet its short-term liabilities.

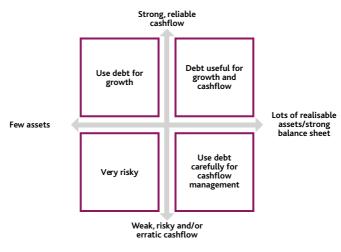
Where a charity has significant investments or endowments, check that they are sensibly and ethically managed. And if the charity has a large **pension deficit**, as many do, check that it has had a recent valuation of pension liabilities, taken proper advice and has a plan in place to manage any deficit.

Debt

It is becoming increasingly common for charities to take on debts to develop assets, fund growth or provide working capital—which would otherwise use up valuable unrestricted reserves. The growth of social investment is prompting many charities that may not have contemplated it in the past to consider debt as a means of financing development.

Charities need to ensure that any debt is sustainable. This depends on two things: strong, reliable cashflow and the charity's balance sheet. Healthy cashflow is a combination of certain revenues and sufficient surpluses to meet debt obligations (interest and principle repayments) comfortably. Where revenue is reliable, with abundant surplus to cover the cost of debt, and the balance sheet is strong, debt is manageable and should not cause concern. Where the charity has few assets and weak cashflow, even modest levels of debt would be a worry (as illustrated in the matrix below). Debt is only useful if it is affordable.

Analysing a charity's debt



Financial outlook

Finally, consider the organisation's outlook—is it a sustainable model? This question is particularly pertinent for social enterprises: while many rely on grant funding to assist with start-up costs, ultimately the organisation aims to earn enough income through trading to be self-sufficient. The business model and ability to cover costs is therefore essential.

- Is the charity living within its means? Is it possible to know this from the information available?
- How far can the charity see its financial future with any certainty?
- How secure is its income, how visible and how diverse? Has the charity anticipated the main risks to its income?
- Can we tell where the money goes? Does the balance of spending reflect the charity's strategy and stated priorities?
- Are there enough funds for a rainy day? Does the charity have enough cash and an appropriate level of reserves? Is any debt manageable?

Does the charity have good financial management?

Financial management refers to the ability of organisations to understand and control their income and spending and balance day-to-day needs with long-term objectives. It does not mean avoiding risks, but managing them properly.

We would expect the chief executive and management team between them to be on top of everything that follows. Small charities may not employ a full-time finance director, or may outsource to external providers. In either situation we would expect the chief executive (or equivalent) to have a good understanding of the finances and be able to answer questions competently. An engaged and knowledgeable treasurer can make a big difference, but it is risky for the treasurer to have sole responsibility for financial decisions. All trustees need some financial literacy and an understanding of their joint and several responsibilities.

Management accounts

A charity without up-to-date management accounts will not be able to make good or timely decisions, or to plan ahead. Management accounts should track monthly and cumulative performance to allow the board and management to assess whether targets have been met and if next year's budget has any relevance, as well as making informed decisions on resourcing. Given the availability of accounting and book-keeping packages, we would expect most charities to be able to produce timely management information, including budgets and forward cashflows.

Increasingly for medium-sized and larger charities this requires a sophisticated understanding of different sources of finance such as public service contract delivery, social enterprise and social investment. For these charities in particular, it is essential that operational and financial information is connected so that management has an accurate and up-to-date understanding of the charity's delivery, income and expenditure.

Processes

Financial management also refers to processes: the controls in place to prevent fraud and financial mismanagement. Following clear and sensible procedures for approving expenditure and making payments can help safeguard against fraud or excess. Does the charity have a process for chasing invoices and managing debtors? Procedures should be clear but not overly bureaucratic. A charity may be able to refer you to its financial procedures manual as a starting point. You can only understand these by discussion with the staff involved. Tone is set from the top, so warning bells should sound if a finance director dismisses questions about procedure as mere detail. A culture of transparency and accountability helps to reinforce good financial management.

- Are the accounts published in good time and without qualification?
- Is management information provided regularly? Do members of the management team and the board understand it?
- Does the information look forward and cover income, expenditure, cash and balance sheet? Do projections look realistic?
- Are good processes and controls in place for managing money, assets and liabilities, and for preventing fraud?

Does the charity have good operational management?

Management decisions should be informed by accurate information. Expectations will vary according to the scale and complexity of the charity, but all charities should have systems in place to monitor indicators relating to essential activities. While some of these indicators will relate to impact measurement, others may cover delivery, audience, contacts, budgets, costs and efficiency. The skill is for management teams to know what is most relevant to them.

Tracking the right indicators allows charities to take more intelligent financial and service delivery decisions, such as how best to reach the target audience or what level of contact with a client achieves the best impact for the cost of delivery. Better use of data can transform an organisation's understanding of need and resources, its own operational effectiveness and understanding of impact. Digital technology can help by allowing charities to connect, coordinate and process this data at speed, as well as helping them to explore new ways to deliver work.

Spotlight on... Fundraising practice

The charity's fundraising should be cost-effective (see **page 53**), sustainable and should align with the charity's mission and values. Trustees need to be comfortable with agreed policies and procedures, and confident they are being followed. This includes meeting the **regulatory requirements** (recently strengthened),²¹ but also consideration of the moral issues. NPC has suggested a '**gran test**', whereby trustees and fundraisers ask themselves whether they would be happy for their own grandparents to be on the receiving end of the charity's fundraising practices.

Given the challenging financial environment for charities, it can be easy for them to be led by fundraising, with decisions driven by what is most likely to bring in cash. Of course, a charity with no income will quickly cease to deliver anything. The best charities make informed judgements about methods that best suit their aims (including which sources of income to pursue, and how), and put their mission first. We look for organisations taking charge of their financial destiny and fitting their financial strategy to meet mission need, rather than the other way around. Operational management includes important but routine activities: quality assurance, ensuring compliance with legal and regulatory duties, <u>data protection</u>,²² and health and safety. Many charities work with vulnerable people and so safeguarding policies and practice must be watertight.

If they are willing to share it with you, look at the organisation's risk register. It should clearly set out the main organisational risks (not an endless list) and, crucially, how the charity is managing them. This is a tool for management, so look for signs that it is used.

Spending money on staff, back office functions and decent IT systems or equipment can help improve operational management. Charities need resources to operate efficiently, and we constantly urge funders to remember this when supporting charities.

- Does the charity make good use of data when making operational decisions? What systems are in place to monitor mission-critical activities and outputs?
- Is there a risk register and is it used? Are policies and procedures in place and implemented on issues such as those listed above?
- If relevant to the charity, have there been any safeguarding incidents in the past year and how were they handled? Is there a member of the board with responsibility for safeguarding? Are all staff aware of what to do?
- Quality standards exist in many areas of the sector. Is the charity accredited and, if so, by whom?

Does the charity make efficient use of all its resources?

Charities have limited resources, and should use them to maximum effect—this includes staff and volunteer time. Try to understand the rationale behind how the charity spends its money and whether this is reasonable. This is not about spending as little money as possible, but spending money wisely and keeping waste to a minimum—while investing in functions that enable the charity to achieve results.

To make sensible decisions about priorities, management need a good understanding of the charity's costs, types of expenditure and how these are likely to fluctuate. An organisation that talks about internal cost controls and benchmarking processes is more likely to be on top of its spending than one that never mentions either. This includes reviewing contracts to procure services and coming up with ways to reduce costs. Management should be able to justify expenditure and point to efforts to improve efficiency. Where all staff, not just finance staff, understand the charity's business model and cost structure, efficiency is everybody's responsibility.

Spotlight on... Efficiency indicators

The costs of both fundraising and service delivery vary according to the nature of charity's work, where it works, and the needs of the people it works with. Not all charities calculate these costs in the same way. Treat these indicators as a starting point for discussion, rather than using them to draw definite conclusions, and be careful to compare like with like.

A charity's **fundraising multiplier** indicates the efficiency of the charity's fundraising function. To calculate it, add the total of voluntary donations and grants to income from events, then divide by the cost of generating voluntary income.

Unit costs are the financial cost to a charity of working with one beneficiary. They can be calculated by dividing the costs incurred by an organisation by the number of people it helps, or by adding together elements of known costs. Remember, this calculation will not tell you what a charity is actually achieving, only the cost of delivering services.

Organisations may have non-financial assets, such as equipment, land, buildings, intellectual property and brand. Are these resources contributing to the charity's overall mission and goals? Many charities have 'legacy assets'—often old buildings. The case to maintain these assets and their part in the organisation's overall strategy should be clear, particularly where they are expensive to keep. Management teams with an eye on efficiency will develop ways of 'sweating' assets, for example, by maximising the use of buildings to develop new income streams. Where a charity owns an intellectual property right but does not have the resources to exploit it fully, the charity should think about how else this could be used to meet its charitable purpose. For example, **Cancer Research UK** licenses its research discoveries to pharmaceutical companies. Only by working with these companies will the drugs receive sufficient investment to take them to clinical trials.

Resources can also be used to leverage additional support from outside the organisation. This might mean convincing a local authority to work alongside them, or attracting pro bono support from corporate partners. Although these have costs associated with them (eg, from managing the relationship with another organisation), they are usually lower than direct staff costs. Charities should be alert to the risks as well as the opportunities in such relationships, and seek partners whose mission and values chime with their own.

What to look for:

- Does the organisation have the right data about costs, outputs and impact to judge whether it is making the most efficient use of all its resources?
- What actions have been taken to improve efficiency when opportunities arise?
- Is the charity making full use of all its assets?

Useful resources

Keeping account: A guide to charity financial analysis

<u>Charity reserves: building resilience (CC19)</u> (Charity Commission)

Charities SORP

Risk management made simple (Sayer Vincent)

The power of data: Is the charity sector ready to plug in?

ASSESSMENT GRID

The assessment grid provides a reminder of the key points covered in the analysis framework and an example of what best practice looks like in each area, as well as indicators of when a charity's performance is satisfactory or below expectations.

A charity demonstrating best practice in an area is highly capable, clearly orientated to do the best for its beneficiaries. and has a 'wow' factor.

satisfactory may have area, but will also have

A charity that is judged below expectations has significant weaknesses in an area, and shows little capacity to improve.

You can use the grid to give an overall picture of a particular charity. This might be a summary assessment at a particular moment in time, or something to return to over time to see where the charity has developed. There are no hard and fast lines between levels of performance, and all charities will have areas of strength and weakness. A commitment to improve is part of what makes an effective charity; using the grid over time can help you distinguish between a charity that is taking steps to improve, and one that is 'coasting' and perfectly content to be average. We recommend that the grid should be used in conjunction with the guide, which goes into more detail in each area.

ANALYSIS1. PURPOSE2. IMPACT3. PEOPLE4. FINANCE &ASSESSMENTFRAMEWORKPRACTICEOPERATIONSGRID

	Key questions	Best practice	Satisfactory	Below expectations
Purpose	Does the charity's vision and mission answer a need?	Targets high priority needs, informed by those affected and by use of evidence. Tackles root causes. Adds value to the sector.	Clear need, informed by evidence, although may not be high priority. Understands role within sector.	Mission lacks relevance or understanding of need. Lacks awareness of wider sector.
	Does the charity have a good strategy for achieving its goals?	Ambitious strategy based on theory of change or similar. Strategy is understood and implemented. Charity adapts to changes in need or circumstance; alive to opportunities without losing mission.	Realistic strategy, broadly understood and mainly implemented.	Strategy weak, irrelevant or not implemented. Charity shows little sign of adapting to change.
	Do the charity's activities reflect the strategy?	Activities reflect the strategy and theory of change. They are based on evidence with sensible links between them. Works collaboratively to increase impact.	Activities mainly reflect strategy and theory of change, some links between them. Collaborates where opportunities arise.	Activities nothing to do with strategy or goal. No theory of change. Duplicates or undermines others.
	Does the charity achieve results?	Reaches target audience with high- quality activities or services and results that improve over time. Achieves wider impact, such as change in policy or others' practice.	Good reach, mainly to intended audience, with activities or services of a decent quality.	Fails to reach target audience; quality of activities or services is poor.

FRAMEWORK

ANALYSIS 1. PURPOSE 2. IMPACT 3. PEOPLE 4. FINANCE & ASSESSMENT PRACTICE

OPERATIONS GRID

	Key questions	Best practice	Satisfactory	Below expectations
Impact practice	Does the charity use information to learn and improve?	Learning, including from mistakes, routinely put into practice to improve services and strategy.	Makes effort to draw lessons from results and seeks to apply them in practice.	Little sign of using information and evidence to improve activities.
	Does the charity know what it is achieving?	Reliable information based on theory of change or similar and aligned to existing evidence. Considers counterfactual.	Charity has reliable information on its reach. Approach based on theory of change or similar.	Lack of clarity regarding intended outcomes; lack of information regarding reach or impact.
	Does the charity have the right approach to evaluation?	Considers outcomes that matter to people affected; board takes an interest. Makes effective use of existing evidence and data collection, and takes a shared measurement approach where appropriate.	Can describe the intended impact of its work through theory of change or similar approach. Uses evidence and collects own data, although may show some weaknesses.	Little interest in understanding impact. Cannot link their work to existing knowledge.
	Is the charity open about its findings?	Open about findings, including weaknesses; promotes knowledge-sharing.	Shares findings; explains method and approach.	Does not publish results, or if so tends to over-claim or otherwise mislead.

ANALYSIS1. PURPOSE2. IMPACT3. PEOPLE4. FINANCE &ASSESSMENTFRAMEWORKPRACTICEOPERATIONSGRID

	Key questions	Best practice	Satisfactory	Below expectations
A People	Does the charity have good leadership?	Strong leadership team with required range of skills and perspectives. Powerful strategic vision; develops leadership in others.	Competent leadership team who can deliver goals. May lack strength in depth.	Lacks vision and ability; fails to gather strong management team.
	Does the charity recruit good people and manage them well?	Excellent staff and volunteer quality and commitment; used effectively and appropriately supported.	Staff and volunteers demonstrate good skills and commitment; approach to recruitment and management may be somewhat ad hoc.	People poorly deployed; weak people management results in low staff morale.
	How good it the charity's governance?	Engaged board with strong skills in all areas and good chief executive—chair relationship. Impact- driven; improves own performance over time.	Board with effective processes and mix of relevant skills, although some areas may be lacking.	Ineffective practice; lack of relevant skills and reflection. Little or no attention paid to impact.
	Do people using the charity help to shape its work?	Ongoing and genuine involvement informs strategy and activities at all levels.	Some involvement; may not reach to all levels.	Rarely consults service users, or consultation is tokenistic.
	Does the charity have a healthy organisational culture?	Values and culture support the organisation's purpose and are consistently demonstrated in practice throughout the organisation. Leadership seeks to influence it positively.	Values and culture support the organisation's purpose; may be a lack of reflection.	Stated values not demonstrated in practice; aspects of culture undermine organisation's ability to do its work.

ANALYSIS
FRAMEWORK

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	Key questions	Best practice	Satisfactory	Below expectations
Finance and operations	Is the charity financially secure?	Healthy and diverse income; healthy balance sheet and strong business model.	Lives within means; balance sheet isn't precarious.	Serious financial concerns threaten organisational stability.
	Does the charity have good financial management?	Strong financial processes; timely information is routinely used; unrestricted income used strategically. Proactive approach.	Good financial processes and controls; understanding of finances based on timely information.	Weak processes and controls; lack of timely or accurate data.
	Does the charity have good operational management?	Uses data to improve services and working practice. Confident and effective risk management.	Relevant operational information is available. Processes for identifying and managing risk.	Inadequate systems; lack of relevant information; little understanding of or attempt to manage risk.
	Does the charity make efficient use of all its resources?	Resources focused to greatest effect. Seeks opportunities to make efficiencies and leverage external resources; record of improvement over time.	Resources focused on activities that contribute to strategy. Commitment to minimise cost.	Poor value for money; haphazard allocation of resources.

TAILORING YOUR APPROACH

Large, complex charities

Disentangling the various activities of a large, complex charity and working out how they all fit together presents a challenge. Does the range of activities make sense? Are connections made between activities, so that impact is enhanced? Has the charity made sense of when to provide one-to-one services to individuals and when to reach broader audiences using large-scale techniques such as digital tools, professional training and events?

The position that large charities occupy within their sector and how they help lead it is fundamental to their wider impact. Do they support or undermine other organisations? Do they share their knowledge and results? Are they open to challenge or do they block efforts to change the status quo?

Large charities are seen by the public as representing a particular issue: they usually have a louder voice and more influence, and we believe they have a responsibility to use these platforms wisely. Where large charities benefit from significant levels of public donations and funding from the public purse, it is more important than ever that they use this money wisely.

Understanding all the activities and projects of a large organisation is not feasible for an outsider, and you will need to rely on assessment of management processes, such as communication up and down and across projects, in order to judge effectiveness. Visiting a variety of sites in different locations can help to show whether this is working. The board and senior management should have a solid grasp of activities, and how they are meeting the charity's purpose.

Campaigning organisations

Running a successful campaign requires careful planning, and it can take a long time to achieve results. The outcomes are uncertain, and it can be hard to attribute change to the charity.²³ However, campaigning can be an extremely powerful tool for bringing about social change, often affecting thousands of people.

Legitimacy and credibility are necessary for an effective campaign. Both require charities to have a strong mandate from their users or members, clear campaign goals and messages (preferably based on evidence), and effective advocates to communicate them.

Because results are uncertain, we would look carefully at the planning and rationale: what is the problem the charity is trying to solve and why is campaigning the best way to do this? What campaigning methods will the charity use and why? How will activities lead to change? Test assumptions about how change will happen and the intermediate outcomes along the way, and make sure the charity is thinking about outcomes not just activities: a good theory of change will do this.

Many campaigns last for years, so they must be able to adjust to changes in government, changes in leadership and cultural shifts, as well as remaining appealing to their audience. Collaboration—often in the form of networks—is also particularly important, building support to increase a campaign's impact.

Community organisations

Community organisations are usually small with a wide range of activities. They are in close contact with local needs, assets and services and are often dependent on individual relationships and local knowledge.²⁴ Community organisations are in a good position to work with communities to find their own solutions to problems rather than imposing answers.

Relevant questions include: how does a community organisation fit into the community? How does it interact with other local organisations across all sectors? Do staff have good relationships with the people using the charity? If you are looking at an organisation in your area, it is easy to get to know the activities of a community organisation by visiting or getting involved as a volunteer—this way you can see first-hand what happens.

The quality and extent of impact measurement varies considerably between community organisations. It is often driven by funders' requirements; the best organisations collect data to demonstrate the outcomes that matter to them and use this to inform what they do. Good financial management is essential, but do be aware that income may be fragile and uncertain.

Charities working overseas

There are practical constraints when analysing organisations that work in developing countries or across more than one country: visiting the charity is costly and understanding the context in which it is working is difficult. The risks involved also tend to be higher—natural disasters, a lack of infrastructure and the political, legal and regulatory environment can all undermine an organisation's good work.

Accessing detailed information on charities where reporting is haphazard and poorly regulated can be tricky. Often organisations do not have basic information about their activities and finances, let alone their impact. More practical challenges include language barriers and properly understanding the local cultural and political context. Seeking out the perspective of another funder can be useful, especially if the funder has visited the organisation themselves and is familiar with the context.

Analysing a charity overseas is largely about assurance: if you are unable to analyse everything directly yourself, you can at least check that the charity itself has given all of these things some thought. For example, check its understanding of the context and of the level of need. Does the leadership know what the government is currently doing in that area? Is the charity's work based on evidence, or particularly innovative? Recruitment can also be a challenge for organisations overseas, and brings its own tensions—how good is the team on the ground? Does it consist of expatriates or local staff, or a combination of the two? Are they appropriately qualified and experienced? The quality of the chief executive is particularly important. Often there may be a single individual driving the organisation, and it can be hard to fill gaps.

For very large charities working internationally, the picture is slightly different: assessing head office is often challenging due to the sheer size and scale of these organisations. Nevertheless, one can look at strategy, impact and use of resources. The quality of different country programmes varies greatly, and donors would be well advised to look at them directly. Fundraisers in central office may be the gateway to doing this, but if you are thinking of making a significant donation, it is worth insisting on speaking to the country director and assessing the strength of the country programme.

Social enterprises

Social enterprises, like charities, exist to fulfil a social or environmental mission. They generate income through trading (selling goods or services) rather than grants and donations, and any surplus is reinvested to further the organisation's mission. A social enterprise's mission might be achieved through its business model-for example, its recruitment practice or supply chain, rather than (or as well as) the activities themselves. A catering company, for example, may achieve its social impact by offering training and employment to vulnerable and socially excluded adults.

Social enterprises take a variety of legal forms. Those that are registered charities file accounts with the Charity Commission, whereas Community Interest Companies (CICs) and companies limited by share and guarantee are regulated by Companies House. Their accounts can be found on the Companies House website.

The social enterprise life cycle is more pronounced than for charities, and they are often but not always—community-based. A commercial mindset and sound business model is particularly important for social enterprises, in order to be self-sustaining.

Get in touch

We hope this guide has been useful to you and we would welcome your comments and feedback—please contact us via info@thinkNPC.org or on Twitter @NPCthinks using the hashtag #CharityAnalysis.

If you are interested in learning more, we run regular training sessions on charity analysis, strategy development and impact measurement. We can also provide independent analysis of organisations on a fee-paying basis, and bespoke consultancy services to charities and funders looking to improve strategy or measure their impact.

For more information on how we could help, visit our website www.thinknpc.org or just get in touch.

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YOUR ASSESSMENT TEMPLATE

	Key questions	Comments
Purpose	Does the charity's vision and mission answer a need?	
	Does the charity have a good strategy for achieving its goals?	
	Do the charity's activities reflect the strategy?	
	Does the charity achieve results?	

ANALYSIS	1. PURPOSE	2. IMPACT	3. PEOPLE	4. FINANCE &	ASSESSMENT
FRAMEWORK		PRACTICE		OPERATIONS	GRID

	Key questions	Comments
Impact practice	Does the charity use information to learn and improve?	
	Does the charity know what it is achieving?	
	Does the charity have the right approach to evaluation?	
	Is the charity open about its findings?	

ANALYSIS	1. PURPOSE	2. IMPACT	3. PEOPLE	4. FINANCE &	ASSESSMENT
FRAMEWORK		PRACTICE		OPERATIONS	GRID

	Key questions	Comments
People	Does the charity have good leadership?	
	Does the charity recruit good people and manage them well?	
	How good is the charity's governance?	
	Do people using the charity help to shape its work?	
	Does the charity have a healthy organisational culture?	

ANALYSIS	1. PURPOSE	2. IMPACT	3. PEOPLE	4. FINANCE &	ASSESSMENT
FRAMEWORK		PRACTICE		OPERATIONS	GRID

	Key questions	Comments
Enance and operations	Is the charity financially secure?	
	Does the charity have good financial management?	
	Does the charity have good operational management?	
	Does the charity make efficient use of all its resources?	

You can download and print further blank templates from our website: www.thinknpc.org/publications/good-charity/

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TRANSFORMING THE CHARITY SECTOR

NPC is a charity think tank and consultancy which occupies a unique position at the nexus between charities and funders, helping them achieve the greatest impact. We are driven by the values and mission of the charity sector, to which we bring the rigour, clarity and analysis needed to better achieve the outcomes we all seek. We also share the motivations and passion of funders, to which we bring our expertise, experience and track record of success.

Increasing the impact of charities: NPC exists to make charities and social enterprises more successful in achieving their missions. Through rigorous analysis, practical advice and innovative thinking, we make charities' money and energy go further, and help them to achieve the greatest impact.

Increasing the impact of funders: NPC's role is to make funders more successful too. We share the passion funders have for helping charities and changing people's lives. We understand their motivations and their objectives, and we know that giving is more rewarding if it achieves the greatest impact it can.

Strengthening the partnership between charities and funders: NPC's mission is also to bring the two sides of the funding equation together, improving understanding and enhancing their combined impact. We can help funders and those they fund to connect and transform the way they work together to achieve their vision.

New Philanthropy Capital 185 Park Street, London SE1 9BL 020 7620 4850 info@thinkNPC.org @NPCthinks

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