

FREY FOUNDATION

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DUE DILIGENCE GUIDE

ABOUT FREY

The Frey Foundation is a multi-generational family foundation. The trustees have chosen a set of priorities including community arts, building community, environment as well as children and families with an emphasis on how can we help get kids ready for school. In addition to the funding priorities, the trustees have also have an interest in working with funding partners – not doing so may cause an organization to go in a direction that they wouldn't have otherwise; single source funding is sometimes not to the long-term benefit of the organization.

MISSION

Investing collaboratively in West Michigan to create a better place to live by strengthening its communities, protecting its natural environment, enhancing the arts, and transforming the lives of individuals and families.

VALUES

We encourage creativity while expecting excellence and accountability in ourselves and others.

PURPOSE

This guide is designed to assist program staff of the Frey Foundation to find out more about applicants and the project they propose for funding. It helps guide the assessment of various aspects of an organization's health as a leading indicator of its ability to successfully implement the proposed project and make an impact. Information presented in this guide is in no particular order of importance.

OVERVIEW

The due diligence checklist is divided into the following three areas:

GOVERNANCE

- History and Record of Performance
- Board and Executive Leadership

OPERATIONS & FINANCIAL HEALTH

- Management Capacity
- Financial Health

PROJECT & BENEFICIARY IMPACT

- Community Context, Planning
- Outcomes and Evaluation
- Other

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TIPS FOR EFFECTIVE INTERVIEWS

It is helpful to use the proposal documents as a starting point for your discussion. This offers an opportunity for the applicant to share the information they are most familiar with – in their own words – which establishes a comfort level that can help start a productive conversation.

1. ALWAYS ASK OPEN-ENDED QUESTIONS.

Avoid questions to which only answers are “yes” or “no”. You will not learn much nor will you generate worthwhile conversations. Open-ended questions typically start with:

- Tell me about...
- How do you...
- What/Who are...

2. KEEP QUESTIONS SIMPLE.

Don't combine multiple areas of inquiry to form a long, complex, difficult-to-track question. One question at a time focused on one issue of interest is the best method to guide a conversation.

3. AVOID QUESTIONS THAT COMMUNICATE JUDGEMENT.

For example, “You didn't think about the implications of... did you?” This is a sure conversation stopper, and will inhibit your ability to foster an open and honest relationship.

4. ALWAYS CONCLUDE YOUR CONVERSATION WITH ONE OF THE FOLLOWING QUESTIONS:

- Is there anything I didn't ask about that you wish I had asked?
- Is there anything we have missed and/or not talked about?

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ORGANIZATIONAL HISTORY & GOVERNANCE

CATEGORY	QUESTIONS TO CONSIDER	KEY INDICATORS	CONCERNS
HISTORY	<p>What have been the most significant accomplishments of the past three to five years?</p> <p>What have been some of the most significant challenges?</p>	<p>Specific examples of how the organization has a proven ability to succeed at its mission.</p> <p>The organization has a track record of results with specific metrics that demonstrates an impact on its constituency or target population.</p> <p>Adapting to change.</p>	<p>The organization's leadership cannot (or will not) openly articulate both successes and challenges.</p> <p>Being overly vague about results.</p>
ROLE OF THE BOARD	<p>Describe your board and the role it plays in the organization.</p> <p>What is the board's role in strategic planning? In fundraising? In financial oversight?</p>	<p>An active board, engaged in fiscal oversight, structured in a way that makes sense for the governance needs of the organization.</p> <p>Board members who are willing to contribute money, with a goal of 100% board giving (amount given is less important).</p>	<p>The board is not active or is disengaged, especially with regard to fiscal oversight.</p> <p>A mismatch between Executive Director and Board perceptions of their respective roles.</p>
COMPOSITION OF THE BOARD	<p>Describe your commitment to diversity and inclusion of staff and board members.</p>	<p>A diversity of membership on the board, with skills and knowledge important to the organization, especially financial management and organizational knowledge.</p> <p>A strategic, ongoing board nominations process.</p>	<p>Little to no change in board members for a long period of time.</p> <p>Lack of process or focus on board development/ recruitment</p>
STRATEGY FORMATION	<p>Do you have a current strategic plan? If not, how do you develop strategy?</p> <p>Who is involved in strategic planning and thinking?</p>	<p>A current strategy for achieving the organization's mission with realistic goals.</p> <p>Involvement of the board in strategy development.</p>	<p>Leadership cannot describe any internal process by which opportunities are evaluated and/or goals are set.</p> <p>Lack of accountability measures.</p>

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OPERATIONS & FINANCIAL HEALTH

During the initial proposal review it is important to perform a review of the organization’s annual operating budget and the proposed project budget (both revenue and expenses), as well as recent audited financial statements and 990 tax filings.

There is important linkage between the documents review and the applicant interview to understand the financial health and overall capacity of an organization. By using the financial documents as a starting point for your conversation about financial health, you will be able to explore broader issues of financial management more deeply.

CATEGORY	QUESTIONS TO CONSIDER	KEY INDICATORS	CONCERNS
ORGANIZATIONAL BUDGET	<p>How do you develop your organizational budget? What is the role of the board in the process?</p> <p>Has your organizational budget increased or decreased from last year? Please explain why.</p> <p>What is your anticipated organizational income breakdown in the committed, identified and unknown categories?</p> <p><i>For organizations that have both 501(c)(3) and (c)(4) entities in their structure:</i></p> <p>Do you have a cost sharing agreement in place? Is it up to date?</p> <p>Is the (c)(3) or the (c)(4) the lead agency?</p> <p>How often do reimbursements happen?</p>	<p>The executive director understands the financial aspects of the organization.</p> <p>The expenses and income outlined in the budget are reasonable.</p> <p>The organization appears to have appropriate income streams and a realistic budget that adequately covers core operating costs.</p> <p>A comparison of the budget to actuals year-to-date shows that the organization is close to meeting its budget.</p> <p>There is someone in the organization that knows its financial performance and can explain any patterns.</p>	<p>The E.D. cannot answer, off the top of his head, in round numbers, the question “What is your current annual budget size.”</p> <p>The board is not involved in the budget development process.</p> <p>In reviewing anticipated income (committed, identified, unknown), the unknown is too big.</p> <p>Budgeted income exactly equals budgeted expense—this is a “plugged” budget; nature is never this precise.</p> <p>Unexplainable budget gaps.</p>

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CATEGORY	QUESTIONS TO CONSIDER	KEY INDICATORS	CONCERNS
<p>PROJECT BUDGET</p>	<p>Describe the budget for the proposed project and how it supports the plan outlined in the proposal narrative.</p> <p>How much of the project funding is committed? What will happen if you don't receive the anticipated funding from other sources (known and unknown)?</p> <p>How did you arrive at your budget estimates?</p> <p>Changes in annual operating budget as a result of program.</p>	<p>The project budget is aligned with the organizational budget.</p> <p>The overall project budget seems appropriate for what is described in the proposal narrative.</p> <p>There appear to be appropriate income streams and a realistic budget that adequately covers program costs.</p>	<p>The project budget is unrealistic and/or not consistent with the proposal narrative.</p> <p>In reviewing anticipated income (committed, identified, unknown), if the unknown is too big.</p> <p>If they are not aware of what the impact of having the new program will have on the annual operating budget.</p>
<p>FINANCIAL SYSTEMS & REPORTING</p>	<p>What financial statements do you generate? How frequently? Who prepares them? Who reviews them?</p> <p>Describe the financial expertise on your board.</p> <p>What role does the board play in financial oversight?</p> <p>What is the process for providing the board with regular financial information?</p> <p>(For fiscally sponsored projects.) How often do you receive reports from your sponsor?</p> <p>How do you access potential sponsors?</p>	<p>The organization has regular audits.</p> <p>The board has member(s) with financial expertise, and the board performs regular financial reviews.</p> <p>The board receives financial reports at least quarterly.</p> <p>Management and program staff understand how to read the financial statements.</p> <p>Financial reports are used to inform programmatic and other decisions.</p>	<p>There are no financial reports or statements generated.</p> <p>The organization has financial statements, but they are not reviewed by the board, or they are out of date (more than two months old).</p> <p>The organization borrows from restricted funds.</p> <p>The organization's mid-year financial statements indicate it is way off budget.</p>

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CATEGORY	QUESTIONS TO CONSIDER	KEY INDICATORS	CONCERNS
FINANCIAL POSITION & TRENDS	<p>Describe your organization’s current financial state.</p> <p>(If debts exceed available cash) what is your plan for debt reduction?</p> <p>(If there was an operating loss) what are you going to do to avoid another loss this year?</p> <p>Does your organization have an endowment? If yes...</p> <p>How much is the total value?</p> <p>What is your spending policy?</p> <p>Where is it held?</p> <p>Is any of it spendable? (i.e. Board Designated)</p>	<p>The organization has a history of breaking even or operating in surplus.</p> <p>The financial manager and executive director can describe the organization’s current financial state.</p> <p>The organization has a long-term vision of where it wants to be financially.</p>	<p>The organization does not have enough cash on hand to meet demands.</p> <p>The organization has a growing accumulated deficit because it ended the past fiscal year with a deficit and is projecting another deficit this year.</p> <p>The balance sheet shows negative net assets.</p> <p>The organization has no debt reduction plan.</p> <p>There are unusual items in the organization’s financials (loans from board members, unpaid salaries) that are not clearly accounted for.</p> <p>The auditor has issued a “qualified opinion.”</p>
FUND DEVELOPMENT PLANNING AND OVERSIGHT	<p>Describe your fund development plan (i.e., fundraising goals and plan for reaching them).</p> <p>How is the board involved in fundraising?</p> <p>What role do board members play in developing strategies to maintain or grow the organizations’ contributed income?</p> <p>How do you monitor progress against your fundraising goals? What role does the board play in this process?</p>	<p>There is a plan for raising money, developed with the involvement of board members.</p> <p>The board of directors is aware of or involved in the organization’s fundraising goals and activities.</p>	<p>The organization cannot articulate a plan for fundraising.</p> <p>The board is not involved in fundraising.</p> <p>The board members responsible for fundraising and development oversight don’t have the skills or interest.</p> <p>The budget projects a perfect breakeven, and the fundraising budget number is exactly the amount needed. Ask for last year’s actuals and see if the current-year fundraising goal is reasonable, or is just “plugged.”</p>

Note: The foundation subscribes to [GuideStar’s](#), Financial Scan tool which provides comparison financial information taken from the 990 tax returns for most non-profit organizations for up to 5 years. Consider generating a Financial Scan report to assist in the evaluation of the financial trends of potential grantees.

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CATEGORY	QUESTIONS TO CONSIDER	KEY INDICATORS	CONCERNS
FUNDING MIX	<p>How would you describe the diversity of your funding mix?</p> <p>What areas, if any, do you seek to change or improve?</p> <p>How?</p> <p>What are your concerns, if any, about your funding picture?</p>	<p>The organization has diversified contributed income, as well as earned income (if appropriate).</p> <p>The fundraising goals (for the organization or the project) and overall budget are realistic based on the economy and past experience.</p>	<p>The E.D. and board member(s) cannot articulate their funding mix.</p> <p>The organization is overly dependent on one source of funding.</p> <p>The organization has had a difficult time meeting the public support test and maintaining its public charity status.</p>

Determine an organization's dependence on any single source by looking at the revenue line items as a percentage of organization's total expenses.

Public support test is a formula established by the IRS; grantees should understand this issue and track its support to ensure that it is not in danger of losing its public charity status.

PROPOSED PROJECT PLANNING & IMPACT

CATEGORY	QUESTIONS TO CONSIDER	KEY INDICATORS	CONCERNS
PROJECT PLANNING	<p>Describe the basis for your approach to this project. What research did you rely upon for your proposed approach?</p> <p>Describe the resources needed to accomplish your goals, and how you plan to obtain them.</p> <p>Geographic target of project.</p> <p>If relevant, discuss the following: Scalability of model Replicability of model Potential for broad impact An innovative approach Stakeholders/Beneficiaries input</p>	<p>The methodology makes sense, given what is considered accepted or best practice in the field.</p> <p>The project design supports the applicant's theory of change (whether consciously articulated or implicit).</p> <p>The project plan allocates appropriate resources (staff, expertise, and money, an appropriate time frame) to accomplish what is anticipated.</p>	<p>The logic model or rationale for the program does not appear reasonable.</p> <p>The approach is outmoded, showing a lack of awareness of developments in the field in recent years.</p> <p>Little or no engagement of beneficiaries in planning</p>

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CATEGORY	QUESTIONS TO CONSIDER	KEY INDICATORS	CONCERNS
<p>PROJECT OUTCOMES</p>	<p>What are the goals and outcomes identified for this project?</p> <p>Describe your organization’s greatest strengths in terms of your capacity to achieve your intended outcomes.</p> <p>What significant challenges inhibit your ability to achieve your intended outcomes?</p>	<p>Desired outcomes are plausible and aligned with mission & strategy.</p> <p>Goals are realistic and achievable within the grant period.</p> <p>The resources available are appropriate, and the cost of the program will result in a reasonable impact.</p> <p>Outcomes are SMART: specific, measurable, achievable, realistic and time sensitive.</p>	<p>Project plans are overreaching — goals are too ambitious or resources available are clearly insufficient to reach the goals.</p> <p>The outcomes are not in alignment with the theory of change for the project.</p> <p>The cost-benefit analysis is unacceptable (i.e., it is not worth the expense for the anticipated impact).</p>
<p>EVALUATION</p>	<p>How do you evaluate your programs? What tools do you have in place?</p> <p>How do you incorporate what you learn into your ongoing and future work?</p> <p>What is the plan for evaluation for this project?</p> <p>What resources are allocated for evaluation in the project budget?</p>	<p>Organization knows what it accomplishes and can articulate how it will apply what it learns.</p> <p>If outcomes are not achieved, leaders can explain why and have strategies to improve ability to meet outcomes.</p>	<p>Organization has little or no understanding of the value of tracking its outcomes.</p>

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OTHER

CATEGORY	QUESTIONS TO CONSIDER	KEY INDICATORS	CONCERNS
COMMUNICATIONS	Who do you consider your key audience(s)? Organizationally? Proposed Project?	The organization has a clear message to communicate about its work and role in the community.	Lack of awareness of the need to communicate.
EXTERNAL RELATIONSHIPS	What partnerships or collaborations are you involved in? What role do you play?	The organization looks for ways to collaborate, and engages in creative partnerships.	Lack of involvement in or awareness of key networks or coalitions.
PROJECT STAFF	Who are the staff members responsible for the proposed project? What are their backgrounds and qualifications?	There is sufficient staff with the skills and experience to do what the organization says it will do.	The key project staff do not have the necessary experience and/or training to do the job.
CAPITAL PROJECTS	Why is the new facility needed? What is the square footage and the cost per square foot? Change to ongoing operational expenses? Other Items to consider : Site selection, Environmental impact, Impact on other foundation priorities Disposition of existing space		
COMMUNITY COLLABORATION	How involved is your organization? In the field? In the community?	Actively engaged with community/regional partners. Regularly shares with others.	Insular approach. Not aware of other similar projects or organizations. Project overlaps or duplicates efforts already available.

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NEXT STEPS

At the close of a Due Diligence interview, consider the following set of items to wrap up the meeting:

1. Review the information grantee needs to get back to you about (or vice versa).
2. Communicate intention to follow-up with additional questions.
3. Communicate intention to interview other project partners.
4. Ask if grantee has any questions.
5. Ask if anything was missed or should have been asked.
6. Communicate timeline of Board decision and notification.

REFERENCES & RESOURCES

[The Due Diligence Tool](#) | Grantmakers for Effective Organizations

[Due Diligence Done Well](#) | Grantmakers for Effective Organizations & La Piana Consulting