

What Does Effective Due Diligence Look Like?

Due diligence is a process that helps grantmakers get to know grantseekers. Typically, it's seen strictly as a means to ensure an organization's financial and legal compliance. However, when done well, due diligence has the potential to provide insight into such critical attributes as the role of the organization's board, the position the nonprofit holds in its field and community, and the level of alignment between our own mission and the goals of the grantseeker. The difficult part of due diligence is in asking the right questions and in a way that makes the most of the nonprofit's time and resources. Efficient due diligence efforts avoid overburdening nonprofit staff with excessive and difficult to navigate applications and forms that provide little value. This piece provides an overview of what it takes to carry out an effective due diligence process.

Due diligence refers to the process through which a grantmaker learns more about an organization's financial and organizational health, mission, priorities and strategies to help to guide a grantmaking decision. This process is essential for grantmakers who leverage information from grantseekers to assess organizations and recommend grants to boards or decision-making committees. If done inefficiently, due diligence leaves nonprofits with overwhelming and redundant questions and forms. Even worse, a poorly designed due diligence process may not provide grantmakers with the information that can give a true picture of the grantseeking organization. When we take the time to design a more efficient and thoughtful process, due diligence benefits both grantmakers and grantseekers.

There are three key questions a due diligence assessment helps answer:

- How well do the organization's proposed activities align with the grantmaker's guidelines and priorities?
- How well do the activities advance the field, provide needed services or generate new learning?
- How does it compare to the other proposals?

For more on this topic, see, [Due Diligence Done Well: A Guide for Grantmakers](#) (Washington, D.C.: GEO, 2010).

Depending on the history and status of the organization, there may be additional questions beyond the proposal that would be helpful to answer. For instance: Does the organization have a successful track record — or, if it is a startup, does it have the leadership and capacity to achieve its goals? Does it operate under an appropriate governance structure?

These relevant and narrow questions help us understand whether an organization can succeed in reaching desired goals. While due diligence will not prevent the failure of an organization or a project, it can ensure that our staff has a solid understanding of the various strengths and challenges a proposal presents.

The Benefits

Taking the time to design an effective due diligence process can significantly improve the way we operate and interact with grantseekers. Some commonly reported benefits include:

- **Added confidence.** Due diligence allows us to make funding decisions based on a deeper understanding of how each grantseeking nonprofit operates and its larger strategies.
- **Greater alignment.** This knowledge provides us with an understanding of a grantseeker's planned activities and goals and how they apply to our grantmaking strategy.
- **More transparency.** Due diligence is a two-way street, providing us with a window into the grantseeker's capacity to achieve its goals as well as giving grantseekers an understanding of our funding interests and how grantmaking decisions are made.
- **Better relationships with grantees.** A thoughtful approach to due diligence can lay the groundwork for a stronger relationship with grantseekers and grantees.
- **Better insights into the issues facing nonprofits and the communities they serve.** In the course of due diligence work, we learn more about what is really happening on the ground with the issues and communities we care about.

Four Things to Think About

Here are a few rules of thumb to guide the due diligence process:

- **Communicate at every turn, with every grantseeker.** This means explaining the due diligence process, its purpose, the steps and associated expectations to all grantseekers prior to its start. This also

includes transparency about our financial and time restraints and following up with grantseekers with the results of the process in a timely manner.

- **Remember that due diligence is the first step in a long-term relationship.** By taking the time to help the grantseeker see that we have a strong sense of the issues their organization is working on and the challenges they are facing, and respecting (and learning from) the expertise of their staff and leadership, we open the door to a more reciprocal and authentic relationship.
- **Imagine each step through the grantseeker's eyes.** Thinking about how every step of the due diligence process can help, hinder and impact grantseekers will inject a sense of empathy in the due diligence process that can benefit grantmakers and grantseekers alike.

Due Diligence Priorities

Below is a compilation of some of the key types of information to gather during the process:

- **Organizational history and track record:** This includes reviewing the history and track record of an organization, as well as learning about its key milestones, to help develop a solid understanding of the sustainability of its programs and operations.
- **Governance and executive leadership:** Understanding how the board functions and how it collaborates with the executive director can give important insights into how the organization operates.
- **Organizational vision and strategy:** The board, executive director and staff should have a shared understanding of what their work is about, where it is leading them and their constituents, and what core strategies they are following to reach their goals. It is helpful to know that the organization's work is founded on realistic goals, proven tactics and strategies that are feasible, given the resources and the capabilities the organization brings to its work.
- **Human resources:** Grantmakers should have confidence in the organization's overall management structure. Attributes to look for include: clear job descriptions, logical lines of reporting for staff and investments in staff training and development.
- **External communications:** As part of due diligence work, grantmakers may want to explore whether the organization has a clear sense of its audience, a clear message to communicate about its work and its role in the community, and an appropriate communications plan for doing so.

- **Relationships and networks:** Board members and staff leaders should understand their organization's position in the field and where there are formal and informal opportunities to cooperate with others.
- **Financial health:** The due diligence process provides a review of a nonprofit's broader financial strategy and plan. This includes their systems for developing realistic budgets, their capacity to monitor those plans through accurate, timely reports that compare budgets to actual financial performance, any potential cash flow challenges and whether or not they maintain sufficient financial reserves.
- **Planning, outcomes and evaluation:** In general, the organization should have a plan for evaluating its progress and applying what it learns. For unrestricted grants, learning and evaluation measures should be in place to assess overall progress towards the organization's mission and capacity building goals. For project-based grants it is important to know that the project methodology is sound, that the work is aligned with the organization's mission, strategy and theory of change, and that the project plan allocates sufficient resources and an appropriate time frame to accomplish project goals.

Conclusion

Whatever the size or type of grant at stake, due diligence when done well has the potential to provide grantmakers a deeper understanding of the nonprofits operating within similar fields of interest. When designing your process, consider some of these comments from nonprofit leaders who found a process useful:

- "It was easy to find the information and documents they asked for. We didn't have to create a lot of new material just for them."
- "It was clear from the start what they wanted from us and what criteria they would be using to make their decision."
- "I knew how long it would take and understood the likelihood that we would get the grant."

By providing insight into a nonprofit's strengths and weaknesses, grantmakers and grantseekers can begin to engage in honest conversations about how to best support the realization of shared goals.