

RAISING THE BAR ON YOUR FINANCIAL MANAGEMENT

“Understanding Nonprofit Financial Statements”

Presented by:

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Today's Goals



- Understand the financial statements used by NPO's
- Reporting requirements / options – *audit v. review v. compilation*
- What options do organizations have? These are YOUR financial statements!
- Understand what they tell us (and don't) – *focus areas*
- Budgeting pitfalls
- What's new?
- Tips for management & board members



PURPOSE?

- Tell a story about the organization
- Picture of where you are
- Picture of what happened – financially
- Picture of how you got there
- Where you are going?



Key considerations

- Who will be reading the statements?
- What will they be looking for?
- What do you want them to see?



Audits, Reviews & Compilations

■ Audits

- Highest level of service
- 3rd party confirmation & testing of transactions
- Requires independence from CPA
- Required in NH if annual revenues > \$1m
- May be required by users
- No “abridged” version of an audit
- NPO’s with annual revenues > \$500k require GAAP statements (not an audit)



Audits, Reviews & Compilations

■ Reviews

- Primarily analytic and predictive procedures
- Independence required by CPA
- No third party confirmation

■ Compilations

- Internal financials dressed up
- No testing performed on figures
- Independence not required



Considerations

- Needs of users
- Need for comparative statements
- Alternatives to full disclosure GAAP F/S
- Independence



What are these things called financial statements?

- Statement of Financial Position
(for profit equivalent = Balance Sheet)
- Statement of Activities
(for profit equivalent = Income Statement)
- Statement of Cash Flows



Other Statements

- Statement of Changes in Net Assets
(For profit equivalent to Net assets = Retained earnings)
- Statement of Functional Expenses



Relationships

- Statement of Financial Position – assets and liabilities at a single point in time
- Statement of Activities – financial activity over a period of time
- Cash flows – sources and uses of cash over a period of time



Statement of Financial Position (Balance Sheet)

- Snap shot – single point in time
- Assets of the organization – what it owns
- Liabilities of the organization – what it owes to others
- Net assets – what is left over



Assets

- Current assets
- Property, plant and equipment
- Investments (recent changes to endowment funds)
- Other assets
- Liquidity
- Classified vs. non-classified statement



Basic Principles

- Cost vs. fair market value
- Conservatism
- Accrual vs. cash basis



Liabilities

- Current liabilities
 - Accruals
 - AP
 - LOC
 - CMLTD
- Long-term liabilities
 - LTD
 - Deferred revenue



Net assets

- Unrestricted
- Temporarily restricted
- Permanently restricted
- Will discuss later



Statement Examples (handouts)

- Example #1 – Care Ministry Centers, Inc.
 - *Classified, comparative, single column*
- Example #2 – Green Mountain College
 - *Classified, comparative, single column, PP&E*
- Example #3 – Rolling Hills Scouting Council
 - *Classified, by Fund, single year, 2 pages*
- Example #4 – Cherished Child Homes
 - *Unclassified, comparative, single column*



Statement of Activities

- Activity over a period of time – one year, one month, one quarter
- Income statement – revenue and expenses
- Unrestricted
- Temporarily restricted
- Permanently restricted
- Format options - examples



Restrictions



- Time restrictions
- Purpose restrictions
- Restrictions always come from the donor
- Board designated (NOT restricted)
- Release from restriction
- Donor (and development) education



Revenue

- Variety of sources
- Gifts
- Grants
- Operations
- Sale of merchandise
- Investment appreciation and I&D
- In-kind
- Unrelated business



Expenses

- Program
- Fundraising
- Administration



Change in net assets

- “Profit”
- Reconciliation of net assets at beginning and end of the year (by restriction)



Statement Examples (handouts)

- Example #1 – Care Ministry Centers, Inc.
 - *Columns by restriction, comparative totals*
- Example #2 – Green Mountain College
 - *Single column, comparative*
- Example #3 – Rolling Hills Scouting Council
 - *Columns by Funds, single year presentation*
- Example #4 – Cherished Child Homes
 - *Columns by Restriction, comparative totals, 2 pgs*



Statement of Cash Flows

- Cash activity over a period of time
- Cash flow provided by/used in operations
- Cash flow provided by/used in investing activities
- Cash flow provided by/used in financing activities



Operating cash flow

- Reconciles change in net assets (“profits”) with change in cash
- Effect of changes in current assets and current liabilities
- Do you have a positive cash flow from your core business or are you financing operations? *See Green Mountain Example*



Investing activities

- Effect on cash flow of buying and selling:
 - Investments
 - Property, plant and equipment



Financing activities

- Effect on cash flow from:
 - Borrowing
 - Repaying debt



Other Financial Statements

- Statement of Changes in Net Assets
 - typically part of Statement of Activities

- Statement of Functional Expenses
 - Allocation guidelines (handout)



Statement Examples (handouts)

- Example #1 – Care Ministry Centers, Inc.
- Example #2 – Green Mountain College
 - No add'l stmt – more detail in stmt of activities
- Example #3 – Rolling Hills Scouting Council
- Example #4 – Cherished Child Homes
 - Subtotal for personnel costs, depreciation separate



Analytic Tools - Profitability

- Components of income statement
- Revenue sources
 - Operations vs. gifts vs. investments
- Expenses
 - Program vs. fundraising vs. administration
- Profitability
 - Business segments



Analytic Tools - Profitability

- Comparative
 - To prior year
 - To budget
 - To industry
- Techniques
 - Absolute dollars
 - Trends
 - Ratios

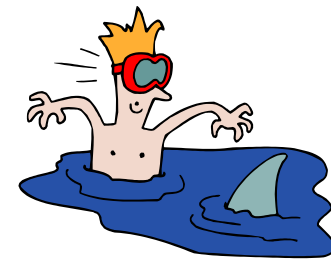


Analytic Tools – Financial Strength

- Liquidity
 - Current ratio
 - Quick ratio
- Debt usage
 - Short-term vs. long-term
 - Leverage
 - Debt vs. equity
 - Debt vs. total assets



Danger Signs



- “Nonprofit syndrome”
- Not understanding what makes money and what doesn’t
- Not controlling administrative expenses
- Inadequate return on fundraising expense
- Misuse of debt



Roles and Responsibilities

- Board
 - Overall fiduciary responsibility for the organization
 - Hiring top management
 - Approve budget
 - Monitor results
 - Hire auditor



Roles and Responsibilities

- Management
 - Day to day operations
 - Fiscal management
 - Prepare budget
 - Systems and procedures
 - Report results



Roles and Responsibilities

■ Auditor

- Report to the Board (SAS 114)
- Examine financial statements for compliance with GAAP – “Auditor’s Opinion”
- Report weaknesses in procedures and controls to the Board– SAS 112/115 Letter and Management Letter
- Differences between audit report and internal financials



Budgets



- Cash Flow vs. P&L budget
- Depreciation
- Restricted giving impact
- Modifying (working budget)
- Zero-based budgeting vs. surplus
- Conservatism



Other Issues

- Financial statement footnotes
 - Does wording make sense?
 - Explanatory items (strategic plans)
 - Many new disclosure requirements
 - Included in SAS 112/115 requirement for financial expertise
- Financial statements vs. 990
- A-133 audit

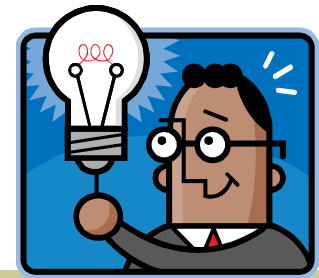


What's New?

- Form 990
 - Major redesign effective for 2008
 - Increased 990-EZ thresholds
 - Start these procedures now!
- UPMIFA and 117-1 disclosure
 - Endowment funds
 - New state interpretations
 - Substantial new disclosure
- FAS 157 Fair Value disclosure
 - Management assessment of FV
 - Substantial new disclosure

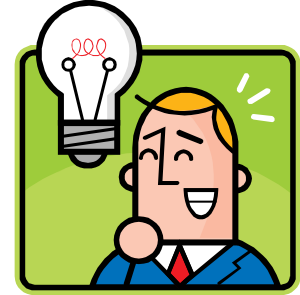


Tips for Board Members



- Ask Questions!
- You have a fiduciary responsibility to understand your financial statements – not just the FC
- Request cash projections – how much cash do you need for your operations?
- If AR is significant - understand collection issues
- Be aware of internal controls and how you may be a part of it (whistleblower policy)
- Know what relationships are typical for your type of organization – trends/ratios

Tips for Management



- Provide a narrative summary of financial results (dashboard)
- Provide financial information at least 7 days before the meeting
- Provide comparisons to budget and/or prior year results
- Graphs are great!
- Request training from external auditors
- Repetition is ok

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