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Building on Success Cohort Learning Session 1: **Financial Management**

November 21, 2019

Welcome



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Welcome to the Financial Management Cohort Learning Session

Before the session begins:

- ✓ **Take a moment with your BOS Team to write your organization's mission in 3 words on your name tent card.**

Throughout today's session when you participate, you will be asked to share your name and your organization's three word mission.



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Building on Success Cohort Learning Session 2: Financial Management

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November 21, 2019

What do you want to learn?



Agenda Overview

1. Welcome and Introductions
2. Agenda Overview
3. Understanding and Monitoring
Dinner and Networking
4. Planning
5. Communicating
6. Governance and Financial Management
7. Resources, Upcoming Strategic Planning, & Wrap-Up

How We Will Work Together

Norms	Outcomes
<p data-bbox="208 601 813 644">How we will work together</p> <ul data-bbox="208 715 877 1158" style="list-style-type: none"><li data-bbox="208 715 722 758">• Begin and end on time<li data-bbox="208 772 691 815">• Attend every meeting<li data-bbox="208 829 498 872">• Share ideas<li data-bbox="208 886 556 929">• Active listening<li data-bbox="208 943 877 986">• Collaboration (among groups)<li data-bbox="208 1001 683 1100">• Be vulnerable, share weaknesses<li data-bbox="208 1115 542 1158">• Confidentiality	<p data-bbox="967 601 1663 701">Tangible results your organization hopes to achieve</p> <ul data-bbox="967 772 1692 1272" style="list-style-type: none"><li data-bbox="967 772 1450 815">• Draft a strategic plan<li data-bbox="967 829 1257 872">• Fundraising<li data-bbox="967 886 1441 929">• Tools for onboarding<li data-bbox="967 943 1692 1100">• Staff: when to hire, how to sustain, admin costs for staff vs. for programs<li data-bbox="967 1115 1673 1158">• Scaling up a small organization<li data-bbox="967 1172 1663 1272">• Learn how to manage a board, run productive meetings

What is Financial Management?

- Systematic accumulation of accounting data
- Reporting on current position
- Planning for future activities

Chart of Accounts

- How the organization's financial information is organized
- Basis for coding all transactions and budgets
- Unified Chart of Accounts as starting point
- Includes: Assets, Liabilities, Net Assets, Revenue, and Expenses

Accounting Software

- QuickBooks is most common among small organizations
- Available in both on premise and online versions (TechSoup)
- Provides for greater efficiency, reliability and transportability of financial data

Internal Controls

Internal controls are a set of policies and procedures to prevent deliberate or misguided use of funds for unauthorized purposes.

Internal Controls – Key Principles

1. Segregation of duties
 - no accounting process is handled by one person from beginning to end
 - bank statement reconciliation
 - two signatures on checks over \$ limit

Internal Controls – Key Principles cont.

2. Physical controls over assets

- Checks
- Cash
- Equipment

3. Transparency

- Communicating financial information on a timely basis

Policies and Procedures

- Should be clearly documented and easily understood by “outside” individuals
- Realistic to maintain
- Listed by job title
- Cite relevant forms
- Indicate appropriate timeframes

Standard Financial Statements/Reports

1. Statement of Activities (P&L, profit & loss statement)
2. Statement of Financial Position (Balance Sheet)
3. Statement of Cash Flows
4. Statement of Functional Expenses

Standard Financial Statements/Reports - Continued

5. IRS Form 990
6. Annual organization budget
7. Other internal financial statements (year to date budget performance)

1. Statement of Activities

- Identifies the source and use of funds for a specific period of time
- Indicates whether there is a surplus or loss for that period of time

Q: What has our overall financial performance been this month and to date?

Sample Statement of Activities

STATEMENT OF ACTIVITIES
For the year ending December 31, 2019

	Without Donor Restrictions	With Donor Restrictions	Total
REVENUES AND OTHER SUPPORT			
Contributions	673,493	200,035	873,528
Government Contracts	167,754		167,754
Program Fees	15,841		15,841
Interest	87		87
Net assets released from restriction	214,693	(214,693)	0
Total Revenue and Other Support	1,071,868	(14,658)	1,057,210
EXPENSES			
Program	847,436		847,436
Management & General	111,056		111,056
Fundraising	78,230		78,230
Total Expenses	1,036,722		1,036,722
Change in Net Assets	35,146	(14,658)	20,488
Net Assets at beginning of year	196,960	107,243	304,203
NET ASSETS AT END OF PERIOD	232,106	92,585	324,691

Cash-Basis vs. Accrual-Basis Accounting

	Cash Basis	Accrual Basis
Income recorded when...	Cash is received. (Deposit)	Income is earned or promised. (<u>Receivable</u>)
Expenses recorded when...	A check is written (Expenditure)	An obligation is incurred. (<u>Payable</u>)

Cash vs. Accrual?

	Advantages	Disadvantages
CASH BASIS	Easy to understand Fewer transactions	Not GAAP compliant Incomplete picture
ACCRUAL BASIS	GAAP Compliant More meaningful data	Harder to understand More transactions
MODIFIED BASIS	Use easier method for internal interim reporting	Audit looks different from internal statements; may lead to surprises

2. Statement of Financial Position

- Lists all an organization's assets (what it owns), liabilities (what it owes) and resulting net assets
- $\text{Assets} - \text{Liabilities} = \text{Net Assets}$
- Net assets are broken down into two categories -
With Donor Restrictions and Without Donor Restrictions

Q: What is our financial health? Can we pay our bills?

Sample Statement of Financial Position

BALANCE SHEET As of December 31, 2019

	<u>2019</u>
ASSETS	
Cash and cash equivalents	358,953
Accounts Receivable	2,700
Contributions Receivable	77,500
Property and Equipment	8,855
Prepaid Insurance	10,756
Security Deposit	1,460
Total Assets	<u>460,224</u>
LIABILITIES	
Accounts payable	73,533
Refundable Advances	62,000
Total Liabilities	<u>135,533</u>
NET ASSETS	
Without donor restrictions	232,106
With donor restrictions	92,585
Total Net Assets	<u>324,691</u>
TOTAL LIABILITIES AND NET ASSETS	<u><u>460,224</u></u>

Accounting for Contributions

- Unrestricted – May be used for any purpose within the organization's mission
- Restricted – May only be used in the way the donor allows. What matters is the intention of the donor...

Only a donor can restrict. The Board can designate.

Types of Restrictions

- Temporarily Restricted - Funds that have donor-imposed conditions or restrictions that are reasonably expected to be met by the organization (time or purpose).
- Permanently Restricted - Funds that carry donor restrictions as to their use which can never expire. (Typically an endowment.)

How Do Your Net Assets Change?

Income – Expenses = Change in Net Assets

Your net assets increase if you have more income than expenses.

Your net assets decrease if you have more expenses than income.

3. Statement of Cash Flows

- Reconciles the organization's beginning of year cash balance with the end of the year balance.
- Typically includes cash provided or used by:
 - operating activities
 - financing activities
 - investing activities

Sample Cash Flow Statement

STATEMENT OF CASH FLOWS
For the year ending December 31, 2019

CASH FLOWS FROM OPERATING ACTIVITIES	
Change in net assets	20,488
Adjustments to reconcile change in net assets to cash provided by operating activities:	
Depreciation	6,445
Increase (decrease) in cash arising from changes in assets and liabilities:	
Accounts receivable	4,450
Contributions receivable	9,900
Prepaid insurance	403
Security deposit	250
Accounts payable and accrued expenses	(48,753)
Refundable advances	62,000
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>55,183</u>
CASH FLOWS FROM INVESTING ACTIVITIES	
Equipment purchases	<u>(3,084)</u>
NET CASH USE BY INVESTING ACTIVITIES	<u>(3,084)</u>
CASH FLOWS FROM FINANCING ACTIVITIES	
Proceeds from (payment of) short-term debt	<u>(75,000)</u>
NET CASH PROVIDED BY (USED BY) FINANCING ACTIVITIES	<u>(75,000)</u>
NET DECREASE IN CASH AND CASH EQUIVALENTS	<u>(22,901)</u>
CASH AND CASH EQUIVALENTS - beginning of year	<u>381,854</u>
CASH AND CASH EQUIVALENTS - end of year	<u>358,953</u>

4. Statement of Functional Expenses

- Reports all expenses by their natural classification (i.e., salaries, supplies, rent, etc.)
- Typically separates program and administrative expenses

Sample Statement of Functional Expenses

STATEMENT OF FUNCTIONAL EXPENSES For the year ending December 31, 2019

	Program Services	General and Administrative	Fundraising	Total
Salaries	529,983	43,385	48,678	622,046
Payroll taxes	43,177	3,539	3,971	50,687
Employee benefits	37,079	3,039	3,410	43,528
Audit and accounting	0	38,120	0	38,120
Facility fees	15,257	0	0	15,257
Depreciation	5,490	450	505	6,445
Education and staff training	17,288	1,417	1,589	20,294
Furniture and equipment	11,620	951	1,069	13,640
Insurance	11,242	921	1,034	13,197
Interest	0	1,784	0	1,784
Materials and supplies	17,368	538	603	18,509
Meeting costs	17,726	1,470	2,493	21,689
Miscellaneous	2,165	7,189	76	9,430
Postage	463	37	43	543
Professional Fees	62,910	2,549	7,405	72,864
Printing and advertising	51,224	3,730	5,184	60,138
Rent	15,114	1,239	1,390	17,743
Repairs and maintenance	255	22	23	300
Telephone	5,537	454	509	6,500
Travel and transportation	3,538	222	248	4,008
TOTAL EXPENSES	847,436	111,056	78,230	1,036,722

Using Your Financial Statements: Key Financial Indicators

- Variance (or trend) analysis
- Ratio analysis
 - Current Ratio
 - Quick Ratio
 - Day's Cash
 - Management & General %

Current Ratio

Do I have enough **ASSETS** to cover my **Liabilities**?

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

Hint: A current ratio of less than 1.0 indicates that the organization may not have sufficient current assets to meet current payment obligations.

Quick Ratio

Do I have enough cash to pay my bills?

$$\text{Quick Ratio} = \frac{\text{Cash} + \text{Cash Equivalents}}{\text{Current Liabilities}}$$

Hint: A quick ratio of less than 1.0 indicates that the organization may not have sufficient current assets to meet current payment obligations.

Day's Cash on Hand

$$\text{Day's Cash} = \frac{\text{Cash} + \text{Cash equivalents}}{\text{Operating Expenses}/365}$$

If not another penny of income was received, how many days could the organization continue to pay its' bills?

Management and General Percentage

Management

And General % = $\frac{\text{Mgmt. and General Expense}}{\text{Total Expenses}}$

Hint: appropriate range

Group Exercise: Using Financial Statements

Instructions:

- ✓ Review the provided financial statements
- ✓ With your table, answer the following questions -
 1. How financially healthy is this organization?
 2. What concerns might you have?
 3. Do you think they are able to meet their financial obligations?
 4. What questions would you ask to find out more?
- ✓ Share observations with large group

5. IRS Form 990

Filing guidelines:

	Form to File
Gross Receipts less than or equal to \$50,000	990-N (e-postcard)
Gross Receipts less than \$200,000 Total Assets less than \$500,000	990-EZ or 990
Gross Receipts greater than \$200,000 Total Assets greater than \$500,000	990

6. Annual Organization Budget



Will talk about budgets and process later...

Audits

- An “audit” refers to a set of financial statements that have been audited by a Certified Public Accountant.
- The purpose is generally to provide assurance to third parties (funder, regulator, etc.)
- The objective is the expression of an opinion on the accuracy of financial statements and their conformity with GAAP

Audit cont.

- Examines and tests supporting documentation
- Tests adherence to internal control policies
- Verifies asset and liability balances
- Includes a management letter

What triggers an audit?

Legal requirements

- State of Connecticut
 - 1) Department of Consumer Protection - \$500,000 in gross revenue (specific definition)
 - 2) State Single Audit Act - \$300,000 of state money expended
- Federal - \$750,000 in federal contract dollars expended

What triggers an audit? Cont.

Best practice guidelines

- Wise Giving Alliance - \$1 million in gross income
- Standards of Excellence Institute - \$500,000 in gross income
- Independent Sector - \$1 million in gross income

Funder Requirements

Alternatives to an audit

Review – Similar to an audit, but only provides limited assurance by the auditor, limited internal control testing and no verification of balances

Compilation – presents the financial statements in GAAP format, but provides no assurance for accuracy, etc. (basic restatement of organization produced numbers)

DINNER – Networking Challenge

- Change your table for dinner
- Meet one new person
- Find out about their organization and what inspired them to get involved

Cost Allocation

- Common (or shared) costs are expenses that are not easily identifiable with a single function.
- Cost allocation is the process of assigning the cost among two or more activities/programs.
- A cost allocation plan is written documentation of methods used to allocate costs

Common Cost Allocation: Step 1

Categorize Expenses

Program: Program staff, program materials

Administrative: finance staff, audit expense, board meeting expenses

Fundraising: development staff, event expenses

Common Costs: rent and utilities, computers, office supplies, receptionist

Common Cost Allocation: Step 2

Choose Allocation Method

Frequently used cost allocation rates:

1. FTE
2. Payroll
3. Square Footage

Common Cost Allocation: Step 3

Allocate Shared Costs

1. Line by Line Method

-- a different rate of usage for each line item, or groups of line items

2. Bottom Line Method

-- all shared costs are grouped together and one allocation rate is used

Capitalization and Depreciation

Capitalization means that:

- an item has a useful life of more than one year
- the item is recorded as an asset when purchased rather than expense

Capitalization and Depreciation

Depreciation is the process by which the cost of a capitalized item is recorded over the useful life of the item

The value of the asset is reduced each year due to wear and tear, age or obsolescence

Budgeting

- The budget is an organization's annual financial plan that translates organizational goals and objectives into dollars
- Two purposes:
 1. Project income and expenses
 2. Monitor actual results against projections

ROAD MAP

Types of Budgets

- Line item
- Program-based Budget
- Capital Budget

10 Step Budgeting Checklist

(from Nonprofits Assistance Fund)

1. Determine timeline
2. Agree on goals
3. Understand current financial status
4. Agree on budget approach
5. Develop draft expense budget
6. Develop draft income budget

10 Step Budgeting Checklist cont.

(from Nonprofits Assistance Fund)

7. Review draft budget
8. Approve budget
9. Document budget decisions
10. Implement budget

Budgeting Strategies

- Budgeting for a surplus
- Surplus vs. reserves
- Funding depreciation
- Methods? Zero-based? Income? LY Comparison?

Monitoring the Budget

- Monthly budget comparisons
- YTD budget comparison
- Budget revisions/mid-course corrections

Managing Cash Flow

- Appropriate use
- How to think about it
- Credit cards – fraud, can't be used to fill gaps

Telling Your Financial Story

- What does the board need to see on a regular basis? Sample report to board...
- Communicating with funders
- Budget narratives

Group Exercise: Telling Your Financial Story

Instructions:

- ✓ Using the provided template, work with your team to complete a financial narrative for your organization
- ✓ Identify 2-3 questions that someone reading your narrative might have
- ✓ Share your organization's financial narrative with the other organization at your table

Sidetrack: Technology

- If time... talk about some technology resources
- Techsoup www.techsoup.org
- Idealware www.idealware.org
- NTEN www.nten.org

Governance and Financial Management: Ten Basic Board Responsibilities

1. Determine mission and purposes, and advocate for them
2. Select the chief executive
3. Support and evaluate the chief executive
4. Ensure effective planning
5. Monitor and strengthen programs and services
6. **Ensure adequate financial resources**
7. **Protect assets and provide financial oversight**
8. Build and sustain a competent board
9. Ensure legal and ethical integrity
10. Enhance the organization's public standing

Fiduciary Duty and the Nonprofit Board

- Fiduciary definition: of or relating to a holding of something in trust for another
- Board members must always act for the good of the organization and exercise reasonable care in all decision making without placing organization under unnecessary risk.

Three Fundamental Fiduciary Duties of a Nonprofit Board

- Duty of Care
- Duty of Loyalty
- Duty of Obedience

How does a Nonprofit Board Fulfill Its Fiduciary Duty?

- FINANCIAL DIRECTION
- OVERSIGHT

Prepare, Approve, and Monitor the Budget

- Develop a budget with projected income and expenses
- Approve the budget before the fiscal year begins
- Monitor income and expenses monthly using clear and understandable financial reports
- Ensure adequate cash to meet financial obligations (make payroll)
- Compare budget-to-actual
- Review and approve a year-end financial report

Guard Assets With Adequate Financial Controls

- Establish written financial management policies
- Define financial and accounting procedure (signing checks, handling cash, approving expenses, using credit cards)
- Establish a clear policy to manage potential conflicts of interest
- Request regular audits (if required)

Oversee Legal Obligations

- Verify that all filing requirements and tax obligations are completed (Form 990, tax payments (employment and others))
- Ensure that required reports are submitted to funders

Who's Responsible for Financial Direction and Oversight?

- Board
- Treasurer
- Finance Committee
- Staff

Role of the Finance Committee

- Develop an annual operating budget for board approval
- Identify and develop financial reports needed by the board for regular review and ensure that reports are accurate and timely
- Monitor on a regular basis adherence to the budget
- Report to the board any financial irregularities, concerns, opportunities
- Develop and recommend financial policies to be adopted by the Board
- Ensure that financial policies are being followed
- Recommend to the board whether the organization should have an audit. If so, select the auditor and work with the auditor, unless there is a separate audit committee
- Ensure sound management and maximization of cash and investments
- Maintain appropriate insurance coverage (i.e. directors and officers coverage (D & O) and general liability coverage)

Role of the Treasurer

- Attend all board meetings
- Maintain knowledge of the organization and personal commitment to its goals and objectives
- Serve as the chair of the finance committee
- Manage, with the finance committee, the board's review of and action related to the board's financial responsibilities
- Ensure that appropriate financial reports are made available to the board on a timely basis
- Regularly report to board on key financial events, trends, concerns and assessment of fiscal health
- Present the annual budget to the board for approval
- Recommend to the board whether the organization should have an audit

Why Does Fiduciary Duty Matter?

Because Things Can Go Wrong

- Organizations can drift into financial trouble
- Financial fraud can happen
- Financial resources can be spent ineffectively

What You Can Do

- Ask questions about your organization's finances
 - ✓ Do we receive reliable, timely, and easy to understand financial statements and reports?
 - ✓ What do these financial statements tell us?
 - ✓ How financially health is our organization?
 - ✓ Is there anything of concern?
- Conduct a Financial Management Self-Assessment at your next board meeting
 - ✓ What does your organization do well?
 - ✓ What can your organization do better?

Resources, Next Session and Wrap-Up



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Additional Resources

- Propel Nonprofits
<https://www.propelnonprofits.org/resources/>
- FMA, Fiscal Strength for Nonprofits
<https://fmaonline.net/nonprofit-financial-management/financialresources/>
- Wallace Foundation
<https://www.wallacefoundation.org/knowledge-center/resources-for-financial-management/pages/default.aspx>
- National Council of Nonprofits
<https://www.councilofnonprofits.org/tools-resources/financial-management>



Upcoming Strategic Planning Sessions March 26 and April 30, 2020

- Full-day Sessions at Chrysalis Center
- Begin to assemble your planning team (5-8 stakeholders)
- Look for email from Betsy Johnson in January, with links to strategic planning webinar, reading and pre-work
- Reach out to your consultant for pre-work support !



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Closure / Next Steps

- Please complete feedback forms and leave on table!
- Look for emails with links to Strategic Planning webinar and pre-session readings and pre-work
- Next Session:
Thursday, March 26, 2020: Strategic Planning
- Check the weblink for session materials





Thank You !