OCTOBER 2018

NOT-FOR-PROFIT FINANCIAL RESILIENCE GUIDE

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Financial Health

1. How much money is unrestricted and available for use?	
a) Cash (under current assets – how much is restricted?)	• If your organization receives government funding, the amount of "cash" under current assets in the Statement of Financial Position (Balance Sheet) will be restricted by the same/similar proportion of government funding to donations the organization has. ○ If the NFP only has government funding, cash will be restricted and unavailable for other use
b) Reserves (net assets/fund balances – how much is restricted?)	• Assess the proportion of reserves (net assets or fund balances) that are restricted versus unrestricted/internally restricted and thus available for use
2. How sufficient are reserves?	
a) How many months reserves do you have for emergency purposes? (tip: recalculate target $ goal amount and the actual availability of reserves - annually)	• Does the organization have at least 3 months of operating expenses in an emergency reserve minimum? • Formula to calculate three months of operating expenses: ○ (total expenses / 12) x 3 = $?
b) How much money has been borrowed from reserves? **c) How many months or years has the organization borrowed from reserves?**	• Hopefully none! If the organization has borrowed from reserves, hopefully it was only due to delayed receivable and the money borrowed was returned to the reserves/savings of the organization within the same year. • Withdrawing from reserves and not replenishing the reserves is a sign of risk.
d) How much money is available or accessible for 'opportunities or unfunded needs'	• Calculate how much the organization needs to pay for needs that are not traditionally funded each year (i.e. technology, training, strategic and business planning, evaluation work, etc.) and assess how much is available in the reserves – apart from the money set aside in emergency reserves (to finance these needs each year) • Set a financial target to raise and save money to fund this work on an annual basis.

3. Are there cash flow challenges or deficits?	
a) Know the difference between needing money for cash flow shortages vs. deficits	• This is confusing for some. Note: if your organization receives funding in advance of each period and it still requires access to a line of credit or loan because of shortfalls in cash at any time, the organization may be experiencing a deficit. • If the organization uses a line of credit or a loan because funders pay late, ask them if they can adjust their payment schedule as the organization is paying interest fees to finance the line of credit or loan. • If your organization is accessing a line of credit or loan because of a deficit(s), assess which areas produce the deficit and restructure and/or generate additional revenue.

b) How many fiscal years have ended in an unrestricted surplus?	• Ending the year with a surplus in restricted funds is not helpful if the organization has to return this money to the funder and it means that money granted to the organization was not spent within the year as planned.
	• Ending the year with a surplus in unrestricted funds is good as these funds will be reinvested in the organization!
	    ○ 0 - 2% low amount of surplus
	    ○ 2 – 4% moderate
	    ○ 4 – 6% good

c) What is the variance between projected annual revenue and actual year-end revenue?	• Review the historical variances between projected budget and year-end actual figures. Variances above 10% will be hard to manage at the 4th quarter and the following fiscal year, and dangerous if deficits require money to be taken out of hard-earned reserves. Variances must be managed month to month so that spending can stay in line with revenue generation so that deficits do not occur.
d) Have cash flow challenges and/or deficits required debt (line of credit/loans)?	• Ensure you know the difference between whether the organization required debt to finance a late payment from a funder versus requiring debt to finance a deficit • If a loan/line of credit was not required, great! • If the accountant has had to delay paying bills because there was insufficient cash in the bank, please investigate, as this can be a sign of risk ○ If a line of credit was required for 2 or more months, please investigate as this may be a sign of risk.

e) How many years has the organization had debt?	• If the organization is paid by funders in advance of the period of program delivery and the organization still requires a line of credit or loan, please investigate as this may be a sign of risk o If the organization has accessed a loan/line of credit for >5% in the past 3 years, please investigate as this may be a sign of risk
f) How many years has the organization borrowed from reserves?	• If the organization has not been asked/told by CRA to draw down on its large amount of reserves and has borrowed from reserves, please investigate as this may be a sign of risk o If your organization has accessed a loan/line of credit for 1 or more years, please investigate as this may be a sign of risk
g) Has the auditor indicated that there are insufficient revenues to finance the organization's expenses to the end of the fiscal year? Has the auditor given a "going concern" opinion?	• If yes, this is a very serious risk and must be investigated and remedied immediately
4. Are receivables flexible, timely and reliable?	
a) How much of funded expense lines do you have flexibility with?	• Having some flexibility to move funding between lines aids resilience and adaptation • Even if your funder has not traditionally allowed this type of flexibility, do not hesitate to ask if you feel that the organization can be more effective or efficient if some funding was moved between expense lines.
b) Is the payment schedule for funding appropriate?	• Funders may not know the appropriate funding schedule required by your organization. For new programs conduct a cash flow and before taking on any new funding. For existing programs, conduct a cash flow forecast to assess if the funding payment schedule is still adequate.
c) Are gift promises / pledges from donors reliable?	• In times of economic uncertainty, rising interest rates or unemployment, individuals may curb their giving. Ensure that gift promises and pledges from donors are reliable.

<table>
<tr><th colspan="2">5. How probable and severe are decreases to revenue expected?</th></tr>
<tr><td>a) Severity depends on capacity to absorb decreases in revenue
Revenue includes funding, earned income, fundraising, fee for service
b) Revenue decreases can be due from:
government cut backs or defunding
economic recessions
changing nature of fundraising from new generations
changing sources of revenue (social media, crowdsourcing, etc.)</td><td>Each organization will have a different level of capacity to absorb decreases in revenue.
Conduct a contingency planning exercise to determine the potential impact from reductions in revenue
Assess each source of revenue and the expected modest, moderate and high reduction of revenue. Next attempt to balance the budget in each of the three scenarios to assess what actions need to be taken to ensure the budget balances in each of those scenarios, if possible.</td></tr>
<tr><th colspan="2">6. How probable and severe are increases to costs expected?</th></tr>
<tr><td>a) Salary increase commitments</td><td rowspan="2">In times of revenue fluctuation organizations must balance both reductions to revenue and expected increases to costs.
Many costs increase each year outside of an organization’s control, some of these costs include: rent/lease, audit fees, insurance, health benefits, hydro and waste management, food costs, etc.</td></tr>
<tr><td>b) Costs that increase that are outside your control; lease/rent, insurance, health benefits, hydro/waste, audit, food</td></tr>
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Financial Practices and Systems

1. A real understanding of true cost and true bottom-line	
a) True and full program costs including administrative allocation are known and captured in reporting	• Ensure that the method for allocating costs is based on true and full cost allocation which includes allocation of administration, accounting, management, operations and facility costs that are used by each program • If this costing exercise is done inconsistently or using inappropriate bases for allocation, the program budget will be incorrect
b) True program budgets and bottom-line are known by management	• It is critical that management know the true costs and true-bottom line of programs as this will allow them to more effectively monitor, manage and adapt to changes in the program
c) The financial bottom-line of programs are known by finance committee and the board (deficit, break-even, surplus)	• It is imperative that the board, finance committee and managers know which programs are in deficit, break-even and surplus so that this can guide their innovation, adaptation response, and allow them to make informed decisions
d) The number of programs in deficit and the $ amount per program is known	
e) The number of years that a program(s) has experienced plateau funding and/or increasing deficits.	• As costs increase outside of your control each year, generating the same amount of revenue is not viable. You will find yourself cutting expense lines every year and restricting the organization from effectively delivering programs.
2. **Financial reports that can produce timely, factual, relevant and easy to understand information**	
a) Financial reports are available a maximum of 30 days after the previous month	• Financial reports that are produced 2 months or more after the month in question do not provide the organization with adequate financial monitoring and oversight
b) The annual budget and calendarized expenses are in the accounting system and not only in Excel	• This is absolutely critical! Ask your accountant if the budget has been inputted in the accounting system for the year and calendarized revenue and expenses for each month so that the organization can receive financial reports with variances that are accurate and so that the organization can effectively and efficiently produce cash flow forecasts.
c) Financial reports include projected budget and actual numbers, and the $ and % variances – and a narrative	• The format of the monthly Statement of Operations (budget report) must include both the projected amount and actual amount so that the board can assess if the organization is on budget, it should also include the $ and % variances so that it can assess and prioritize the variances that are most important to speak to.
d) Restricted funding is tracked and recorded as restricted and used appropriately.	• Restricted funds should always be recorded as such • It is not allowable to use restricted funds for purposes not intended by the funder.

3. The organization completes and submits required documentation on a timely basis	
a) Annual audit is completed on time	• Failure to comply with any one of these items will increase the exposure to risk
b) Funder reports are submitted on time	
c) T3010 / T2 submitted on time	
d) Government remittances submitted on time.	

Financial Stewardship:

1. Recognize that financial literacy and financial stewardship is a muscle that needs to be exercised	
a) The board should receive financial reports monthly, whether they meet or not	• Exposure to the financial statements each month, especially when accompanied by a narrative summary report of the financial performance and progress of the organization will strengthen the ability to integrate understanding of finance in developing strategies and stewarding the organization towards increasing resilience
b) The financial reports include Words not just Numbers (use a narrative report to describe the financial status)	• Include a narrative report that summarizes the organization's performance, outlines the top revenue and expense variances and that also stimulates discussion regarding the viability of the organization in future years.
c) Provide a list of questions that board members can ask so that they feel more comfortable asking questions	• Some board members feel shy about asking the right questions - consider providing them with a list of questions with respect to understanding the financial statements so that they can feel more comfortable in engaging in finance related discussions
d) Make time for a discussion on the current financial position and overall financial health of the organization - where everyone participates (15 minutes minimum).	• Talk about the current financial report, the overall financial health of the organization, the future viability of the organization and how to effectively position the organization for resilience in the future
2. The Board, Finance Committee, Executive Director and Managers understand the true financial position <u>and</u> 3, 5- or 10-year trends of:	
e) Assets - restricted/unrestricted cash, receivables	• Has the proportion of unrestricted cash (in the current asset section of the Statement of Financial Position) grown over this period? That's good! If it has declined, investigate the reasons why, this can be a sign of weakness.
f) Liabilities - bank loans, mortgages, deferred contributions	• Has the organization used bank loans, line of credit increasingly over this period? Why? Are financing tools used to finance the timing of funding or to finance deficits? Financing deficits is a sign of risk.

g) Reserves – unrestricted liquid net assets (or fund balances)	• Have unrestricted/internally restricted net assets (or fund balances) grown over this period? That's good! If it has declined to finance deficits this is a sign of weakness and the reasons for the decrease must be investigated.
h) Revenues – by type/source	• Have revenues decreased by any one or more sources in this period? • Has revenue decreased overall in this period? • Declining revenues on a 3, 5, &/or 10-year basis is a risk, investigate.
i) Expenses – costs rise each year due to external forces…	• Has the organization been forced to go into debt, restructure, cutback on necessary expense lines due to rising costs and insufficient revenues? • Consider restructuring programs and operations, seek economies of scale, generate additional revenues if possible and balance budgets before taking on more debt to finance deficits.
j) Annual surplus, deficit, or break-even	• Is the annual bottom-line trend positive or negative? • If deficits are common and if they are increasing, this is a sign of risk
3. The Board and Finance Committee Members, Executive Director and Managers understand the true bottom line of programs	
k) The true full cost and bottom-line of programs is considered in decision making about funded programs	• It is difficult to understand which programs to restructure and those to continue to support and grow if the organization is not aware of which ones are producing a deficit, surplus or are break-even.
l) Strategies to increase revenue for deficit producing programs are discussed and included in plans	• Developing specific revenue generating and fundraising strategies to generate revenue for deficit producing programs is important. • If the deficit producing program is funded by government, educate your funder on the bottom-line of the program as they may be unaware to the extent that the funding provided is insufficient and may be causing financial stress on the organization.
4. Budgeting must include multi—year financial planning:	
a) Setting goals to increase emergency, operating and capital reserves annually	• How much is there in the unrestricted reserve for emergencies? Capital? Other opportunities? • Set realistic annual financial targets and develop strategies that orient the organization to meeting those annual targets
b) Reviewing a 3- and 5-year trend analysis for: revenue, expense, reserves, assets and liabilities to determine other financial goals	• After a full analysis of the 3- and 5-year trends has been completed, determine which other financial goals the organization must put in place to ensure resilience

c) **Calculate ratios to assess liquidity (i.e. current and quick ratios) and trends over 3 – 5 years**	• Current assets must equal current liabilities at minimum (current ratio), if current liabilities are more than current assets, strategies must be put into place to inject more revenue.
5. Ensure a level of comfort at the board in having these financial stewardship discussions:	
a) What does the 3, 5- and 10-year revenue and reserves trend indicate for this organization?	
b) Why does the organization have a line of credit or loan? Why – for deficits or timing of funding?	
c) How can we strengthen the revenue mix model?	
d) Does the organization borrow from its reserve funds? Why – for deficits or timing of funding?	
e) If money is withdrawn from reserves does the organization replenish the reserves on a timely basis?	
f) Which funding contributions can be considered high or low quality? To assess high or low quality, think about the associated administrative burden, the amount of funding that can help fund expenses to cover administrative and operations, flat-lined funding year after year, increased output requirements…	
6. Ensure a level of comfort at the board in having these financial stewardship discussions:	
g) What are the perils of lack of diversification and over-diversification of government funded revenue? i. Example: The Ministry of Children, Community and Social Services (MCCSS) has assessed that organizations with 70% and greater reliance on revenue from one funder are at increased risk ii. Similarly, an organization can be overly diversified. An organization with a large number of funders will experience significant funding and administration requirements and will require additional unrestricted revenues to cover the associated costs to meeting the administrative requirements.	
h) The organization's capacity for making/saving money to cover expected program deficits (working capital) in the future?	
i) What is our capacity to generate revenue and save it for non-funded 'essentials'?	
j) Which programs produce a surplus, deficit or break-even and what can we do about changing the deficit producing revenue models or cost structure of those programs?	
k) What are the organization's major areas of risk?	

Financial Risk Assessment

a) Know how your funder(s) assess your organization's financial health and risk	• For example, MCCSS uses a new Financial Risk Assessment Review framework (FRAR) that includes many financial ratios. ○ MCCSS has assessed 511 agencies and 23% have been found to be at high risk, 51% at moderate risk
b) Be aware of discussions on decreasing funding and assess how probable and how severe the cuts will be	• Stay connected, get informed, plan proactively
c) Know your organization's tolerance to funding cuts, increases in revenue, decreases in fundraising	• Conduct scenario and contingency planning using the amount of the expected revenue decrease and the expected annual cost increases - see e) below.
d) How reliant you are on funding to fund key admin positions, systems, infrastructure before cutting a deficit producing program	• Remember that even a deficit producing program is likely to be contributing some money to administration. Cutting deficit programs can weaken the organization's ability to fund administrative expenses. Restructure programs carefully!

e) Scenario plan to assess the potential impact of funding changes	• Understand the tolerance to decreases to reserve and revenue decreases and expense and/or debt increases
	  ○ If a 4% reduction in revenue is expected
	  ○ If a 2% increase in costs are expected
	    ▪ The organization will have to find an additional 6% of revenues
	    ▪ E.g. 6% in revenues for an organization with:
	      • $1M in revenues is $60,000
	      • $3M in revenues is $180,000
	      • $5M in revenues is $600,000
	• What is the organization's capacity to lose funding due to shifts?
	  ○ of program funding to commissioning/ individualized funding
	  ○ of program funding to performance/outcome-based funding
	• What is the organization's capacity to withstand decreases from fundraising from baby-boomers?

NOTES