

Nonprofit Financial Management

Building a Foundation of Best Practices

Poverty & Opportunity Training Forum - April 11, 2024

StructuralIntegrity

Agenda

- People-centered financial management
- Financial terms and nonprofit financial statements
- Financial management practices
- Grant management and cost allocation

About Us

StructuralIntegrity

Structural Integrity is a nonprofit consulting and technical assistance organization. We strengthen the nonprofit sector by helping mission driven organizations build their foundational operations to **generate capacity, enhance sustainability, and center impact.**

We bring a combined 30+ years of experience working in nonprofit finance and operations, including hands-on experience building and maintaining the financial management systems we are going to discuss today.

Understanding who's here

What role do you hold in the organization?

What is your organizational headcount currently?

People-Centered Financial Management

Financial management goals & mindset



Common Financial Terms & Statements

Terminology

- **Accrual Accounting** - Revenue and expenses are recorded when earned/incurred rather than at the time cash is received or expended.
- **Revenue** - Income, either in the form of cash (such as a check from a donor), or the receipt of an *unconditional* pledge or grant award. In nonprofit accounting, revenue is generated when an unconditional pledge/grant award is received, regardless of cash timing.
- **Expense** - Recognition of the obligation to pay for goods or services received; record as consumed.
- **Net Income** - Revenue minus expenses over a given time period. Due to nonprofit revenue recognition rules, nonprofits can report large swings in net income surpluses and deficits.
- **Operating Reserves** - Available cash and liquid investments. Three to six months of annual operating costs on hand in the form of operating reserves is *generally* considered healthy.
- **Dual Controls** - To prevent a single point of fraud risk. For smaller orgs, at a minimum a board member (Treasurer) should get a copy of the bank statement(s) monthly.

Common Nonprofit Financial Statements

Statement of Activities

Reports revenues earned and expenses incurred over a specific time period, with the difference reporting net income generated or depleted over the period

Statement of Financial Position

Reports what an organization has (assets) and any obligations against them (liabilities) at a specific moment in time. The difference is reported as the net asset position of the organization.
 $Assets - Liabilities = Net Assets$

Statement of Functional Expenses

Required in audited financial statements and tax filings, it segregates the expenses of the organization by program, fundraising, and administrative costs. Funders often rely on this for “overhead” estimates.

More on the Statement of Cash Flows later in the presentation

Financial Management Practices

Financial Management Practices - Budgeting

- An annual financial plan (budget) is driven by annual goals and the resources needed to achieve them
- Typically built on an organization's fiscal year (FY)
- Draft revenue and expense budgets *separately*, then compare them to test for expense feasibility
- Engage staff in informing the budget for the areas of work they lead – what resources do they need to meet their goals? If those resources aren't possible, how do goals need to shift?
- Use a budget structure that's as simple as possible while giving you necessary budget information, review structure annually (based on feedback on prior year's process)
- Board should approve budget; leverage board committees (finance & development) for early feedback
- Share the approved budget with staff, including periodic updates on financial performance

Financial Management Practices - Revenue Forecasting

- Build the revenue budgeted based on known commitments and identified prospective donors – make assumptions and risks clear to staff & board
- Revenue placeholder estimates should be substantiated by data or reason (i.e. event revenue)
- Common to use discounting methodologies based on past giving

Funding Source	Ask Amount	Probability	Budgeted Amount	Explanation
Foundation A	30,000	100%	30,000	Committed
Foundation B	20,000	90%	18,000	Verbal Pledge
Foundation C	15,000	80%	12,000	Gave in 2022 and 2023
Donor A	10,000	60%	6,000	Gave in 2022
Donor C	2,500	30%	750	New Prospect
Totals	\$82,500		\$69,750	

Financial Management Practices - Financial Goals & Cash Flow

- Cash management is essential - revenue can fluctuate over time and long delays can exist between a funding commitment and the arrival of cash
- Both operating reserves and revolving line of credit can work together to help organizations consistently cover their monthly operating expenses
- Orgs can establish a financial goal to either build to or maintain an operating reserve of a certain size, and assess the appropriateness of a proposed annual budget by whether it meets that goal
 - Building a reserve may take multiple years
- To assess a budget's effectiveness at meeting a reserve goal, both a Statement of Activities and a cash flow forecast are needed.
 - A net income budget does not forecast cash flow

Financial Management Practices - Cash Flow

- For most nonprofits, a cash flow forecast and monitoring model, predicting and tracking the timing of cash generation and consumption, is a more useful tool than a Cash Flow Statement
- It can be a simple month-to-month look at forecasted cash inflows and outflows and the month-end operating reserve balance that would result. For example:

	March 30th	April	May	June	April-June Total
Inflows Forecast		30,000	20,000	100,000	150,000
Outflows Forecast		40,000	35,000	45,000	120,000
Balance	25,000	15,000	0	55,000	

- Orgs with a healthy cash reserve can consider investment opportunities to earn interest and are positioned to take on work that may require up front expenses (i.e. reimbursable grants)

Budget Monitoring & Forecasting

- Distributed “budget management” across staff empowers decision-making and increases data quality
- Monthly financial reports should be prepared and reviewed monthly by finance staff, leadership, and Treasurer. Could include:
 - Statement of Activities (actual v. budget)
 - Statement of Financial Position
 - A method to forecast revenue and expense to monitor potential variations from budget
- For decisions that have an impact on future FY expenses (such as hiring & raises), create a multi-year forecasting tool to understand out-year budget implications
- Recommend *at least* two formal financial reviews each FY to decide if the expense budget remains appropriate based on revenue generated and forecasted - suggest reviews after month 4 and 8

Financial Management Practices Grant Management & Cost Allocation

Grant Planning & Alignment

Organizations should first determine if a funding opportunity is right for the org and that it can comply with all funding terms **before** applying.

- Is it mission-aligned and strategy-aligned?
- What capacity will it take to deliver on the outcomes/activities being committed? Will this require adding new resources (staff or nonpersonnel)?
- Does the grant cover full cost of the outcomes/activities being committed, and for what duration of time? How will grant activities be sustainable?
- If data/outcomes reporting is required, are systems in place to collect necessary data points?
- Is the organization prepared to understand and comply with all grant requirements, including administratively?
- If there's a misalignment with org priorities/resources, is there leeway to shift what's being committed to the funder so it better aligns with what the org wants/has the capacity to do?

Financial Managements Systems - Tracking Restricted Revenue & Cash

- Restricted funding must be tracked to ensure all funds are spent on allowable activities
 - Entirely within finance system, or using excel for spend down plans
- Cash management practices must prevent the use of restricted *cash* for undesignated purposes
- Organizations may also need to implement systems to track staff allocations across grant sources, including timesheets (if required)
- System needed to track grant periods across fiscal years, and ensure unspent grant funds and the obligations attached to them at the end of a FY are included in the next year's budget

Know The Full Cost of Impact

Program - Staff time and nonpersonnel costs that will be needed to achieve programmatic outcomes (55%)

Payroll Taxes & Fringe - Cost must also include payroll taxes and benefits such as insurances, retirement, & payroll fees (5%)

Occupancy & Technology - rent, utilities, equipment, hardware, software, telecom, and supplies (5%)

Fundraising - development staff time to write grants, prepare grant reports and maintain partner/donor relationships (20%)

Administration - finance and ops, HR, program evaluation & design and organizational strategy & leadership (15%)

All these areas support impact. In this example, if direct program costs are calculated to be \$20,000, the cost allocation model informs a full grant proposal of \$36,360 ($20,000/.55$)

Additional Questions / Feedback?

(follow up questions can be sent to info@structural-integrity.org)