Assessing Your Grantees’ Financial Health

City & County of San Francisco

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Jessica Huey, Senior Consultant

November 29, 2018
What are indicators that an organization is financially healthy?
Financially resilient organizations

Stay focused on the long-term while continually assessing and responding to current needs. They understand and are able to tell their financial story.
What does a financially resilient organization look like?

Financial Resilience in Nonprofit Organizations

VALUES

PRACTICES

RESOURCES
Introduction to Financial Statements

Order of statements in the audit

Statement of Financial Position
BALANCE SHEET

Statement of Activities
INCOME STATEMENT

Statement of Functional Expenses

Statement of Cash Flows

Opinion Letter

Notes

Complete package
Revenue restrictions
Depreciation
What does a financially resilient organization look like?

**Balance Sheet**

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**What is Owned**

- Assets
  - Cash
  - Receivables
  - Investments
  - Fixed Assets

**What is Owed**

- Liabilities
  - Bills due
  - Line of Credit
  - Deferred Revenue
  - Debt (short-and long-term)

**Net Worth**

- Net Assets
  - Unrestricted (Board Designated, Fixed Assets, Other)
  - Temp. Restricted
  - Perm. Restricted

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Net Assets = What is Owned - What is Owed
Assets & Liquidity

Accessibility

Cash

Receivables

Investments

Property & Equipment
What does a financially resilient organization look like?

Statement of Activities & Statement of Functional Expenses

What was Earned

Unrestricted Revenue

What was Spent

Statement of Functional Expenses

Expenses

Results

Surplus (Deficit)
## Financial Health Analysis Tool

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<tr>
<td>Fiscal Year Ending:</td>
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<tr>
<td>Did your organization have an operating surplus or deficit?</td>
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<tr>
<td>Unrestricted Revenue &amp; Support (A)</td>
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<td>Less:</td>
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<tr>
<td>Total Expenses (B)</td>
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<tr>
<td>Change in Unrestricted Net Assets or “Operating Surplus or (Deficit)” (A-B)</td>
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<td>$0</td>
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<tr>
<td>How are resources allocated across programs and supporting services?</td>
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<tr>
<td>Total Program Expense</td>
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<tr>
<td>Divided by total expense:</td>
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<tr>
<td>Program Expense %</td>
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<td>Total Management &amp; General Expense</td>
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<td>Divided by total expense:</td>
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<tr>
<td>Management &amp; General Expense %</td>
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<tr>
<td>Total Fundraising Expense</td>
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<tr>
<td>Divided by total expense:</td>
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</table>
Operating Results

What was Earned
- Unrestricted Revenue

What was Spent
- Expenses

Results
- Surplus (Deficit)

1. Total unrestricted net income is positive over sum of 2 years or explanation [pilot]

2. YTD net income is either a positive number or explanation
What does a financially resilient organization look like?

- **Money in the Bank**: Cash and Cash Equivalents
- **What was Spent on Average Per Month**: Average Monthly Operating Expenses
- **Operating Runway**: Total change in cash is positive over 2 years or explanation [best practice]
- **Months of Cash on Hand**: In current audit agency has at least 60 days of cash (doesn’t include non-cash in operating expenses) [best practice]
What does a financially resilient organization look like?

**Working Capital Ratio**

Cash and Other Assets Converted to Cash within the Next 12 Mos.

What is Owed in the Next 12 Mos.

How Assets Can Cover Liabilities in the Short-Term

Total Current Assets \( \div \) Total Current Liabilities = Working Capital Ratio

Working capital ratio is greater than 1
Liquid Unrestricted Net Assets (LUNA)

Unrestricted Net Worth

Unavailable Net Worth

6 Months of Operating Reserves

Unrestricted Net Assets

Unavailable Net Worth

Illicit Net Assets

Liquid Unrestricted Net Assets

7 Months of Operating Reserves

What does a financially resilient organization look like?

Liquid Unrestricted Net Assets (LUNA)
We believe that the audit evidence we have obtained is sufficient and appropriate to provide basis for your audit opinion.

**Opinion**

In our opinion, the financials statements referred to above present fairly, in all material respects, the financial position of Nonprofit Org as of June 30, 2018, and the changes in its net assets and its cash flows for the years that ended in accordance with accounting principles generally accepted in the United States of America.

San Francisco, CA
September 14, 2018

Unmodified opinion

Audit completed within 6 months of end of fiscal year
Notes to the Financial Statements

- Basis of accounting
- Fixed assets
- Debt
- Restricted net assets
- Related party transactions
- Subsequent events
- Commitment and contingencies

No material weaknesses or going concern in the notes
Discounting of contributions receivable

The Organization discounts its multi-year contributions ("pledges") and grants receivable in order to present these receivables at present value in accordance with generally accepted accounting principles ("GAAP"). However, GAAP requires that once pledges are discounted and recorded each year, the discount rate used should be applied consistently across the applicable periods and not be changed for those pledges in future years. We noted that the discounts on these receivables are being revised subsequently to the time the contribution was initially recognized. We proposed a $45,000 adjustment related to this matter, which was recorded in the Organization’s financial statements.

Recommendation

We recommend that when pledges are discounted and recorded, the discount rate for those pledges should not be changed in the future.

Management response

We are aware that the discount rate used to discount pledges raised in prior years should not be changed. In fiscal year 2013, however, the organization elected to use the risk free rate of US Daily Treasury Yield Curve Rates in calculating the net present value of pledges not expected to be paid for more than one year instead of the Federal Reserve Commercial and Industrial loans rates used in prior years. To date, we have assessed that all receivables due in 2015 are collectible based on donors’ historical records and commitment to the organization.

To be consistent with the US Daily Treasury Curve rates as basis in calculating the discount for the pledges due in 2015, the receivables raised in fiscal year 2012 were discounted using the rate as if the change happened in fiscal year 2012.
Accounting Standards Update (ASU)

- ASU 2016-14:
  - Issued in August 2016
  - First major revision since 1993
  - Effective Date: Calendar 2018 or Fiscal Year 2019
Key Provisions

Liquidity & Availability

Net Asset Classification

Functional Expenses

ASU 2016-14

Underwater Endowments

Investment Return
Net Asset “Classification”

- Unrestricted Net Assets
- Temporarily Restricted Net Assets
- Permanently Restricted Net Assets

Net Assets Without Donor Restrictions

Net Assets With Donor Restrictions
Liquidity & Availability of Resources

**Qualitative**

Disclose: how a nonprofit manages its available liquid resources

**Quantitative**

Availability of financial assets to meet cash needs for *general expenditures* within one year of balance sheet date
Cost Allocation Methods

By Staff (FTE)

Program A
Management & General

Fundraising
Program B

By Space Usage (Sq Ft)

By Participants
## Internal Financial Reports

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<thead>
<tr>
<th>1g</th>
<th>Cash flow projections [best practice]</th>
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<table>
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<tr>
<th></th>
<th>Budget Owners</th>
<th>Leadership Team</th>
<th>Board of Directors</th>
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</thead>
<tbody>
<tr>
<td>Budget-to-Actual Revenue &amp; Expenses for program, contract and/or org-wide</td>
<td>X</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Performance Dashboard</td>
<td>X</td>
<td>X</td>
<td>X</td>
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<tr>
<td>Management Narrative</td>
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<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Statement of Activities</td>
<td></td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Balance Sheet and supporting schedules</td>
<td></td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Cash Flow Projection</td>
<td></td>
<td>X</td>
<td>X</td>
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<tr>
<td>Year End Projection</td>
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<td>X</td>
<td>X</td>
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</tbody>
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<thead>
<tr>
<th>6a</th>
<th>Balance Sheet is current</th>
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<tbody>
<tr>
<td></td>
<td>Current bank reconciliation</td>
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</table>

<table>
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<tr>
<th>6d</th>
<th>P&amp;L is current</th>
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<tbody>
<tr>
<td></td>
<td>Includes ytd revenue and expense by program, contract or funding source</td>
</tr>
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</table>

| 6f                             | Ytd net income is positive |
Resources

Public Website: [http://www.sfgov.org/controller/nonprofits](http://www.sfgov.org/controller/nonprofits)
- Training Materials
- Monitoring Form
- Resources for Nonprofits

Internal Website (login needed):
[https://elibrary.controller.sfgov.org/csa/performance/nonprofitmonitoring/SitePages/Home.aspx](https://elibrary.controller.sfgov.org/csa/performance/nonprofitmonitoring/SitePages/Home.aspx)
- Monitoring Workflow
- Contractor Libraries
- Monitoring Resources

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Isabel Ochoa *(Trainings)*
Performance Analyst
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Isabel.M.Ochoa@sfgov.org
Resources

- **The Key to Long Term Financial Health Liquid Unrestricted Net Assets (LUNA).** Hilda Polanco, New York Nonprofit Press, May 2012:

- **Keeping it in Reserve: Grantmaking for a Rainy Day.** Hilda Polanco and John Summers, Nonprofit Quarterly, May 2016:


- **Nonprofit Audit Guide**

- **StrongNonprofits.org**
What does a financially resilient organization look like?

Fiscal Management Associates (FMA)

- Established in 1999 to serve not-for-profit organizations around the country
- Provides customized financial management, accounting, software, organizational development, human resources, and other consulting services
- Works directly with organizations or through funder-supported management and technical assistance programs

FMA's mission is to empower not-for-profit organizations with the knowledge and skills to successfully serve their constituents and fulfill their missions

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