

# Linking Money to Mission

## Strategic Financial Management

**Presented by**

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# Checking In



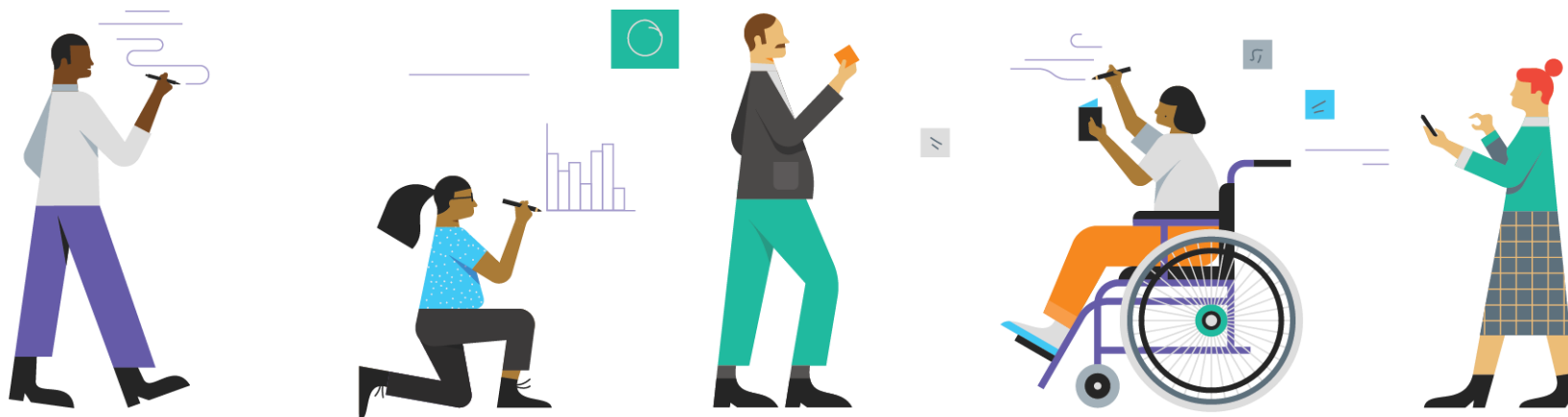
**What is one word to describe your energy this morning?**

# Nonprofit Finance Fund: Where Money Meets Mission

*NFF envisions a world where capital and expertise come together to create a more just and vibrant society.*

**We unlock the potential of mission-driven organizations through:**

- **Tailored investments**
- **Strategic advice**
- **Accessible insights**



# Goals

1

Review the nonprofit operating context to understand the **foundations of nonprofit financial health**

2

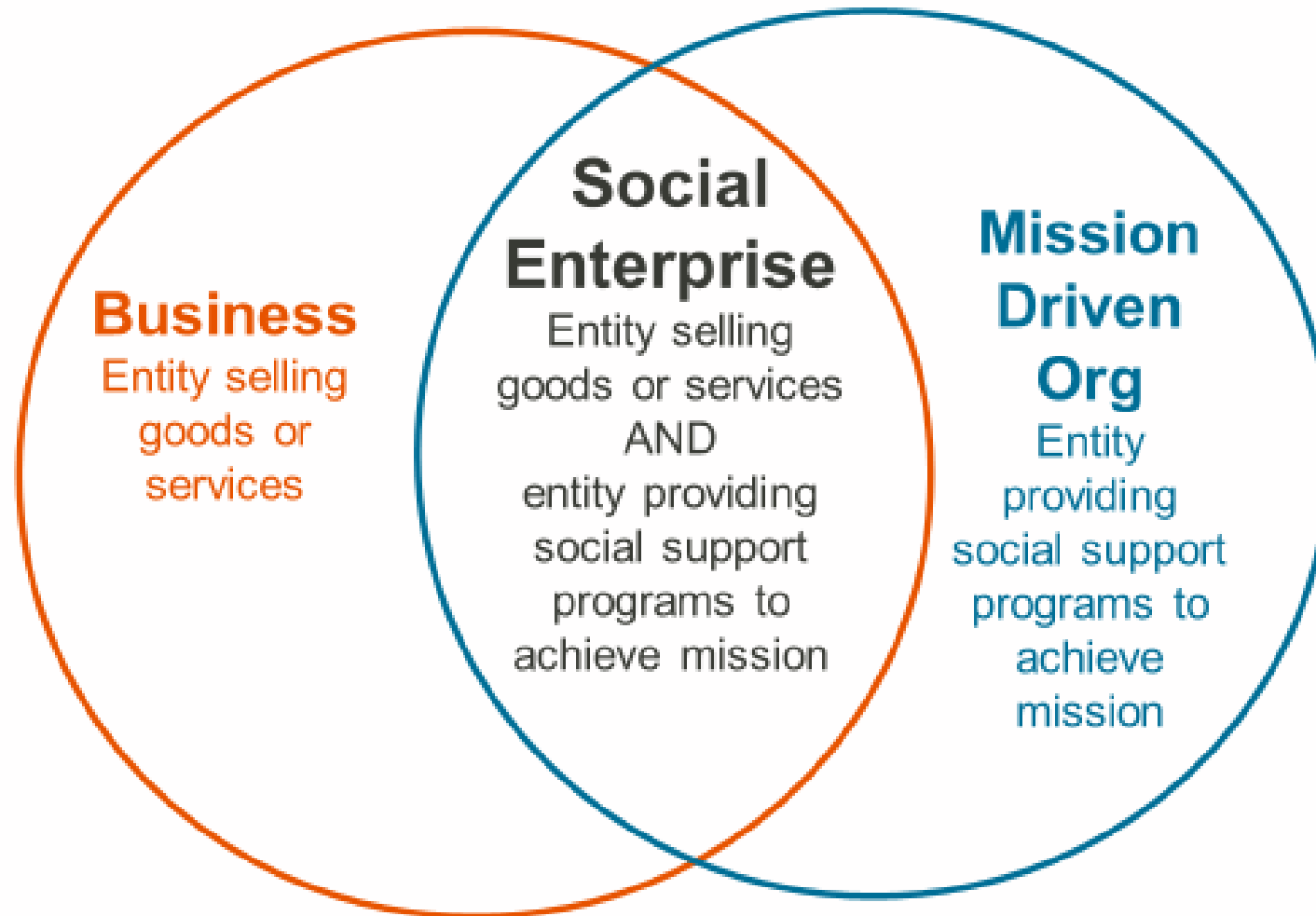
Understand and be able to analyze and articulate your **business model**

3

Understand and be able to analyze and articulate your **capital structure**

# Operating Environment for Nonprofits

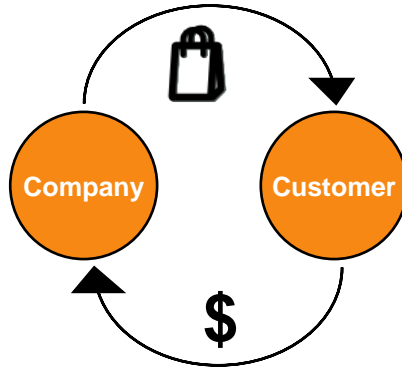




# “Rules” of For-Profit Finance

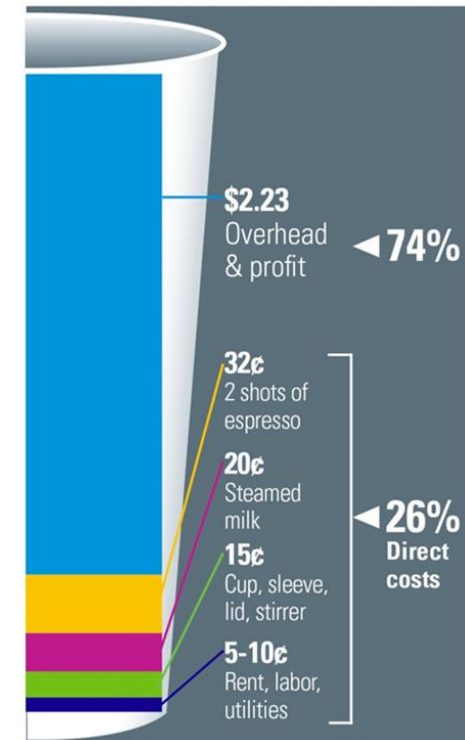
In the **for-profit** world:

- Customer buys the product



- Management decides how the money is spent
- **Overhead and profit** are included in the price, and are seen as **necessary and regular** part of the business

12-Ounce Coffee = \$3.00



# “Rules” of Nonprofit Finance

## Multi-payor system

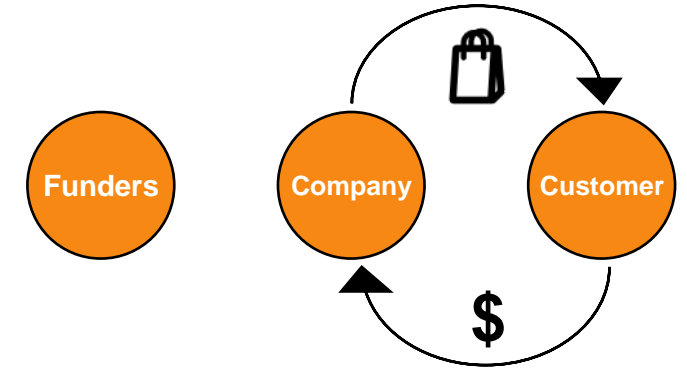
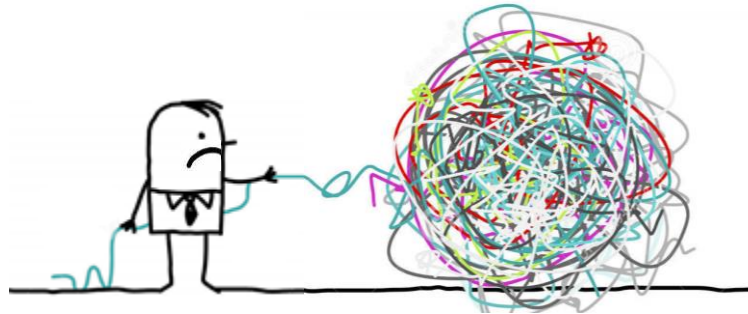
- Client often does not pay
- Third parties pay

## Insufficient and Restricted Funding

- Donations must go to ‘direct services’...
- ...and not to ‘overhead’
- Restrictions complicate finances!

## Money-losing business

- We fill social needs with low/no commercial returns (we pick the hardest work!)
- Profits are seen as unnecessary

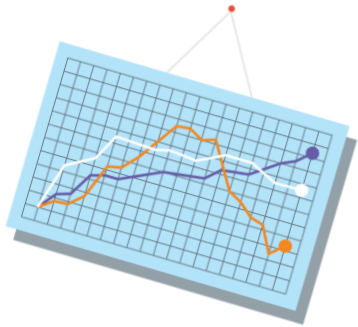




# Harmful Nonprofit Myths

## Myth: Nonprofit = No Profits

- Truth: Surpluses are necessary!
- Tax Status vs. Business Model



## Myth: The 'Overhead Ratio' measures our value

- Truth: Outcomes measure value
- Overhead measures investment into our model

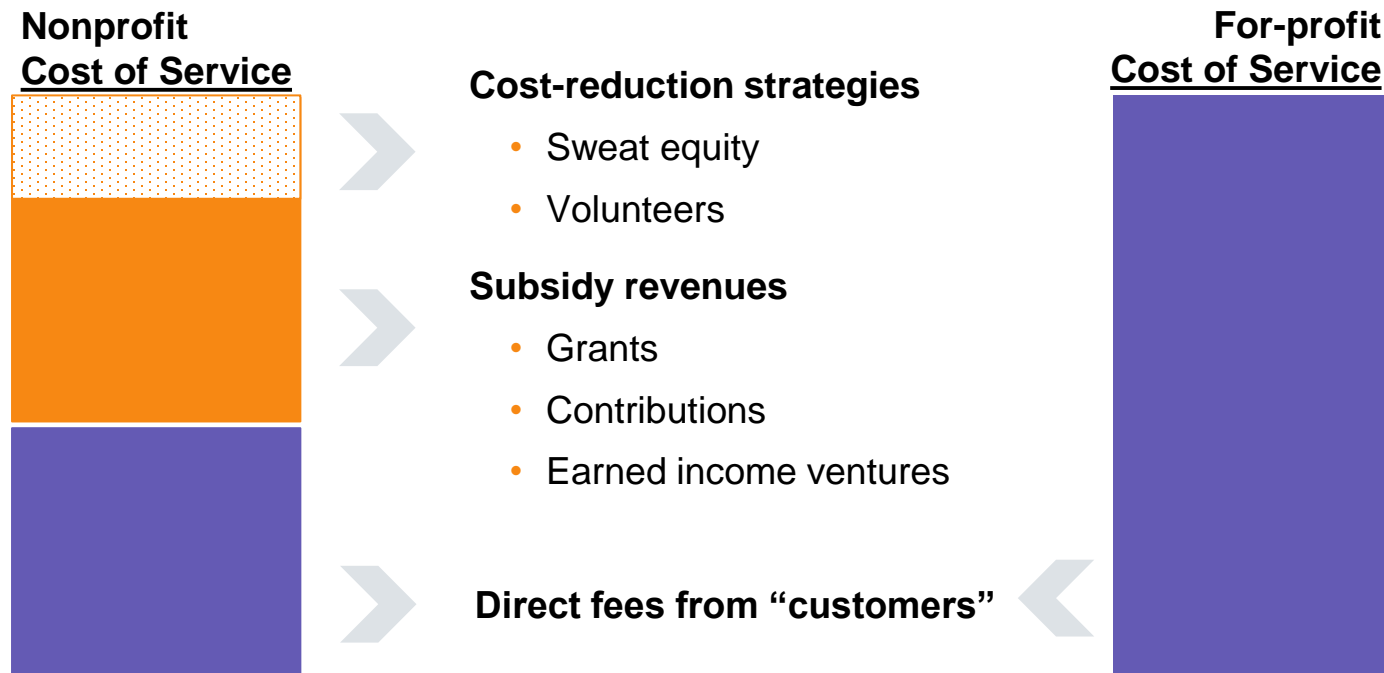
## Myth: Nonprofits can be 'self-sufficient'

- Truth: We'll always need 3<sup>rd</sup> party payors



# Myth of Self-Sufficiency: The Truth About the Nonprofit Business Model

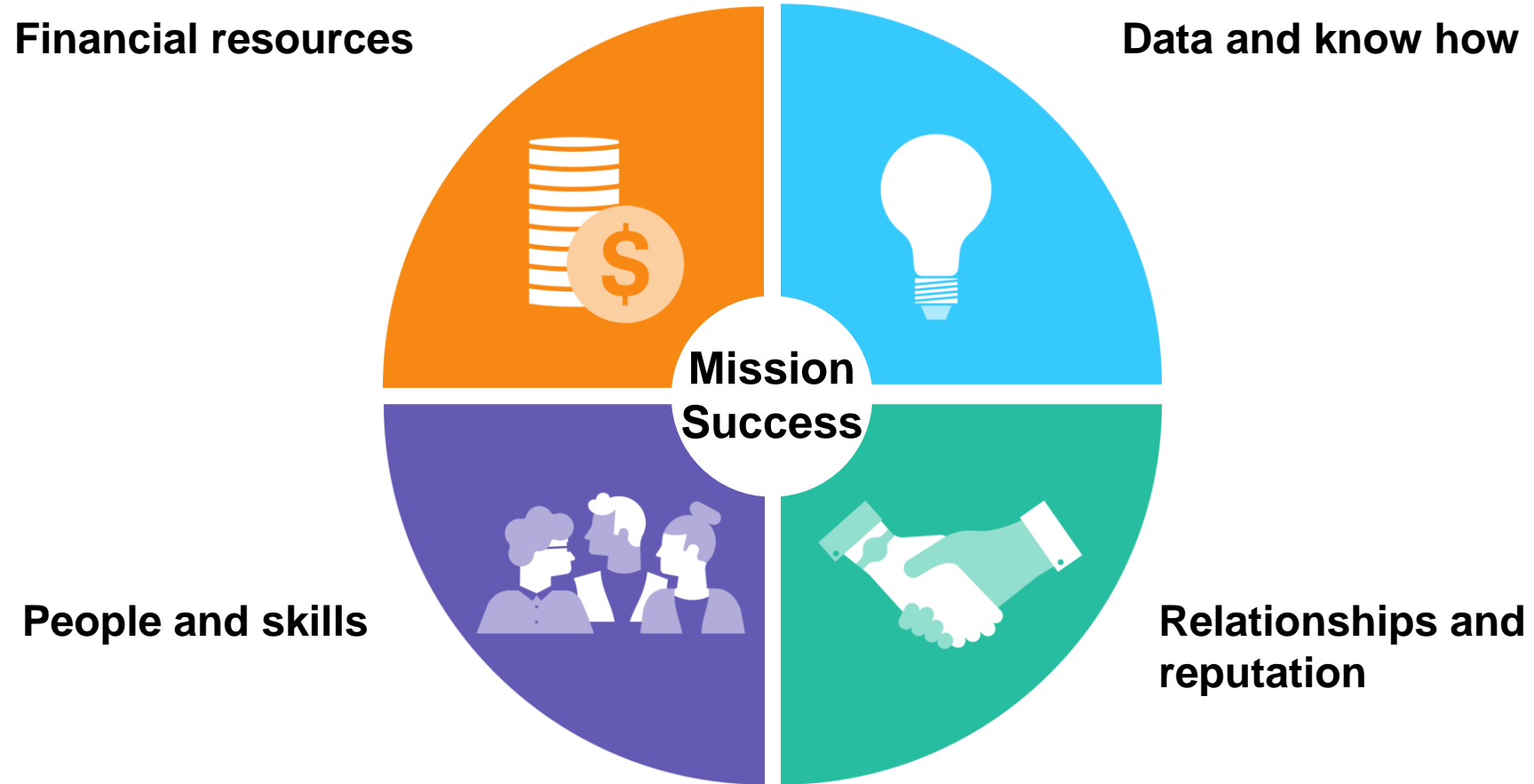
## Nonprofits must run two businesses: Mission & Subsidy



- Subsidy businesses take their own set of capacities to run
- When program growth or change occurs, subsidies must grow in proportion
- Cost reduction strategies can have serious consequences for the mission


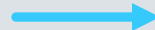
# The Strengths Framework

*How Nonprofits have survived this funding system*



# Understanding Financial Health and Performance

## Business Model and Capital Structure

Business Model	 	Capital Structure
How an organization makes and spends money in service of its mission	<b>Definition</b>	The nature, distribution, and magnitude of balance sheet items
The income statement	<b>Reflected On</b>	The balance sheet
Do you have the revenue to meet and exceed expenses?	<b>Guiding Question</b>	Do you have enough of the right types of resources to accomplish your strategy?
Consistent surpluses; impactful programs	<b>Measure of Success</b>	Mitigate risk, support innovative programs, reinvest in business model

# Full Cost Needs Go Beyond the Income Statement/Budget

## Must haves for *all* organizations

### Total Expenses

Operating, non-operating, and unfunded

### Working Capital

Access to cash for day-to-day needs

### Reserves

Savings, a “rainy day” fund



## Sometimes needed by *some* organizations

### Change Capital

Resources to adapt, grow, partner, or down-size

### Fixed Asset Additions

Money to purchase a new building, new computers, or new vehicles

### Debt Principal Repayment

Mortgage, line of credit, etc.

# Why Full Cost Matters

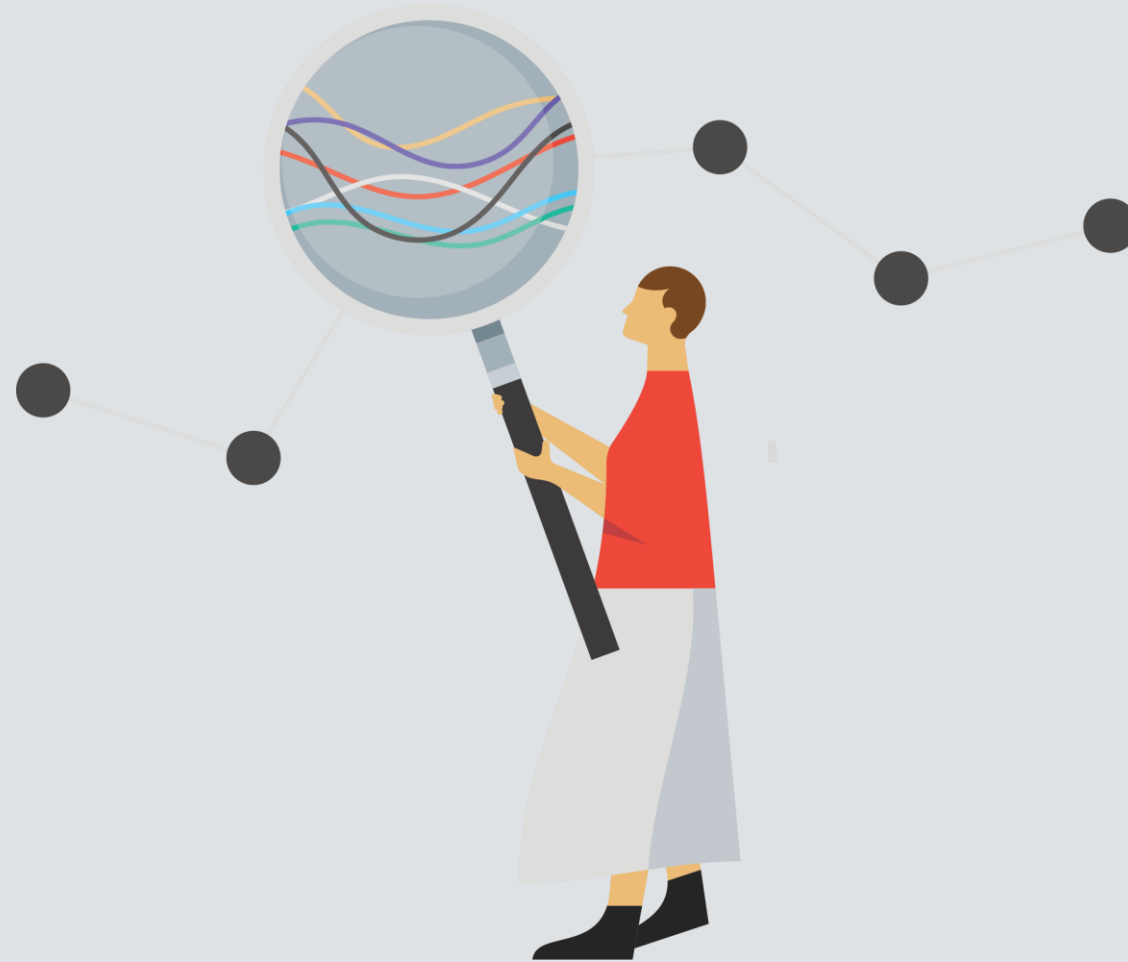
- Lifts the sector out of the false dichotomy of program vs overhead
- Captures both short- and long-term needs
- Holistic, grounded in context, allows for nuance and change over time
- A tool to advance racial equity
- Aligned with Trust-Based Philanthropy



Additional Resources around Full Cost can be found at <https://nff.org/full-cost>

# Business Model

- Understanding the Business Model through the Income Statement
- Assessing Historical Trends & Current Condition



# What is Your Business Model?

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**Business Model:** how an organization makes and spends its money in the service of its mission

**What do you do in service of mission?**

What does it take?

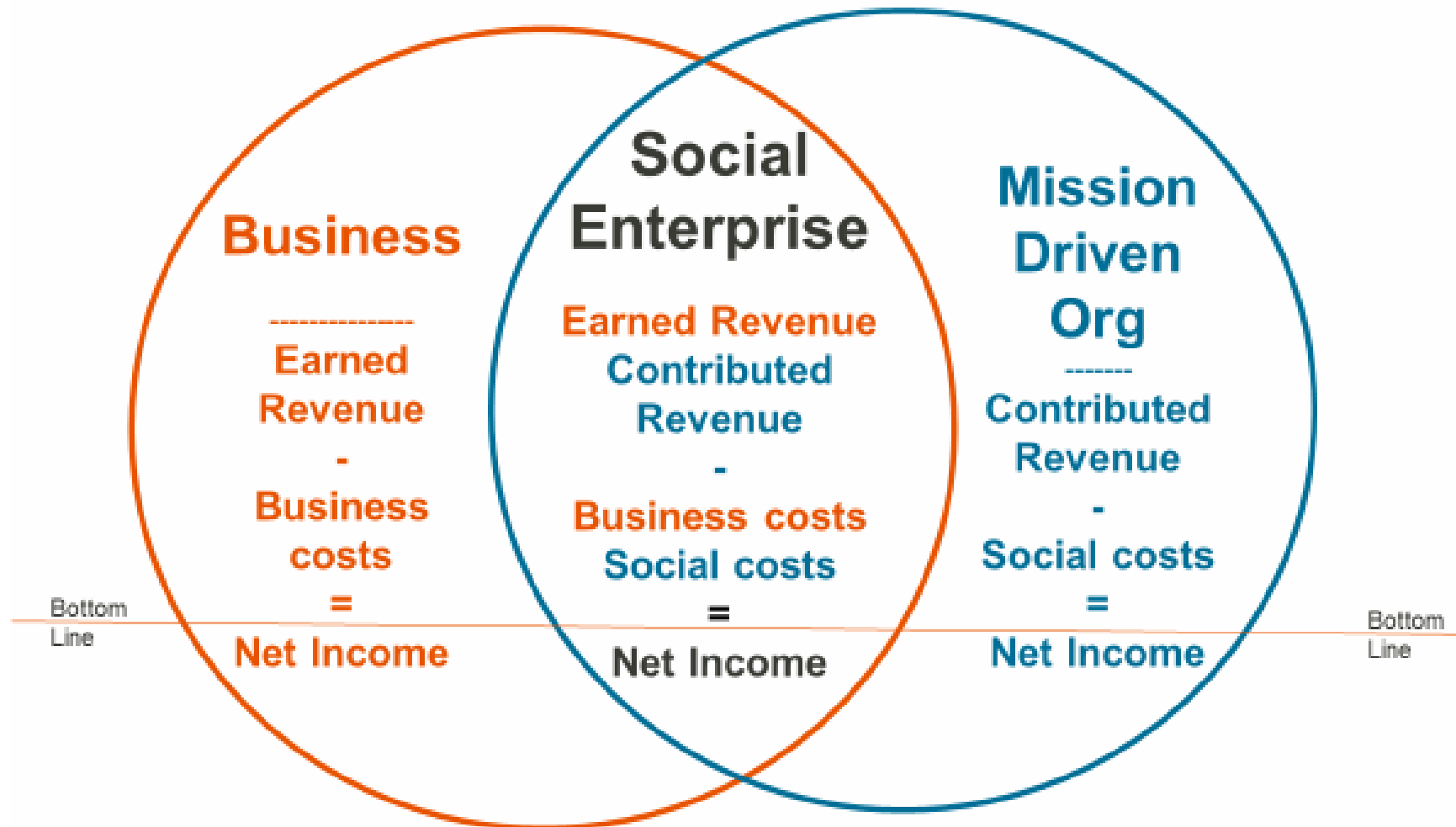
How do you pay for it?

How does it fit into vision and strategy?





# Social Enterprise Financials



# Unpacking the Business Model

## Income Statement

### Revenue

Earned  
Contributed  
Private Sources  
Government

### Revenue Dynamics

- Where did your money come from?
- Were revenue streams reliable or at risk?
- Was seasonality a factor?

### Expenses

Personnel  
Professional Fees  
Occupancy  
Support  
Other

### Expense Dynamics

- How did you spend your money?
- Were expenses predictable?
- Was management responsive to operating changes and prepared to make difficult decisions?

### Surplus / Deficit

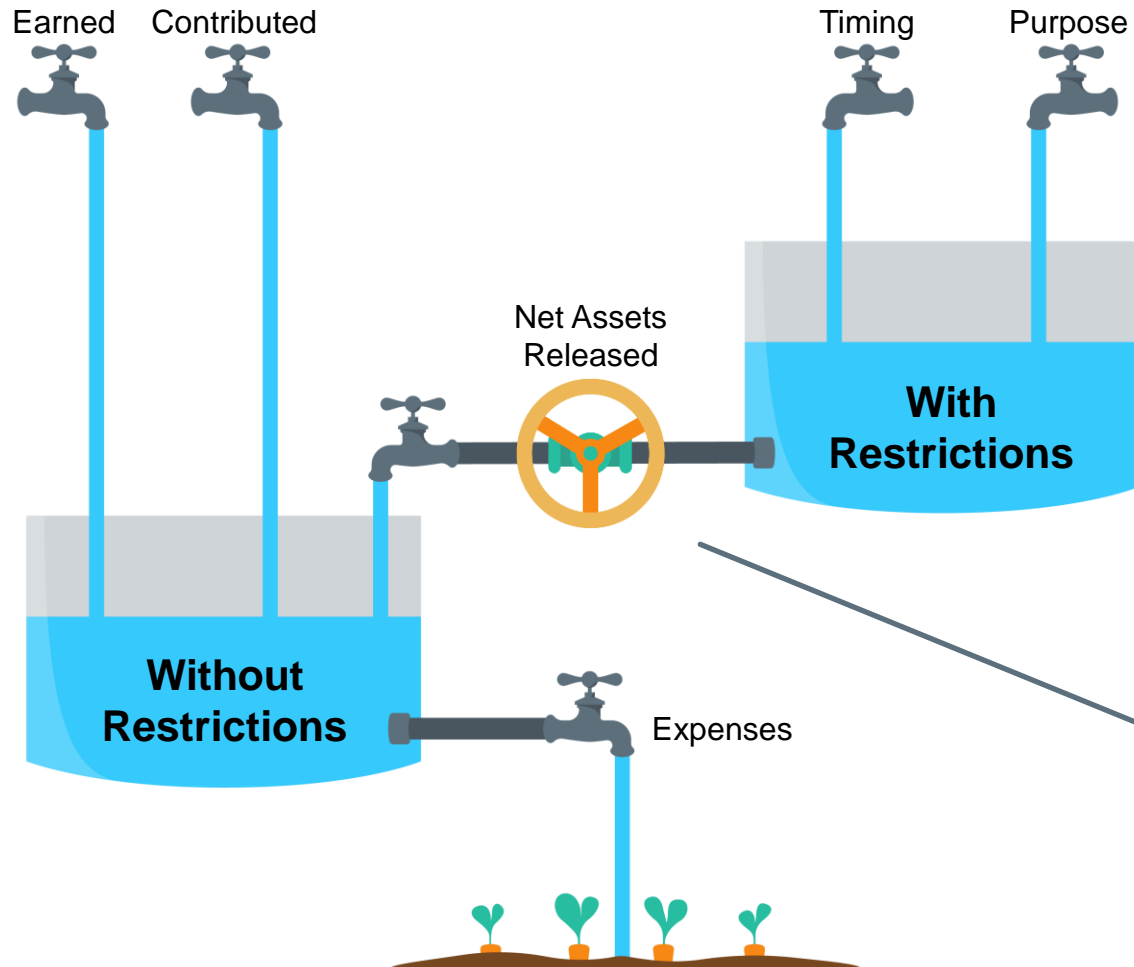
### Profitability & Savings

- Were costs covered?
- Were you able to achieve a surplus?

# Restrictions Affect the Flow of Money

## Revenue Without Restrictions

## Revenue With Restrictions



**Net assets released from restrictions** refers to the transfer of funds from net assets with donor restrictions to net assets without donor restrictions due to the satisfaction of donor-imposed stipulations with respect to timing or purpose of the contribution.

# Income Statement

Restrictions met, funds available for use

	2018			2017
	Without restrictions	With restrictions	Total	Total
<b>Revenue and Support</b>				
Government contracts	550,248		550,248	607,739
Foundation grants	97,235	35,900	133,135	147,235
Special event revenue, net	14,530		14,530	12,054
Individual contributions	14,526		14,526	10,515
Net assets released from restriction	45,250	-45,250	--	--
<b>Total revenue and support</b>	<b>721,789</b>	<b>-9,350</b>	<b>712,439</b>	<b>777,543</b>
<b>Expenses</b>				
Personnel	463,029		463,029	452,315
Professional fees	185,040		185,040	155,680
Occupancy	108,087		108,087	107,532
Support	9,000		9,000	16,908
Interest	7,318		7,318	6,321
<b>Total expenses</b>	<b>765,156</b>		<b>765,156</b>	<b>738,756</b>
<b>Operating Surplus/Deficit</b>	<b>-43,367</b>	<b>-9,350</b>	<b>-52,717</b>	<b>38,787</b>
Non-Operating Activity				
Bequest	55,000		55,000	
<b>Change in net assets</b>	<b>11,633</b>	<b>-9,350</b>	<b>2,283</b>	<b>38,787</b>

# Income Statement

## Clarifying the bottom line

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Operating  
results

Non-operating  
revenue placed  
"below the line"

# Business Model in a Perfect World

If you have a **magic wand**

- Annual surpluses meet short and long term organizational needs
- Programs reflect and meet the needs of the community (informed by data and outcomes measurement)
- You have enough capacity and the right skills on staff
- Staff are fairly paid and supported in their jobs
- Staff and board don't feel tired and panicked



# Q&A



# Capital Structure





# Capitalization

Business Model  
*Annual results of  
operations*



Capital Structure  
*Snapshot of overall  
financial health*



- **Capitalization** = alignment of balance sheet resources with short-term & long-term mission and impact goals
- **Balance sheet** = resources beyond the income statement, (e.g. reserves)



Under-Capitalized



Mis-Capitalized



Well-Capitalized

# Why Capital Structure Matters: Financial Risk Capacity

An organization's ability to **mitigate risk** is influenced by the resources it has on hand.

**If an organization has...**

- Plenty of unrestricted cash and receivables
- A fully available line of credit
- Sufficient reserves available to management
- Little to no wear-and-tear of fixed assets
- Reoccurring surpluses

**...then it has high capacity for risk or change.**

**What are your organization's main risks?**

# How to Read the Balance Sheet

Assets – Liabilities = Net Assets

## Balance Sheet

### Statement of Financial Position

#### Assets

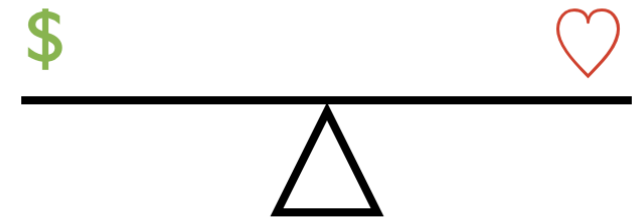
What organizations  
OWN

#### Liabilities

What organizations  
OWE

#### Net Assets

What organizations  
OWN free and clear



# How to Analyze the Balance Sheet

## Assessing Financial Health

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### Balance Sheet

#### Assets

Does the organization have access to appropriate resources?

- Cash – How much? How “liquid?”
- Receivables – Are they slow to collect? Are they at risk?
- Investments – How much? Are they restricted?
- Property and Equipment – How does the organization deal with maintenance issues?

#### Liabilities

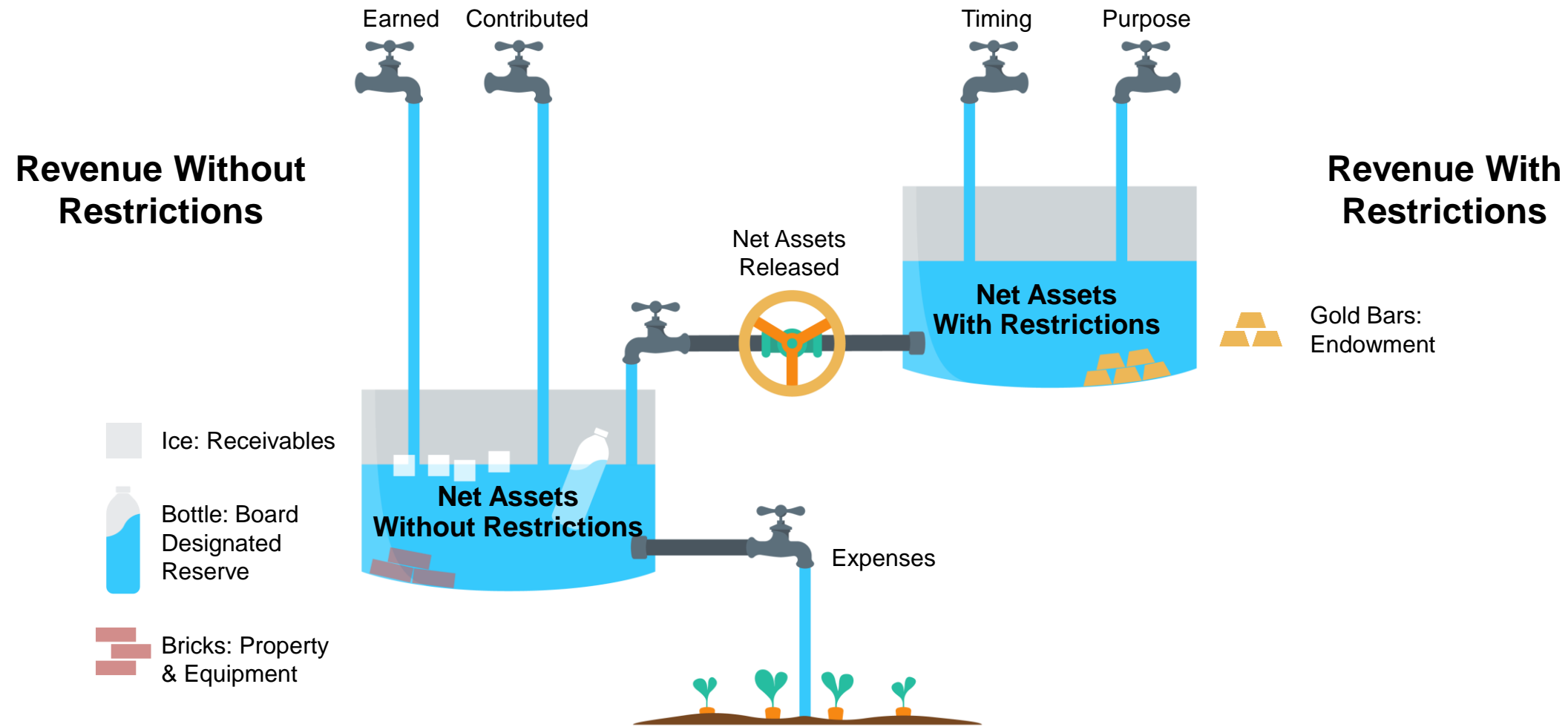
Does the organization owe more than it owns?

- Payables- How is cash flow managed?
- Line of credit, Debt: Do you have a plan to pay back debt?

#### Net Assets

- Net Assets Without Restrictions – Does the organization own more than it owes? How much is liquid?
  - Reserves – Does the organization have them? Are they suitable to their needs?
- Net Assets With Restrictions – Do they support core programs?

# A Closer Look at Net Asset Composition



# Balance Sheet

## ABC Organization

### Statement of Financial Position

	2020	2019
<b>Assets</b>	<b>Total</b>	<b>Total</b>
Cash and cash equivalents	\$ 64,552	\$ 43,671
Accounts receivable	17,027	17,829
Grants and pledges receivable	172,856	148,845
Property & equipment, net	626,041	635,041
<b>Total Assets</b>	<b>\$ 880,476</b>	<b>\$ 845,386</b>

### Liabilities

Line of credit	\$ 60,000	\$ 58,000
Accounts payable	43,652	48,772
Deferred revenue	5,600	6,240
Mortgage payable	302,000	323,150
<b>Total Liabilities</b>	<b>\$ 411,252</b>	<b>\$ 436,162</b>

### Net Assets

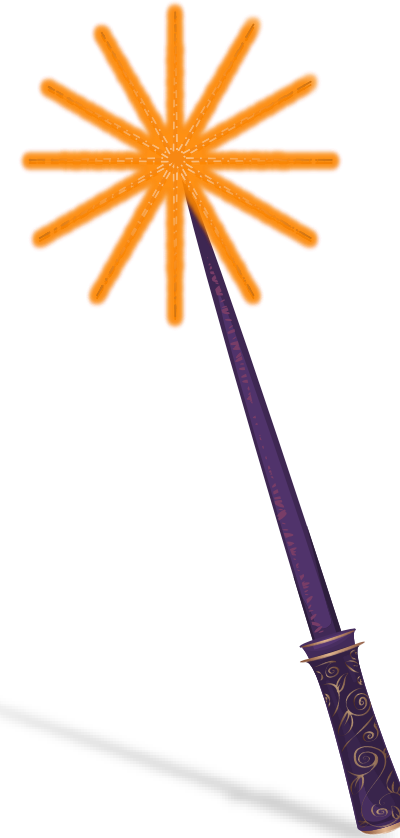
Net Assets Without Restrictions	\$ 340,092	\$ 380,103
Net Assets With Restrictions	129,132	29,121
<b>Total Net Assets</b>	<b>\$ 469,224</b>	<b>\$ 409,224</b>
<b>Total Liabilities &amp; Net Assets</b>	<b>\$ 880,476</b>	<b>\$ 845,386</b>

Balance Sheet	
Assets	Liabilities
	Net Assets

# Capital Structure in a Perfect World

If you have a **magic wand**

- Paying bills and managing cash flows is a breeze
- You're not worried about equipment breaking; you can easily make repairs or replacements
- You've got a plan for any debt
- You're excited by new opportunities, not burdened
- A strong safety net protects from the unexpected and risks inherent in your revenues or programs



# Assess Your Organization:

## Three KEY Measures of Financial Health

Indicators	What It Shows	Where to Find It	How to Calculate
<b>1. OPERATING SURPLUS/ DEFICIT</b> <i>Financial Performance</i>	Your ability to <b>cover operating expenses with revenue</b> from your core business model.  <i>Reflects the business model's strength</i>	<b>Income Statement</b>  <i>Audit, IRS Filing, internal statements, budgets</i>	<b>Operating Revenue – Operating Expenses</b>
<b>2. MONTHS OF CASH</b>  <i>Liquidity</i>	How long you can <b>cover short term obligations and day-to-day expenses.</b>  <i>Best measure of solvency</i>	<b>Balance Sheet</b>  <i>P&amp;L (for expenses) Audit, IRS 990 Filing, Internal Financials, Bank Statements</i>	<b>Total Cash</b>  <hr/> <b>(Total Expenses / 12)</b>
<b>3. MONTHS OF AVAILABLE NET ASSETS (ANA)</b>  <i>Availability</i>	How much of net assets is truly <b>available for use</b> (less restricted cash and outstanding obligations).  <i>Better measure of accessible resources</i>	<b>Balance Sheet</b>  <i>P&amp;L (for expenses) Audit, IRS 990 Filing, internal Financials</i>	<b>Total Net Assets Without Restrictions</b> <b>– (Equity in P&amp;E)</b> <hr/> <b>(Total Expenses / 12)</b>



# Q&A



# Takeaways

Nonprofits operate in a flawed system of inequities. Knowing the harmful myths and advocating with a strengths-based frame can be an **alternate narrative to overcome these barriers.**

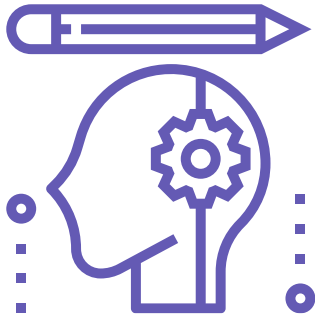
The ability to understand and explain your core business model can help you make strategic decisions about how to **build greater financial stability.**

Understanding your balance sheet can help you know your full costs, maintain financial stability, and **better tell your financial story.**

# Head, Heart, Feet

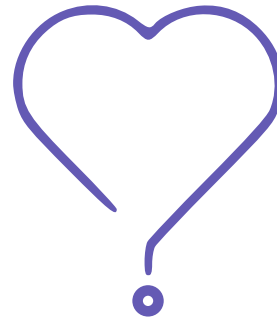
## Head

What did you **learn** from this workshop?



## Heart

How did this workshop make you **feel**?



## Feet

What **actions** will you take to bring this back to your organization and community?



# Thank You!

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