GIANFORTE Family Foundation

EASY CALCULATIONS:

TO HELP YOU INTERPRET FINANCIAL STATEMENTS*

Not every board member needs to be a financial wizard. But, every board member needs to be a financial steward. Effective stewarding starts with learning to read, understand, and ask good questions of financial statements. Sound daunting? This article will help you get started with a few easy calculations.

To perform these calculations, request the following information from your Executive Director for the last complete fiscal year:

- **Statement of Activities** (Profit & Loss Statement)
- **Statement of Financial Position** (Balance Sheet)
- **Funding Sources & Percentages** (Request the total amount donated by each funding source: individuals, corporations, grants, endowments, etc. Also, request the dollar amount donated by your top two donors.)

As you become more comfortable reviewing the statements, you'll want to compare them with those from previous years (or quarters). These side-by-side comparisons will help you evaluate the trajectory of your organization's financial health and identify trends.

Financial statements should be included in every board meeting packet and be reviewed by **all** board members before each meeting. The packet should include the above financial statements as well as the **current annual budget with year-to-date actuals**. You should come to each meeting prepared to ask a question or two.

CALCULATIONS USED TO DETERMINE: FINANCIAL STRENGTH

#1 Liquidity: This calculation measures your organization's ability to pay bills in the short term. Numbers for this calculation can be found on the Statement of Financial Position under "Current Assets" and "Current Liabilities." The answer in the following equation of .369 means the organization has 37 cents for every dollar of "liability" or projected expenditures. Since the answer is less than 1.0, the liquidity for this organization is considered weak or doesn't have enough readily-available assets to cover your short-term expenses.

An answer of 2.5+ is considered **strong**, 2.5-1.0 is **fair**, and below 1.0 is **weak**.

Current Assets/Current Liabilities =	41,000/111,000 = .369 cents to the dollar

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#2 Burn Rate: This calculation shows how many months of cash is on hand. Pull the number for "Cash" from the Statement of Financial Position and pull the "Total Expenses" from the Statement of Activities. The number 12 in the equation below represents 12 months of the year. This calculation can be adjusted to estimate the number of days of cash on hand by replacing the 12 with 365.

Cash reserves of 4+ months are considered **strong**, 2-4 months **fair**, and 2 months or less **weak**.

Cash/(Total Expenses/12 months) =	50,000/(300,000/12) = 2 months of cash

Questions to ask of these calculations:

1. Does our organization have enough cash on hand to pay bills when they come due?
2. Do we have enough cash in reserve?
   a. If you answered "yes," ask: How much (if any) of this cash is designated for a specific purpose? Your Executive Director (with enough notice) can answer this question for you.
3. If you answer "no" to either question, ask:
   a. Has some factor skewed these numbers? (i.e.: Some nonprofits bring in the bulk of their funds during an annual banquet or end of year campaign. Therefore, a quarterly snapshot might be misleading.)
   b. Where can we cut expenses? How can we raise more funds?
   c. What financial goals should we set for future liquidity and burn rate?
   d. What is the reasonable amount of time needed to reach these goals?
   e. What role does the board play versus the Executive Director in reaching these goals?
4. After considering designated gifts, is the burn rate negatively impacted?

CALCULATIONS USED TO DETERMINE: FINANCIAL RISK

#3 Reliance: Building a balanced financial portfolio should be the goal of every nonprofit board. In the next calculation, one donor gives 33.3% (or $20,000) of the annual revenue. **Jackpot?** Probably not - at least for the long-term health of an organization. Your "bread and butter" should come from small to medium-sized local donors or earned income. Why? Simply, losing one $25 or $250 per-month donor is easier for an organization to recoup than losing one large grant. ***Note:*** *Most grantmakers do not want their nonprofit partners financially reliant on their ongoing gifts. Also, if a single donor gives 33.3%+ of your revenue for two consecutive tax years, your nonprofit may "tip." Tipping reclassifies a public charity to a private foundation, resulting in excise taxes and minimum distribution requirements (read more).*

To run this calculation, use the information on donor types: 1. Amount Donated by Largest Single Donor **2.** Amount Donated by Individual Donors **3.** Amount Donated by Grant-Making Organizations (total and individual amounts) **4.** Amount Donated by Corporate Donors **5.** Any other donor types that are unique to your organization. For guidance on "normal" percentages of giving by donor type, read this short article.

Note: *Your organization's policies on donor anonymity requests may limit the information your Executive Director is able to provide - specifically, the names of certain donors.*

Revenue Source/Total Revenue =	20,000/60,000 = .333 or 33.3% of total revenue

#4 Self-Sufficiency: Nonprofits that generate earned income often achieve greater overall financial health. Earned income reduces financial risk through a strong business model directly connected to your organization's mission. ***Note:*** *Earned income must be related to your nonprofit's mission or may be subject to unrelated business income tax.*

Options include thrift stores, tutoring, training, and other services offered for a fee. Though earned income operations are a wise move, some nonprofits suffered losses in 2020 because their revenue-generating vehicles (primarily thrift stores) were closed. This should not deter you from developing an earned income business plan; just be aware of the risks. In the calculation below, **the higher the self-sufficiency ratio, the lower the financial risk.**

Both numbers needed to run this calculation can be found on the Statement of Activities. "Earned Revenue" may also be listed as "Program Services Revenue."

Earned Revenue/Total Expenses =	10,000/160,000 = .062 or 6.2% of total revenue

Questions to ask of these calculations:

1. Do we rely too heavily on any one source? What would happen if X donor ceased giving?
2. Which donor type needs to be strengthened in our donor portfolio?
3. Is our earned income program generating sufficient income? (Consider costs associated with staff time, designated facilities, utilities, material costs, etc.)
4. Should we consider new ways to generate earned income?

Interested in learning more? Here are a few ideas:

- Ask another board member or the Executive Director to help you grow in your ability to read, understand, and ask good questions of the financial statements.
- Read *Nonprofit Accounting & Financial Statements*, by Thomas Ittelson
    - This article was informed by Ittelson's book.*****
- Read *Nonprofit Bookkeeping & Accounting for Dummies*, by Sharon Farris