



k·squaredSM

*Financial and Operational
Business Consulting*

Butler MBA Board Fellowship Program

March 12, 2011

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Types of Nonprofits

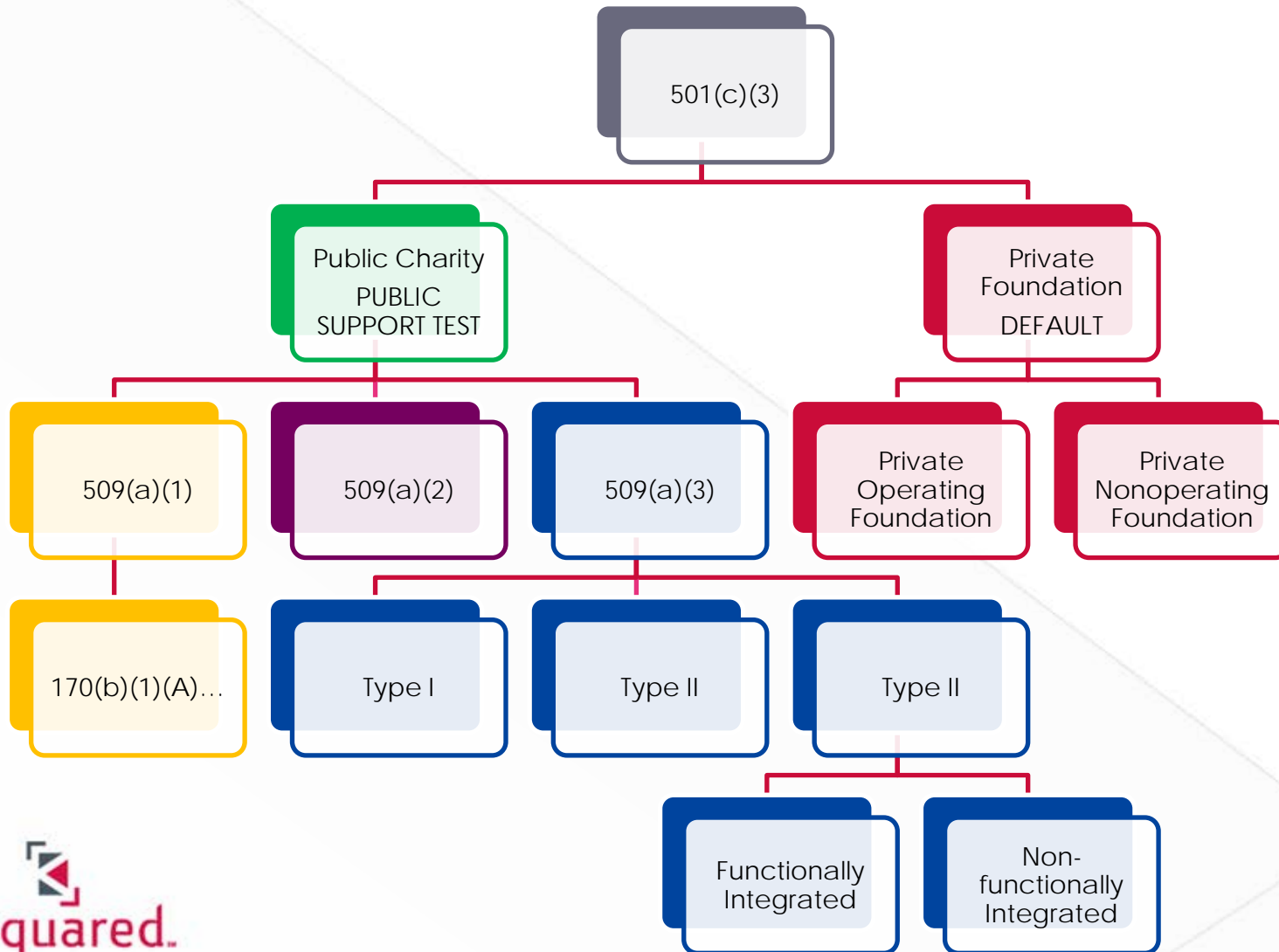
- 501(c)3: Organizations formed for educational, scientific, literary, charitable or religious pursuits

(only classification for which donations are deductible)

Types of Nonprofits

- 501(c)4: Social welfare organization – usually focus on advocacy
- 501(c)5: Labor unions and agriculture
- 501(c)6: Business and trade associations
- 501(c)7: Social and recreational clubs
- 501(c)10: Domestic fraternal societies and associations
- In total, there are 28 different 501(c) org's!

“Not-for-Profit”



“Not-for-Profit”

- Arts & Culture
- Human Services
- Health
- Education
- Environment
- Economic Development
- Advocacy and Lobbying

“Not-for-Profit”

- Religious
- Fraternal
- Service
- Professional Societies
- Private Foundations

Not-for-Profit



Cannot Make a Profit

Fiduciary Responsibility

- **A Fiduciary:** An individual, corporation or association holding assets for another party, often with the legal authority and duty to make decisions regarding financial matters on behalf of the other party.
- **Legal Responsibility:** A board and its individual members are considered agents of a corporation and are **liable for the actions of a nonprofit organization.**

Financial Statements

- Statement of Financial Position
- Statement of Activities
- Statement of Cash Flows
- Statement of Functional Expenses
(Voluntary Health and Welfare Organizations)

Stmt. of Financial Position

- For-profit comparison: Balance Sheet
- This is what the organization owns, \$ they owe others and \$ others have committed to paying/giving them
- Information provided:
 - Liquidity
 - Donor restrictions
 - Net assets

**National Youth Training and Resources Organization
Comparative Statements of Financial Position
For the Years Ended December 31, 1999 and 2000**

	<u>2000</u>	<u>1999</u>
Assets		
Cash	\$ 200,000	142,000
Pledges Receivable (net)	120,000	65,000
Investments	755,000	700,000
Prepaid Expenses	15,000	13,000
Fixed Assets (net)	220,000	40,000
Total Assets	<u>\$ 1,310,000</u>	<u>\$ 960,000</u>
Liabilities and Net Assets		
Liabilities		
Accounts Payable	50,000	60,000
Grants Payable	25,000	
Refundable Advances	20,000	
Long Term Debt	200,000	-
Total Liabilities	<u>\$ 295,000</u>	<u>\$ 60,000</u>
Net Assets		
Unrestricted	\$ 325,000	\$ 300,000
Temporarily Restricted	45,000	-
Permanently Restricted	645,000	600,000
Total Net Assets	<u>\$ 1,015,000</u>	<u>\$ 900,000</u>
Total Liabilities and Net Assets	<u>\$ 1,310,000</u>	<u>\$ 960,000</u>

Donor Restrictions

Net Assets

Unrestricted Net Assets minus Fixed Assets = \$105,000 Unrestricted



Statement of Activities

- For-profit comparison: Income Statement
- This is how much \$ the organization has earned and how and where they have spent their \$
- Information provided:
 - Diversification of revenue
 - Program expense versus supporting services
 - How an organization utilizes its resources
 - Investment performance
 - Operating within constraints of resources?

National Youth Training and Resources Organization
Statement of Activities
For the Year Ended December 31, 2000

Investment Performance

Changes in Unrestricted Net Assets:	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenues and Gains:				
Public Contributions (net)	\$ 800,000	\$ 165,000	\$ 45,000	\$ 1,010,000
Program Service Revenue	46,000			46,000
Investment Income	42,000	5,000		47,000
Net Assets Released from Restrictions	125,000	(125,000)		0
Total Revenues, Gains, Other Support	\$ 1,013,000	\$ 45,000	\$ 45,000	\$ 1,103,000
Expenses and Losses:				
Program Services	\$ 676,000			\$ 676,000
General Administration	197,000			197,000
Fund-Raising	115,000			115,000
Total Expenses and Losses	\$ 988,000			\$ 988,000
Increase in Net Assets	\$ 25,000	\$ 45,000	\$ 45,000	\$ 115,000
Net Assets at Beginning of Year	300,000	0	600,000	900,000
Net Assets at End of Year	\$325,000	\$45,000	\$645,000	\$1,015,000

Diversification of Revenue

Utilization of Resources



Operating Within
Constraints of Resources

Stmnt of Functional Expenses

- No for-profit comparison
- Provides more detail on how \$ was spent
- Tells you “natural” expenditures, expenses by program/activity, overhead

Stmt. of Functional Expenses

- Natural expense versus functional expense

	<u>Program</u>			<u>Total</u>	<u>Management</u>	<u>Fund</u>	<u>Total</u>
	<u>A</u>	<u>B</u>	<u>C</u>	<u>Program</u>	<u>and General</u>	<u>Raising</u>	
Salaries, wages, and benefits	\$7,400	\$3,900	\$1,725	\$13,025	\$1,130	\$960	\$15,115
Equipment maint and rental	2,075	750	1,925	4,750	0	0	4,750
Supplies and travel	865	1,000	490	2,355	240	560	3,155
Services and professional fees	160	1,490	600	2,250	200	390	2,840
Office and occupancy	1,160	600	450	2,210	218	100	2,528
Depreciation	1,440	800	570	2,810	250	140	3,200
Interest	0	0	0	0	382	0	382
Total expenses	\$13,100	\$8,540	\$5,760	\$27,400	\$2,420	\$2,150	\$31,970

National Youth Training and Resources Organization
Statement of Functional Expenses
For the Year Ended December 31, 2000

	Program Services		Supporting Services		Total Expenses
	Educational/ Scholarships	Recreational Programs	General Administration	Fund- Raising	
Salaries	\$ 65,000	\$ 88,000	\$ 82,000	\$ 15,000	\$ 250,000
Employee Benefits	15,000	22,000	20,000	3,000	60,000
Payroll Taxes	7,000	11,000	10,000	1,500	29,500
Total Personnel Costs	\$ 87,000	\$ 121,000	\$ 112,000	\$ 19,500	\$ 339,500
Professional Fees	-	-	-	45,500	45,500
Supplies	45,000	10,000	8,000	8,000	71,000
Telephone	10,000	15,000	7,000	7,000	39,000
Postage	10,000	5,000	5,000	3,000	23,000
Occupancy Costs	20,000	20,000	15,000	3,000	58,000
Equipment Rental and Maintenance	5,000	5,000	20,000	-	30,000
Printing and Publications	20,000	45,000	\$ 2,000	26,000	93,000
Travel	40,000	40,000	\$ 1,000	3,000	84,000
Conferences and Meetings	20,000	15,000	7,500	-	42,500
Scholarships	143,000	-	-	-	143,000
Interest	-	-	14,500	-	14,500
Total before Depreciation	\$ 400,000	\$ 276,000	\$ 192,000	\$ 115,000	\$ 983,000
Depreciation	-	-	5,000	-	5,000
Total Expenses	400,000	276,000	197,000	115,000	\$ 988,000

How are allocations determined?

Unique Financial Aspects

- Endowments *
 - Donor restricted
 - Board restricted
- Restricted funds *
- Key financial ratios *
- Internal financial management – cash basis
- Sustainability
- Cost of services
- Staff as a percentage of total cost

Restricted Funds

- Restricted **only** by donor
- Temporary restriction
 - Purpose or time
- Permanent restriction
 - Use of earnings on permanently restricted funds
- Use of funds
- How do you change or eliminate a restriction??

Reserve vs. Endowment

- Operating reserve
 - An unrestricted fund balance set aside to stabilize a nonprofit's finances by providing a cushion against future unexpected cash-flow shortages, expenses or losses.
 - What is a reasonable amount?
- Endowment
 - A fund that is made up of gifts and bequests that are generally subject to a requirement that the principal be maintained intact and invested to create a source of income for an organization.

Endowment

- Donor restricted
 - Permanent restriction
 - Temporary restriction
 - Use of Earnings
- Board restricted
 - Unrestricted

Financial Considerations

- Operating reserve/working plan to establish
- Positive/growing/sustained net assets
 - Unrestricted versus restricted
 - Multiple years of deficits?
- Comparison between years
 - Trends
- Comparison to budget
- Reasonable overhead percentage
- Diversification of revenue*

Key Financial Questions

- Does the organization have a diversity of funding sources?
 - What is diverse?
 - Diversity of fundraising sources
 - What is the fundraising strategy?
 - Dependency on few funding sources?
 - Allocation/diversity of funding sources

Key Financial Questions



- Does the organization have sufficient reserves? Are they wisely invested?
- How is the budget (expense and revenue) determined? Is this reasonable and realistic?
- Fundraising strategy?
- Thinking beyond one year?
- Management Recommendation Letter

Key Financial Questions

- Is the financial plan consistent with the strategic plan?
- Is the organization filing all of the required documents?
 - Form 990 (Federal) * – **Request a copy**
 - Form 990T (if necessary) *
 - Form NP20 (Indiana)
 - Property tax exemption and return
 - Sales tax exemption
 - Other?

Sales Tax Exemption

- File Form NP-20A to obtain exemption from paying sales tax
- Use NP-1 (ex. Below) when making purchases

 Form NP-1 State Form 51065 (4-03)	Indiana Department of Revenue Indiana Government Center North Indianapolis, Indiana 46204 Indiana Nonprofit Sales Tax Exemption Certificate (This certificate may not be used to collect sales tax)	TID: 0128566345 LOC: 000 Corresp ID: 0700045904607 Issued: 07/17/2007
0700045904607  IMPACT 100 GREATER INDIANAPOLIS PO BOX 40531 INDIANAPOLIS, IN 46240-0531		
Organization is only exempt from payment of sales tax on purchases for which the organization is granted exemption.		

Ratios – What They Indicate

Current Ratio

$$\frac{\text{Current Assets}}{\text{Current Liabilities}}$$

- Ability to pay current liabilities as they mature (higher number is better)

Quick Ratio

$$\frac{\text{Cash and Cash Equiv}}{\text{Current Liabilities}}$$

- Ability to pay current liabilities with only cash and cash equivalents (higher number is better)

Current Ratio

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Current Portion?

4.47

Quick Ratio

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Current Portion?



2.67

Ratios – What They Indicate

Debt to
Equity Ratio

$$\frac{\text{Total Liabilities}}{\text{Net Assets}}$$

- Indicates the balance between “equity” and debt
- The greater the number, the “more leveraged” the organization

“Highly Leveraged” is **not** a good thing.....

Debt to Equity Ratio

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.29

Ratios – What They Indicate

- Balance spent on **mission** (program) in relation to total expenses (higher number is better)
 - At least 65% - 70%

$$\frac{\text{Total Program Expenses}}{\text{Total Expenses}}$$

Program services
to total expense

- Relationship between overhead expenses to total expenses (lower is better)
 - No more than 30% - 35%

$$\frac{\text{Total Fundraising, Mgmt \& General Expenses}}{\text{Total Expenses}}$$

Supporting services
to total expense

National Youth Training and Resources Organization
Statement of Activities
For the Year Ended December 31, 2000

% spent on Program

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68%

% spent on M&G

**National Youth Training and Resources Organization
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32%



Ratios – What They Indicate

- **Efficiency** of fundraising (lower number is better)
 - Cost per \$100 raised
 - Factors affecting fundraising costs

$$\frac{\text{Total Fund-Raising Expenses}}{\text{Total **Related** Contributions}}$$

FR Expense to
Funds Raised

National Youth Training and Resources Organization
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\$11.39 per \$100 raised

**“Data is valid only
when viewed in the
context of the
single, specific
organization for
which it has been
computed.”**

Financial Statement Audit: Role of the Board

- Selection of Auditor
- Approval of Financial Statements
- Finance, Audit, Investment Committees
 - Independence of audit committee
 - Involvement of management
 - Separation of committee responsibilities

Does the Organization Need an Audit?

- Who is requesting an audit?
 - Grantor or other funder
 - Board
 - Executive Director
 - Other?
- When should an audit be conducted?
 - Federal requirements (\$500,000 of federal funds)
 - Size of organization ($\$0 < \$250,000 < \$1,000,000$)
 - Audit vs. Review vs. Compilation

Audit vs. Review vs. Compilation

	Audit	Review	Compilation
Level of Assurance	Reasonable (Highest Level)	Limited	None
Procedures Performed	Verification and Substantiation	Inquiry and Analytical Procedures	Basic
Obtain Understanding of Internal Ctrl?	Yes	No	No
Test Effectiveness of Internal Ctrl?	Frequently, not always	No	No
Test Transactions	Yes	No	No
Express Opinion on Financial Statements?	Yes	No	No

Financial Statement Examples

- Group Activity

Form 990

- Information return (vs. tax return)
- Public document (except Schedule B)
- **A marketing tool!!**
- Revisions to 2008 Form 990
 - Last revision 1979
 - Transparency, accountability
 - Reflect changes in NFP sector
 - Promote compliance
- Who is preparing your Form 990?

Form 990-EZ

- May file Form 990-EZ if:
 - For 2008 tax year, gross receipts are less than \$1 million and total assets are less than \$2.5 million.
 - For 2009 tax year, gross receipts are less than \$500,000 and total assets are less than \$1.25 million.
 - For 2010 and later tax years, gross receipts are less than \$200,000 and total assets are less than \$500,000.

Form 990-N

- Must file electronically (<http://epostcard.form990.org>)
- EIN
- Tax Year
- Legal name and mailing address
- Any other names the organization uses
- Name and address of principal officer
- Web site address
- Confirmation org's annual gross receipts are normally \$25,000 or less
- If applicable, a statement that the organization has terminated or is terminating (going out of business)

Form 990-PF

- Annual return for Private Foundations
- Private Foundations subject to excise tax on investment earnings
- 5% distribution requirement
- More restrictive than public charity

Org's Not Req'd to File Form 990

- Certain religious organizations (e.g., churches, temples)
- Certain governmental organizations
- Certain political organizations

Form 990 – Role of the Board

- Disclosure on Form 990: Was a copy provided to governing body before filed?
- Familiarity with contents!

Overview of New Form 990

- Summary page with signature block
- Statement of program service accomplishments
- Checklist of required schedules
- Statements regarding other IRS filings and tax compliance
- Governance, management and disclosure
- Compensation Reporting
- Financial Reporting

The Summary – Page One

- New to the Form 990
- Provides an overview of the organization
- Highlights the organization's
 - Activities
 - Governance
 - Revenue
 - Expenses

Accomplishments – Page Two

- Opportunity to highlight accomplishments
- Complete info for three largest programs
 - Total revenue
 - Total expenses
 - Describe achievements
- Significant changes (additions, deletions, modifications) to programs identified

Schedules

A. Public Charity Status	I. Grants and Other Assistance Provided to Others
B. Schedule of Contributors	J. Compensation Information
C. Political and Lobbying	K. Tax Exempt Bonds
D. Supplemental Financial	L. Transactions with "Interested Persons"
E. Schools	M. Non-Cash Contributions
F. Foreign Activities	N. Liquidation/Termination/Dissolution/Significant Disposition of Assets
G. Fundraising and Gaming	O. Supplemental Information
H. Hospitals	R. Related Organizations and Unrelated Partnerships



	No changes
	Schedule A
	NEW
	Similar info

Form 990 – Key Items

- Summary financial information (Part I)
- Program service accomplishments (Part III)
- Excess benefit transactions (Part IV, questions 25a & b)
- Governance and Management (Policies) (Part VI)
- Compensation (Part VII) (Schedule J)
- Board of Directors (Part VII)

Form 990 – Key Items

- Transactions with “interested persons” (Schedule L)
- Further explanations of items within forms and schedules (Schedule O)
- Related organizations (Schedule R)
- **ALSO:**
 - Stmt of Revenue (Part VIII)
 - Stmt of Functional Expenses (Part IX)
 - Balance Sheet (Part X)

Executive Compensation

- Process
 - Question on Form 990 Part VII:
 - Independent review and approval
 - Comparable data
 - Written documentation of deliberation and decision
 - UWCI survey
- Expense reimbursement
- Risk of excess benefit transactions
- Deferred compensation differences

Part VII: Who and What to Report

Who	What
Current Officers, Directors and Trustees	No minimum threshold, report all compensation
Current Key Employees	Report those paid over \$150,000 of reportable compensation
Current Five Highest Compensated Employees	Report those paid over \$100,000 of reportable compensation
Former Officers, Key Employees and Highest Compensated	Report those paid over \$100,000 of reportable compensation
Former Directors and Trustees	Report those paid over \$10,000 in capacity as former director or trustee

Presentation

Form 990 Schedule

Name and Title	Average Hours Per Week	Position (check all that apply)						Reportable Compensation from the Organization	Reportable Compensation from Related Organizations	Estimated Amount of Other Compensation from the Organization and Related Organizations
		Individual Trustee or Director	Institutional Trustee	Officer	Key Employee	Highest Compensated Employee	Former			

Schedule J – more extensive

Part I Questions Regarding Compensation

	Yes	No								
<p>1a Check the appropriate box(es) if the organization provided any of the following to or for a person listed in Form 990, Part VII, Section A, line 1a. Complete Part III to provide any relevant information regarding these items.</p> <table border="0"> <tr> <td><input type="checkbox"/> First-class or charter travel</td> <td><input type="checkbox"/> Housing allowance or residence for personal use</td> </tr> <tr> <td><input type="checkbox"/> Travel for companions</td> <td><input type="checkbox"/> Payments for business use of personal residence</td> </tr> <tr> <td><input type="checkbox"/> Tax indemnification and gross-up payments</td> <td><input type="checkbox"/> Health or social club dues or initiation fees</td> </tr> <tr> <td><input type="checkbox"/> Discretionary spending account</td> <td><input type="checkbox"/> Personal services (e.g., maid, chauffeur, chef)</td> </tr> </table>	<input type="checkbox"/> First-class or charter travel	<input type="checkbox"/> Housing allowance or residence for personal use	<input type="checkbox"/> Travel for companions	<input type="checkbox"/> Payments for business use of personal residence	<input type="checkbox"/> Tax indemnification and gross-up payments	<input type="checkbox"/> Health or social club dues or initiation fees	<input type="checkbox"/> Discretionary spending account	<input type="checkbox"/> Personal services (e.g., maid, chauffeur, chef)		
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<input type="checkbox"/> Travel for companions	<input type="checkbox"/> Payments for business use of personal residence									
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b If line 1a is checked, did the organization follow a written policy regarding payment or reimbursement or provision of all of the expenses described above? If "No," complete Part III to explain	1b									
2 Did the organization require substantiation prior to reimbursing or allowing expenses incurred by all officers, directors, trustees, and the CEO/Executive Director, regarding the items checked in line 1a?	2									
<p>3 Indicate which, if any, of the following the organization uses to establish the compensation of the organization's CEO/Executive Director. Check all that apply.</p> <table border="0"> <tr> <td><input type="checkbox"/> Compensation committee</td> <td><input type="checkbox"/> Written employment contract</td> </tr> <tr> <td><input type="checkbox"/> Independent compensation consultant</td> <td><input type="checkbox"/> Compensation survey or study</td> </tr> <tr> <td><input type="checkbox"/> Form 990 of other organizations</td> <td><input type="checkbox"/> Approval by the board or compensation committee</td> </tr> </table>	<input type="checkbox"/> Compensation committee	<input type="checkbox"/> Written employment contract	<input type="checkbox"/> Independent compensation consultant	<input type="checkbox"/> Compensation survey or study	<input type="checkbox"/> Form 990 of other organizations	<input type="checkbox"/> Approval by the board or compensation committee				
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<input type="checkbox"/> Form 990 of other organizations	<input type="checkbox"/> Approval by the board or compensation committee									
4 During the year, did any person listed in Form 990, Part VII, Section A, line 1a:										
a Receive a severance payment or change of control payment?	4a									
b Participate in, or receive payment from, a supplemental nonqualified retirement plan?	4b									
c Participate in, or receive payment from, an equity-based compensation arrangement?	4c									
If "Yes" to any of lines 4a–c, list the persons and provide the applicable amounts for each item in Part III.										



Other Comp. Disclosures (cont.)

- Also must disclose/describe:
 - Written policy regarding reimbursed expenses?
 - Requirement for substantiation of reimbursed expenses?
 - Describe who establishes compensation of CEO/Executive Director
 - Contingent compensation
 - Equity based compensation
 - Accrued/deferred Compensation

Schedule J: When to File

- For any compensation to a former officer, director or trustee, key employee or highest compensated employee
- For any Part VII individual whose reportable compensation and other compensation total more than \$150,000
- For any person on part VII who received compensation from another organization for services to the organization

Role of the Board – Executive Compensation

- Approve CEO/President/Executive Director Compensation

Form 990 Examples

- The Children's Museum of Indianapolis
- Dress for Success Indianapolis
- Impact 100 of Greater Indianapolis

QUESTIONS??

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