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Profitable Solutions for Nonprofits

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Ratios to the rescue

Assess your nonprofit's health by the numbers

As much as you might prefer to concentrate on only your nonprofit's mission, strong financial health is vital to pursuing those goals. Financial statements provide essential information on your fiscal footing. However, you can expand everyone's understanding of your organization's performance and sustainability by monitoring a variety of ratios.

Reasons to "ratio-nalize"

While financial statements will always play an important role, they aren't necessarily the best way to communicate performance to stakeholders. Ratios grab information from your financial statements and can be presented as easy-to-process snapshots.

Ratios also help stakeholders keep an eye on overall financial condition, identify worrisome and promising trends, and make informed decisions. Among other things, they can provide a picture of your organization's current financial standing, its adequacy and use of resources, and its reliance on certain types of funding. Ratios also are an invaluable tool for your leaders' decision-making.

Financial standing

Here are some ways to calculate your organization's general financial health:

Current ratio = Current assets / Current liabilities. The current ratio indicates the ability to satisfy short-term financial obligations (debts due within the coming year). A current ratio of "1" or more generally demonstrates the ability to meet those obligations.

Accounts receivable (A/R) ratio = Accounts receivable aged more than 90 days / Total accounts receivable. As the A/R ratio gets higher, the risk of collection or billing problems — and, in turn, cash flow issues due to lack of expected revenue — grows.

Accounts payable (A/P) ratio = Accounts payable aged more than 90 days / Total accounts payable. The A/P ratio can reflect cash flow or more severe financial problems. For example, the organization may be having trouble paying its bills on time.

Ability to cover costs

These ratios compare your nonprofit's liquid assets to the ongoing cost of operations:

Defensive interval (DI) = Cash plus marketable securities (excluding permanently restricted investments) plus current receivables / Average monthly expenses. The DI measures the number of months' expenses the organization can cover if no additional inflows of quick assets occur. It's particularly useful when contribution inflows are highly variable. A high or increasing value generally is better than a low value.

Liquid funds indicator = Fund balance less restricted endowments, land and plant, property and equipment / Average monthly expenses. This indicator shows the number of months before the nonprofit will completely exhaust its liquid funds, assuming no additional revenue inflows. Because it excludes restricted endowments, it's more conservative than the DI. But like the DI, high or increasing values are positive indicators.

Use of funds

How efficiently and effectively do you use your resources? Consult these ratios:

Fundraising efficiency = Contributed income / Fundraising expense. In recent years, many donors have focused on the amounts nonprofits spend on fundraising compared with the amounts raised. This ratio shows the average dollar amount raised for each dollar in fundraising spending.

Program expense ratio = Program expense / Total expenses. The ratio evaluates a nonprofit's mission efficiency by considering the extent of funding that goes to programs, as opposed to administrative or other expenses. Alternatively, stakeholders may scrutinize the administrative expense ratio, calculated by swapping out program expense for administrative expense.

Cost per unit of service = Program expense / Number of units of service. When nonprofits provide identifiable units of service (for example, meals served), this ratio assesses the financial efficiency of the program over time.

Overreliance on funding sources

Reliance ratios. Finally, reliance ratios can reveal an unhealthy dependence on one funding source. To determine your reliance on any specific funding type (for example, government grants and contracts, individual donations or earned income), divide the amount of that funding by total income.

Say the ratios show that your organization receives almost all of its support from government funding and individual donations. You could see those sources recede if a recession hits, threatening your survival. So, you'd be wise to find ways to diversify your income now.

Performance matters

In a time when charitable-giving incentives are shrinking, nonprofits need to pay more attention than ever to their financial performance. The ratios above can help you steer away from potential problems and market your organization effectively to donors. ■

Making the most of financial data

To use ratios effectively, first determine which ones are most appropriate for your organization. Different nonprofits have different revenue sources, donation and expense patterns, and financial vulnerabilities. Also, the adage "garbage in, garbage out" applies to financial ratios. The ratios are only as reliable as the data used to compute them. Your nonprofit must take steps to ensure that its financial information is accurate, complete, and calculated in a consistent manner.

Finally, you'll want to calculate financial ratios across periods — whether monthly, quarterly or annually. A single-period ratio can shine some limited light on an organization's financial health, but it's of little use for decision-making by leaders. Stakeholders can learn more from watching trends. And even trends must be viewed in the context of relevant internal and external factors, such as a significant one-time gift or an economic downturn.

Landing corporate backing requires a game plan

When the economy is good, corporations tend to be more generous with their donations to not-for-profit organizations. But competition can be stiff and companies don't give away dollars hastily. Groups that make well-thought-out pitches to corporations — and support their requests with solid facts and figures — have the best chance at securing corporate backing.

Where should you focus your efforts?

Unless you have unlimited development resources, you're probably better off focusing on companies with which you have an actual connection. Businesses like to partner with "natural fits" that share their goals, values, and service areas. And they often choose a single theme or focus. For example, pharmaceutical giant Merck works with charities fighting to reduce maternal mortality around the world. And as part of its commitment to boost economic activity, JPMorgan Chase pledged $100 million a few years ago to help revitalize the city of Detroit — help that included deploying its "service corps" of employees to lend a hand to local nonprofits.

Indeed, organizations that enable a corporate donor's employees to get involved often have an advantage. If a firm's charity of choice is a food bank, its employees might volunteer to do everything from providing strategic advice to the organization to repacking fresh produce for distribution to the community's needy.

Companies may also be receptive to charities whose mission matches that of key executives' personal interests. For instance, a company might donate to and raise money for a cancer charity if the child of a company executive suffers from a rare form of the disease.

What will you need to prove?

It's not enough, however, for your nonprofit to match the general interests of a company or its CEO. You also need to make a clear, compelling case that

their corporate dollars will be well spent. Companies want to align themselves with fiscally responsible organizations that can prove they get results.

Companies are likely to ask such questions as: Is your organization self-sustaining? What kind of outcomes does it achieve? Are the outcomes measured in both qualitative and quantitative ways? How much do you spend on programs vs. administration and other costs? What other forms of financial support do you receive?

Although most businesses understand the PR value of donating to or partnering with a charity, it doesn't hurt to remind them of the benefits — for example, community goodwill, increased name recognition, tax breaks, and improved recruiting and employee retention. Emphasize that donations are investments and that the work that donations make possible is a corporate giver's return on the investment.

Should you simply ask for money?

When you approach potential corporate supporters, don't just ask for a check. Some businesses may not be in the position to give generously at that moment. Or they may be looking for a different kind of relationship with your charity. Instead, brainstorm ways your nonprofit and the business can work together for mutual benefit. Here are some ideas:

As mentioned above, some companies encourage their employees to contribute *volunteer time* to a not-for-profit. Consider organizing a day of service with a company that enables the entire office to participate (and still get paid) while your nonprofit tackles a major project (such as repainting your facility). Or ask local employers to consider implementing a matching program that makes financial grants to the nonprofits where their employees contribute or volunteer.

You also might want to inquire about *donated services*. Most people are familiar with pro bono legal services, but other professional firms (accounting, PR, marketing, technology) may also be willing, even eager, to lend your nonprofit their expertise on a short- or long-term basis.

Consider asking for *gifts-in-kind*. Many manufacturers and retailers end up with excess inventory that could be donated — if only the businesses knew whom to give it to. Say you run a food bank. You could contact local food producers, grocers, restaurants and caterers to indicate your interest in their unsold, but perfectly edible, goods.

Be included

According to Giving USA, businesses donated nearly $20.8 billion to charity in 2017 (the last year of data available). This marks an increase of 5.7% (adjusted for inflation) over 2016. To join the groups enjoying greater corporate largesse, your organization needs to develop corporate relationships wisely and strategically. ■

Should you accept that new grant?

Grants — whether from a government agency or a private foundation — are among the most important funding sources for many nonprofits. It's easy to understand why so many organizations are quick to accept every new grant that comes their way. However, that eagerness can backfire in costly and time-consuming ways.

Unpleasant surprises

By its very nature, the nonprofit industry has long been "resource-challenged." Under such ongoing financial pressures, you can't afford to blithely pass up offers of support. Yet you also should avoid blindly accepting grants; doing so could leave you shouldering excessive administrative burdens, cost inefficiencies and lost opportunities.

Smaller or newer nonprofits aren't the only ones at risk of such unexpected consequences. You might think that larger, more mature organizations would have formal grant evaluation processes in place. But that's not always the case.

Further, as an organization grows, it has significantly more opportunities to expand the scope of its programming. This expansion can open the door to more grants, including some that are outside of the organization's current expertise and experience. The organization could end up accepting a grant with requirements to fulfill and struggles it didn't anticipate.

Critical factors

Nonprofits often find it difficult to quantify all the costs and benefits associated with a potential grant. At the very least, though, you should consider the following before accepting any new funding:

Administrative requirements. A small grant can bring a sizable administrative burden. For example, you could be caught off guard by the reporting requirements that come with a grant as small as $5,000. You might not have staff with the requisite reporting experience, or you may lack the processes and controls to collect the necessary data. Often government funds passed through to your nonprofit still carry the requirements that are associated with the original funding, which can be quite extensive.

Grants that go outside of an organization's original mission can pose problems, too. Not only might the grant not consider your learning curve and additional costs, but you might also face an IRS challenge to retaining your exempt status.

Cost inefficiencies. A grant can create unforeseen inefficiencies that undermine its face value. New grants from either federal or foundation sources may have explicit administrative requirements your organization must satisfy.

Nonprofits often find it difficult to quantify all the costs and benefits associated with a potential grant.

Additionally, your nonprofit might run up expenses to complete the program that aren't allowable or reimbursable under the grant. You must net all these costs against the original grant amount to determine its benefit to you.

Lost opportunities. For any unreimbursed costs associated with new grants, consider how else your organization could spend that money (and staff resources). Could you get more mission-related bang for your buck if you spent it on existing programs?

Quantifying the benefit of a new grant or program can be equally (or more) challenging than identifying its costs. You should evaluate *every* program to quantify its impact on your mission. This will allow you to answer the critical question when evaluating a potential grant: Are there existing programs that can be expanded using the same funds to yield a greater benefit to your mission?

Look before you leap

Grants from the government or a foundation can help a nonprofit expand its reach and improve its effectiveness in both the short and long term. They also can hamstring organizations in unexpected ways. Do your homework before you sign on the dotted line. ■

NEWSBITS

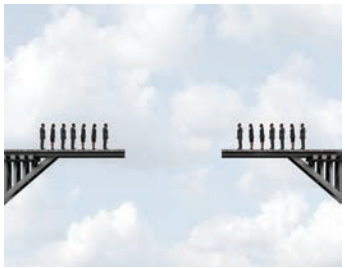
Cryptocurrency donations pose problems

It's hard enough figuring out how to manage donations of art or other nonfinancial assets — now some nonprofits must navigate the challenges that come with cryptocurrency donations. According to Bloomberg, several colleges and universities have recently received crypto donations. These can raise accounting questions, complicate tax filings and require special storage or security.

For example, because the IRS considers cryptocurrency to be property, nonprofits must take more steps than when they process cash or securities donations. Moreover, cryptocurrency has proven subject to dramatic swings in value that make it difficult to determine the optimal time to cash in.

As Bloomberg reports, the University of Puget Sound immediately sold an alumnus's donation of 14.5 Bitcoin for about $10,000 in 2014. Subsequently, the value climbed to more than $200,000. Of course, the value also could have dropped. ■

Foundations out of touch with nonprofits' needs, study says



Foundations aren't as tuned into nonprofits' needs as they think they are, a Center for Effective Philanthropy survey reveals. The survey report, *Strengthening Grantees: Foundation and Nonprofit Perspectives*, examines the support that foundations provide grantees to strengthen their organizations.

Based on responses from 170 nonprofit CEOs and 187 foundation leaders, the researchers concluded that nonprofits most desire help in fundraising, staffing and communications. However, the CEOs see grants for general operating support as having the greatest effect on strengthening their organizations.

The findings suggest that both foundations and nonprofits have a role to play in closing the perception gap: Nonprofits are advised to ask for what they really need, rather than what they think funders want to provide. And foundations should work to reduce the dynamics that discourage nonprofits from doing so, by building strong relationships rooted in understanding and transparency. ■

AI bolsters fundraising potential

Nonprofits are beginning to recognize the potential of artificial intelligence (AI) to make data-based predictions about current and potential donors — and even to draft personalized outreach messages. AI generally refers to the use of computer systems to perform tasks commonly thought to require human intelligence, such as problem-solving and decision-making. It includes "machine learning," an iterative process in which machines improve their performance over time.

For example, Cure Alzheimer's Fund improved its major donor retention via machine learning. AI helped the charity develop outreach plans by suggesting which donors to contact each week throughout the year. The result has been a 49% increase in dollars received through fundraising, the Fund reported. ■

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Best Practices for Your Month-End Close

A recent survey by close management software provider FloQast reports that more than 80 percent of accountants describe the month-end closing process as a negative one. Following are a few best practices that we at LaPorte recommend to our clients to help them streamline the month-end close process.

Develop and Document Standard Procedures

In order for your business procedures to be effective, they must first and foremost be documented. A simple way to do this is to create a master checklist of duties. This checklist can detail the steps in the closing process, list who is responsible, and direct when steps need to be completed.

Continuously Improve the Process

Using standard procedures does not require them to be written in stone. Month-end processes can (and should) change as the business grows, technology changes, etc. Ask your employees for help on how to improve the procedures. Let them know how management uses the month-end reports. Together, identify ways to meet these needs and how to improve on providing the information you need. Also consider automating certain procedures. Perfecting new technology, while time-consuming, is a valuable investment going forward.

Cross-Train Your People

Cross-train your employees so that the truly important steps will get done even if a key employee is unexpectedly out of the office. Cross-training is a good internal control measure, ensures the steps will be completed, and provides a fresh set of eyes that may be able to pinpoint overlooked inefficiencies and find solutions.

Communicate with Employees

Let employees know the "whys" behind assignments. Employees understanding why you need the reports, who relies on them, and the importance of receiving them timely will help employees feel more a part of the process and be incentives to do their jobs even better.

Keep Abreast of Accounting Changes

You need to implement constantly changing accounting standards and tax regulations in the month-end close process. While most changes are not difficult to implement, when you are faced with more complex accounting changes, try to look at your process in a fresh, new light. Sometimes a complete overhaul may be more efficient than adjusting your existing closing process.

When in Doubt, Ask

Our final "best practice" tip is to ask for help if you need it. Let your accountants know if you're struggling. Our LaPorte Accounting Services professionals can review your close process and help you fine-tune it.