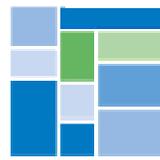




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Board Talking Point: Watching the Dollars

A fundamental and critical responsibility of a nonprofit Board of Directors is to monitor the corporation's financial health. Many board members may feel they lack the expertise needed to effectively monitor finances and are not sure where to begin. However, Board members must overcome this fear and actively review financial information on a regular basis. Because each nonprofit organization has different funding streams and expenses, faces different financial issues and has different resources for financial management, each organization will choose a slightly different set of regular financial reports to prepare and analyze. And, over time as the organization's financial condition changes, the reports requested and reviewed will change.

Questions:

- 1. What documents should the Board review regularly?**
- 2. Should the Board review different documents or review documents more frequently when the organization's financial health is uncertain?**
- 3. Who prepares the financial reports and who reviews them?**
- 4. Is a nonprofit corporation required to have an audit or finance committee? What do these committees do?**

Answers:

- 1. What financial documents should the Board review regularly?**

The answer will depend on several factors, including the extent to which the organization is financially stable, the degree and extent to which the financial picture changes during the period, the availability of cash to meet financial obligations, the availability of staff or other professionals to prepare reports, etc.

When designing your financial reporting schedule, consider including the following reports:

Key Reports

Whether your Board meets monthly or quarterly, below are some of the most important reports to consider. If your board does meet quarterly, these same reports should be reviewed monthly by fiscal staff, the Executive Director, and Treasurer.

At minimum even small nonprofits should generate a Balance Sheet and Budget Variance Report every month. In addition, the Board should be actively involved in developing and should approve the organization's annual budget.

Statement of Position (Balance Sheet) shows what the organizations owns (assets) and what it owes (liabilities) and if it has more assets than liabilities (net assets). This will help answer:

- What is our financial health? Can we pay our bills?
- What resources do we have – in the short, medium, and long term?

Statement of Activities (consolidated) showing budget to actual information (often called the Budget Variance Report). This will help answer:

- What has been our overall financial performance this month and to date?
- How are we doing against our budgeted projections?
- What's the reason or "back story" behind the larger variances (the differences between the budgeted and actual expenses?)

Departmental Income and Expense Statement showing budget to actual information. Having income and expense information by department (including individual programs) or "cost center" is critical to getting a full understanding of the organization's financial health. This report will help answer:

- How are the programs and other cost centers performing?
- How are the pieces faring – in addition to the whole?
- Is specific action called for, such as limiting expenses in certain areas or programs?
- If the organization has government funding, are there modifications that should be made to contract budgets?
- Should changes to foundation grant budgets be requested?

Cash flow projections. Unless your organization has substantial reserves (a year or more of operating expenses in the bank), it is advisable to maintain cash flow projections for your fiscal year. This is especially critical for small organizations, groups struggling with financial uncertainty, and/or organizations with a significant percentage of government funding. Here the focus is strictly on actual cash coming into and leaving the organization. This report will help answer:

- At what points in the year will we most need cash?
- At what points in the year are we on steadier footing?
- Is it necessary to seek short term loans or take other steps (cut costs, for example) to manage cash flow?

An executive summary of financial highlights, analysis, and concerns. This will help answer:

- Have there been any recent financial highlights?
- What are the key trends?
- Has the organization received any important grants?
- What key expenses were incurred?
- What are the explanations for key budget variances?

Additional Reports

Depending on your organization, you may also consider the following supplemental reports (likely on a quarterly basis):

Fundraising Update (showing actuals vs. projections for donations and status reports on all foundation proposals). This will help answer:

- Are fundraising results on track?
- Are our cash flow projections for the next six months – and beyond -- accurate?

Payroll tax reports Most Boards need not review payroll tax reports, but it is helpful to know that these important quarterly reports have been filed – especially if the organization is administering payroll on its own. This will help answer:

- Have payroll tax reports been submitted on time and tax deposits been made?

Fee-for-service report showing number of fee-paying clients and revenue against projections. The need for this report will depend on how big a part of your organization's revenue mix earned income is. If your organization depends significantly on Medicaid billings or some other source of earned income, this is a helpful supplemental report. This will help answer:

- Are we servicing approximately the same number and type of clients as we had anticipated?
- If not, what action or change is appropriate?
- How well are we *collecting* fees from clients?
- Do we need to improve or tighten up our collection procedures?

Annual Reports

Form 990 and CHAR 500. These are federal and state reporting forms that must be filed annually. This will help answer:

- Has the organization fulfilled its reporting responsibilities to federal and state governments?
- Has the organization engaged in any interested party transactions that should be reviewed by the Board?

Audited financial statements for year. Statement of Activities, Statement of Position, Income Statement for each program. Aggregated financial statements with narrative showing key trends. This should help answer:

- What was our financial performance over the past year?
- How does it compare to the previous year?
- In what ways and for what reasons was performance different from the budget?
- What financial implications must be taken into account when planning the upcoming year?
- Can we satisfy our financial reporting requirements to funders?

Management letter from the auditor. This should help answer:

- What changes should we implement related to the financial systems, internal controls, and financial planning?

2. Should the Board review different documents or review documents more frequently when the organization's financial health is uncertain?

The Board of Directors must always take an active role in monitoring the organization's financial health. This is even truer during times of financial uncertainty. If the Board currently meets quarterly it would be appropriate to schedule monthly Board meeting to review financials or delegate that authority to a committee of the Board. These meetings can take place by conference call unless prohibited by the corporation's bylaws or certificate of incorporation. NPCL §708(c). Even if the Board does not formally meet monthly, the person overseeing the finances can circulate key financial reports such as the Balance Sheet, Budget Variance Report, and Cash Flow Projections. If the crisis is severe, the Board or a smaller group of board members (empowered by the full board) should schedule ongoing emergency meetings in between regular meetings. If the organization has a standing finance committee, it is natural to turn to this group for this purpose. This group can provide weekly or even daily assistance to the staff.

The Board should work closely with the organization's staff to determine what reports would be most informative and relatively easy to prepare. Some key reports to consider if your organization is struggling financially include:

Cash flow projections. See above description. In times of financial crisis or uncertainty, this may be the most important report. Consider weekly cash flow projections if the staff or board are making cash-related decisions on a frequent basis (what bills to pay, for example).

Accounts Receivables (AR) Aging Report. This report – which shows what money is owed to you and how long it has been outstanding – can be critical when an organization is faced with cash flow problems. It helps focus staff and board in their efforts to bring in funds. After reviewing the AR Aging Report, for example, a Board member may decide to call a donor about the status of a pledge, or staff may double up their follow-up efforts with a government funder behind on reimbursement.

Accounts Payables (AP) Aging Report. This report shows which of the organization's bills are outstanding – and for how long. When being in the unenviable position of choosing which bills to pay, this report provides important information.

3. Who prepares the financial reports and who should review them?

In a small nonprofit the Board Treasurer or outside accountant/bookkeeper might work with the Executive Director to prepare the financial information for all in-house financial statements and the narrative with financial highlights to be presented to the Board. A Controller or Finance Director would prepare these reports in a larger organization. The Program Director, if you have one, would ordinarily prepare the quarterly fee-for-service report. Similarly, the Director of Development would prepare the quarterly fundraising report.

The Executive Director reviews all reports prior to presenting them to Board members to ensure that the financial information makes sense and can be translated into issues and opportunities facing the organization. In addition, key staff members such as program directors and the director of development should have the opportunity to review income and expense reports for the whole organization – in addition to income and expense reports for their respective functions.

The audit and management letter are addressed directly to the Board of Directors because of its oversight function. Typically, the auditor works with the finance staff to prepare federal and state reports and may be included at board meetings during which presentations are given.

In order for a Board member to fulfill their fiduciary obligation to the corporation they must satisfy the duty of care. This means that Board members must act in good faith and use their common sense in reviewing the corporation's operations. Proper fiscal oversight is among the Board's most important functions. This means that Board members must attend meetings, must review the documents provide to them and must ask questions. To the extent that Board members do not feel comfortable reviewing financial documents and asking questions they need to seek out additional training. This can provided by an outside source or by a board colleague.

4. Is a nonprofit corporation required to have an audit or finance committee? What is the role of these committees?

New York nonprofits corporations are not required to have finance or audit committees. There are, however, situations in which having a finance or audit committee will make it easier for Board members to review reports in greater detail than the full Board is able to.¹ If a corporation wants to form a committee it should first review its bylaws and certificate of incorporation to see if the board is authorized to form a committee. NPCL §712(a). Finance and audit committees will be considered “standing committees” and must consist of three or more board members. *Id.*

Finance Committee

The finance committee is usually charged with overseeing the fiscal health of the organization including actively reviewing financial reports, developing fiscal policies and procedures and overseeing the budgeting process. Recruiting a finance committee can be difficult because few Board members believe they have the fiscal skills to perform the function. However, especially with larger boards where detailed discussions can be challenging, the finance committee serves an important function. Having a finance committee enables a smaller, dedicated group of Board members to review the financial reports in greater detail than the full board. To help the Board fulfill its oversight function, it is important for the Executive Director and the finance committee to present regular reports to the entire board in as clear and concise a manner as possible. These reports should include the financial reports given to the committee and there should be an opportunity for the Board to discuss the reports.

Audit Committee

The function of the audit committee is primarily to select the outside auditors, to meet with them at least once a year upon completion of the audit and to oversee any changes to financial procedure recommended by the auditors. The Treasurer will not usually chair the audit committee although they will be a member of the committee because, at least in part, the auditors are reviewing the work of the Treasurer.²

About Community Resource Exchange

For over 30 years, Community Resource Exchange (CRE) has worked to create a more just, equitable and livable city for all New Yorkers. We provide strategic advice and technical services every year to more than [300 community-based nonprofit organizations](#) confronting social issues such as poverty and [HIV/AIDs](#) in low and moderate income neighborhoods. As one of the most established nonprofit management consulting providers of its kind, CRE provides its clients with information, guidance, [resources for nonprofits](#), skill building and [leadership training for Community Based Organizations](#) to make New York City stronger - one community group at a time.

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¹ For more information on the role of the finance and audit committees and the role they play in corporate governance see *Final Report from the Panel on the Nonprofit Sector* http://www.nonprofitpanel.org/report/final/panel_final_report.pdf.

² For information on the function of the audit committee and internal financial controls, see *Internal Controls & Financial Accountability for Not-for-Profit Boards* <http://www.charitiesnys.com/pdfs/Internal%20Controls%20-%20Final%20-%20Small%20Type.pdf>.