

# Prudent Grantmaking Guidelines - The Financial Analysis

January 9, 2014

Elizabeth L. Mathieu, Esq., TEP  
Mathieu & Ranum, PLLC  
(208) 928-6975



# What is Financial Analysis?

- Going beyond community reputation and general impressions to “hard facts”:
  - Is the Organization stable?
  - Is the project rooted in financial reality?



# Purpose of This Discussion

Questions to go behind the numbers to find

## **Red Flags**

of potential risks

that could endanger the success of the project

# How to Access Financial Information

- **Budget**
- **IRS Form 990 – past 3 years**
- **Or**
  - **Statement of Activities (Income Statement) – 3 years**
  - **Balance Sheet – 3 years**
- **Site Visit**

Also, maybe...

- Cash Flow Statement
- Annual Report
- Audited Statements (*State law – Idaho does not require; but if fundraise in other states or asked for by donors*)
  - Are the reports/information consistent?
    - Timely?
  - Clear enough to be useful to your analysis?



# Project Budget

- Should state revenues (and sources) to support Project and its expenses for a time period.
- Direct and indirect expenses should be included. (overhead allocations, ex. salaries, operating costs of organization, insurance etc.)

# Proposed Project Budget - Questions

- What are the major assumptions underlying the budget and are they realistic?
- Is there a project plan and is it realistic in light of resources (financial and human) available?
- Are the revenues and expenses in line with other current and past projects of the charity?
- Are the revenues projected to support the project well diversified and if not already in the charity's hands...
  - Are they in line with charity's ability to fundraise ?
    - Check history regarding other projects and generally in previous years.



# Statement of Activities (Income Statement)

- States revenue and expenses over a time period
- Surplus = profit
- Deficit = loss
  - Take from previous surpluses or will have future liabilities

Impacts the Balance Sheet



# Sources of Revenue

- Contributions
  - Unrestricted
  - Temporarily Restricted by Donor for use in year reported
  - Permanently Restricted by Donor for use in year reported
- Contributed Goods
  - Value calculated at what the charity would have paid if bought
- Contributed Services
  - Specific skills
  - Would have bought if not contributed
- Earned Revenue (programs, investments, other)





# Revenue - Questions

- Are the sources of revenue well diversified (ex. numerous donors, events, investments, government funding) and growing?
- Are actual revenues fairly close to budgets over the past 3 years?
- Are any significant changes from previous years explainable?



# Expenses

- General Overhead (ex. compensation, payroll taxes, legal, accounting, travel, conferences, other)
- Programs/Projects
- Fundraising activities



## Expenses - Questions

- Are any line items larger than seems reasonable?  
(ex. *Compensation, travel, vendors*)
- Do expenses track with budgets over the past 3 years?
- Do fundraising expenses seem high as compared to net resulting revenue?
- Operating deficits for more than a year?



# Balance Sheet

## Snapshot at One Point in Time

### Assets

Cash

Pledges Receivable (net)

Investments

Prepaid Expenses

Fixed Assets (net)

*Total Assets*

### Liabilities and Net Assets

Liabilities

Accounts Payable

Grants Payable

Refundable Advances

Long Term Debt

*Total Liabilities*

Net Assets

Unrestricted

Temporarily Restricted


Permanently Restricted

*Total Net Assets*

*Total Liabilities and Net Assets*

# Balance Sheet - Questions

- Are current assets more than current liabilities so you are comfortable charity can pay its bills?
- Is cash + investments = 6 mo. + of operating expenses?
- Have Accounts Payable or Receivable changed significantly in comparison to previous years? Why? Is the charity paying its bills + collecting amounts owed in a timely manner?
- Is the charity investing its cash and investments prudently?
- Are Unrestricted Net Assets growing for future rainy days?



IRS Form 990  
Has Answers to  
Many Financial Questions

# Required Annual IRS Filing of Form 990

IRS Form 990 (2010 tax year and later)**	Form to File
Gross Receipts < \$50,000	990-N
Gross Receipts < \$200,000 and Total Assets < \$500,000	990-EZ
Gross Receipts ≥ \$200,000 and Total Assets ≥ \$500,000	990

\*\* Charities' filings are available on [Guidestar.org](http://Guidestar.org). There are 10,700 Idaho charities on the site.

# Information in IRS Form 990

Information	Where in the 990?
Identity, Tax Status and Summary Information	Heading and Part I, page 1
How much revenue was received and from what sources (contributions, programs, investments, etc)?	Summary: Part I, lines 8- 12 Details: Part VIII, page 9
How did expenses break down among program, management and fundraising expenses?	Summary: Part I, lines 13 – 18 Details: Part IX, page 10
Are there changes in, or a deficit regarding Net Assets?	Summary: Part 1, lines 20 - 22 Details: Part XI, page 11



# Information in IRS Form 990

Information	Where in the 990?
New programs and financial results of three largest ones	Details: Part III, page 2
Who are the charity's board members and how much do top staff and \$100K vendors get paid?	Details: Part VII, page 8
What are the charity's management and governance policies?	Details: Part VI, page 6
What does the charity's Balance Sheet look like? Any major changes?	Summary: Part 1, lines 20 - 22 Details: Part X, page 11



Form 990  
ALSO...

**Read Schedule “O”**

*It is a narrative to explain line items in 990*



# Possible Process

## 1. Initial Grant LOI

- Review Letter
- Compare to previous applications and WRWCF decisions
- Check Publication 78 and IRS list of Automatic Revocations of Tax-Exempt Status
- Review Annual Report if there is one
- Review 990s for 3 years if available

## 2. Follow Up Grant Application

- Review Detailed Budget for Organization and Project



## 3. Possible Site Visit Financial Questions

- Operating experience of Management and Board with this charity and/or others (Financial management focus)
- 3 years Statement of Activities and Balance Sheet (if no 990)– See Questions earlier in presentation
- Previous Projects: Ask about revenue, expenses and successes of a few previous projects
- Major contributions (donations) breakdown to determine diversity of revenue sources
- 2 donor references to determine donor satisfaction
- If no 990 on Guidestar, confirm that filed on time for last 3 years
- Ask about status of payment of employment taxes



# Conclusion

Budgets are just numbers unless they have reasonable assumptions, a plan, good management and good oversight

**And remember**

Nothing in fine print is ever good news...

*Andy Rooney*



# Appendix A

Approving a Project:  
Summary of 10 Questions to  
Which the Answer Should Be  
“Yes”



To Recommend a Project,  
Answer “Yes” to the Following Questions  
 (“No” = “Red Flag”)

1. Is the charity/ies proposing the project financially stable or, if not, is there a plan to get there? (*Any “rainy day” \$ available?*)
2. Are there no unexplained, troubling trends in revenue or expenses looking at the last 3 years if possible?
3. Are the sources of revenue well diversified (particularly contributions/donations)?



## “Red Flag” Questions (cont’d)

4. Are the standard financial reports you request provided on a timely basis and does the Executive Director/President understand them?
5. Does the Board Treasurer have financial analysis experience?
6. Is the charity’s/ies’ board/s engaged and employee turnover low?
7. Are donors generally satisfied?





## “Red Flag” Questions (cont’d)

8. Are there key milestones to gage the success of the proposed program?
9. Does the charity/ies have the necessary resources (human and financial) to carry out the proposed program?
10. Have previous projects performed well against budgets?

***Smell Test***

# Appendix B

## Some Key Ratios

To determine how many months charity could operate with no new revenue:

$$\frac{\text{Cash + Liquid Investments}}{\text{Expenses per Month}}$$

To determine if charity might have cash flow problems (e.g. unable to pay bills):

$$\frac{\text{Accounts Payable over 90 Days Late}}{\text{Total Accounts Payable}}$$

# Appendix B

## Some Key Ratios

To determine savings rate (look at 3 years for trend –  
Could Net Assets be used up?):

$$\frac{\text{Total Income} - \text{Expenses}}{\text{Total Expenses}}$$

How much is spent to raise \$1 of contributions?  
(Charity Navigator Benchmark: \$0.35 but can vary –  
compare to similar organizations in Valley)

$$\frac{\text{Fundraising Expenses}}{\text{Contributions}}$$