

# A White Paper for Nonprofit Organizations: Understanding Cash Flow

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## Synopsis

Nonprofit leaders are not always familiar with, or comfortable with, the subject of financial management. This means that financial challenges may be overlooked or ignored. But whether in a poor or a robust economic environment, those with responsibility for a nonprofit cannot disregard the implications of good financial management. With that in mind, one of the most important areas of finances for any organization is cash flow. With or without significant cash reserves, most small to mid-size organizations need to keep a watchful eye on their cash flow. This white paper will explore the importance of understanding how cash flows into and out of an organization and will present various cash flow reports and tools to help the leaders of nonprofits create an accurate picture of their organization's financial situation.

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## 1. Defining Financial Management for Nonprofit Organizations

Everyone in a leadership position in a nonprofit organization, much like their counterparts in the for-profit sector, should have a reasonably good grasp of the group's financial situation. This includes being comfortable with budgets and financial statements, having the insight beyond the numbers to identify newly evolving trends, to recognize the actual cost of programs and services and to position the organization for generating income and raising awareness. Today, there is also a greater emphasis than ever before on risk management and internal controls as necessary ingredients for minimizing the chance of fraud. Understanding all of these gives the leaders the ability to make sound decisions based on reliable facts and reasonable assumptions.

Under optimum circumstances the organization should have a knowledgeable Treasurer on the Board who can work with the audit or finance committee (if the board is large enough for this kind of division of labor) as well as being in contact with the organization's auditor. The Treasurer can help to train staff, oversee the bookkeeping procedures and review the monthly bank statements and bank reconciliations in tandem with the Executive Director. Often a certified public accountant, financial professional or banker assumes this role for the Board.

Key terms that every nonprofit leader should be comfortable with include:

Financial Statements: Nonprofit financial statements are comprised of four financial reports: the statements of financial position, activities and changes in net assets, functional expenses, and cash flows.

- The statement of financial position is a snapshot of the financial status of the nonprofit at a specific point in time, such as on the last day of the month, quarter or year.
- The statement of activities and changes in net assets provides a record of the organization's financial situation, including the earnings, the expenses that need to be subtracted from revenue and the net change in assets, i.e., profit (or loss) that results over a period of time such as a month, quarter or even a year.
- The statement of functional expenses is described as a matrix since it reports expenses by their function (programs, management and general, fundraising) and by the nature or type of expense (salaries, benefits, rent, utilities, supplies, depreciation.)
- Cash flow statements show how changes in balance sheet accounts and income affect cash and cash equivalents, and breaks the analysis down to operating, investing, and financing activities. Essentially, the cash flow statement is concerned with the flow of cash in and cash out of the nonprofit organization. The statement captures both the current operating results and the accompanying changes in the balance sheet.

Cost Analysis: This involves conducting a review of the real costs of the organization's activities, both measurable, tangible costs and indirect expenses such as overhead and payroll. Without a clear picture of what a program costs in its entirety, it is virtually impossible to determine if it should be continued or canceled. An honest cost analysis can help the organization know when it is appropriate to keep investing in a service or event, or when to stop.

Internal Controls: This is a process by which an organization's resources are directed, monitored, and measured. It plays an important role in preventing and detecting fraud and protecting the organization's resources, both physical (e.g., equipment and property) and intangible (e.g., reputation or intellectual property.)

Risk Assessment: This is the identification and analysis of relevant risks that can impede a nonprofit from achieving its objectives for the purpose of determining how those risks should be managed. Risk assessment implies an initial determination of operating objectives, then a systematic identification of those things that could prevent each objective from being attained. In other words, it's an analysis of what could go wrong. Although nonprofit leaders often want to believe they are exempt from fraud because of the good will that is at the heart of their mission, the reality is that they are just as vulnerable as any other company, and they must be prepared for any circumstances.

Budgeting: A budget is not comprised of actual numbers. Instead, it is a prediction based on past experience and future expectations that help the organization anticipate what is to come. While some 'real' numbers may be plugged in when available, for the most part the figures are determined by forecasting the most likely situations. Misleading or unrealistic budgets regarding fund raising revenues or general overhead costs or the costs of a specific program or service can lead to disaster. However, keeping a watchful eye on a reasonable budget will help nonprofits stay aligned with their expectations of what will be earned and what will be spent. While the budget may not provide an exact picture, it does offer excellent guidelines for any group, helping them stay on track.

*Why is it important for the nonprofit leaders to be familiar with these financial terms?*

Nonprofits are frequently reminded that being a nonprofit is a tax status, not a business plan! This means that even though they would prefer to spend 100% of their time concentrating on achieving their vision and fulfilling their goals as stewards of the community, they must devote some time and attention to their infrastructure, gaining information and awareness in order for their organization to flourish.

In fact, in a nonprofit survey conducted by Sobel & Co., responding donors consistently said they expect the nonprofits that they support to have knowledgeable leaders and solid processes in place to ensure that their contributions will be used wisely. Those nonprofits that are lacking in financial awareness do little to gain the confidence of their supporters and to maintain their own credibility in the community.

## 2. Understanding Cash Flow

### *Why Cash Flow Matters*

Cash flow is one of the most powerful tools in cash management for any nonprofit organization because it enables leadership to prepare for surpluses as well as deficits by observing the actual cash flowing in and out of the organization. In other words, a cash flow projection is a forecast of an organization's cash (and cash equivalents) income and expenditures on a weekly or monthly basis, identifying up and down cash fluctuations. This is especially important for groups that earn a significant portion of their revenue during specific times (much as the Salvation Army does during the holiday season) but that have expenses which must be addressed throughout the year. Unlike the organization's annual budget or long term strategic plan, the cash flow projection records only cash transactions over a specific period of time.

For a nonprofit organization, the biggest challenge is likely to be managing cash flow - and arguably the most important financial statement for a nonprofit is the cash flow statement. The overall purpose of managing cash flow is to make sure that there is always enough cash to pay current bills.

### *The Process of Creating a Cash Flow Projection*

The cash flow report is an important tool for the leadership and Board of Directors because it illustrates the actual flow of money through the organization and identifies how much cash is available to pay expenses each month. By managing cash flow and referencing a weekly or monthly cash flow projection, the organization can be more effective and efficient. Keep in mind that one of the most important objectives of managing cash flow is to make sure that there is enough cash on hand to cover payroll, payroll taxes and pay current bills.

Nonprofits can manage cash flow by examining a cash flow projection. Basically, the cash flow statement includes total cash received minus total cash spent. Cash management looks primarily at actual cash transactions. (Note that nonprofits must file a financial statement called Cash Flow Statement or Statement of Cash Flow -- this statement is not the same as a cash flow projection.)

The cash flow projection or reporting process begins by identifying each month's anticipated income and concludes with a report of each month's actual cash flow. Cash coming in can be divided into groupings that include individual donations, corporate contributions, special events fees, service fees or other investment revenue. Cash exiting the organization may be tracked by creating common categories such as payroll expense – taxes, salaries and benefits; utilities and telephone; rent or mortgage and property tax; office supplies and postage; insurance; printing; advertisement; web maintenance and other technology support; travel and conferences and other miscellaneous expenses not listed.

The projection should be updated monthly, if not weekly, with accurate information such as details from receipts, checks, bills and account figures. Having the cash flow projection easily accessible and current enables the organization to watch for peaks and valleys, looking at the beginning cash balance each week or month and updating information based on actual or projected transactions to understand the true cash situation. This helps the nonprofit entity avoid having to react to unanticipated surprises. Without an accurate cash flow projection to rely on, the organization may find itself scrambling when payments are due and cash is low. The projection gives the group time to explore options and avoid potentially embarrassing or harmful situations.

### *How to Manage Cash Based on the Cash Flow Projection*

Having an updated cash flow projection allows the organization the time it needs to plan for cash deficits and cash surpluses, exploring all its options before a crisis situation develops. Knowing that cash will be needed for some key expenses that cannot be put off, such as payroll, taxes, insurance, rent and utilities, can help the organization be better prepared to manage the intake and outflow of cash.

Short of the more drastic steps of borrowing money or liquidating assets, there are typically two ways for nonprofit organizations to improve cash flow. The first is to increase fund raising efforts (including grants.) Advanced planning can allow the organization to accelerate interactions with existing donors as well as with prospective contributors when necessary. This may mean launching an aggressive telephone campaign, changing the date of the major fundraiser, or trying a new direct email solicitation campaign that has never been a part of the mix before.

### *Cash Deficit*

In a tough economy such as we have been experiencing since 2008, deficits in cash flow are more common than ever. But nonprofits that acknowledge the challenge early on have a better chance of overcoming cash flow difficulties than others who have not planned as well. Reducing unnecessary costs, saving when possible, using volunteers more aggressively and even reaching out proactively to major supporters, can all help the nonprofit achieve its goals and be in a better financial position.

The second option, less easy to implement, is to speed up collections of accounts receivable. (e.g., program services, grants, contributions, etc.) While it is hard to change the pace for grant givers and others who owe the organization money, it is always worth a try. The cash flow projection provides the ability to look to the future and hasten the collection process before it becomes critical. Additionally, the organization can extend payables by slowing payments to vendors. (If you use this tactic, be sure to call and alert your vendors to avoid surprising them and disrupting strong relationships.)

Additional opportunities may exist to increase cash flow by generating revenue from existing assets. A sample of this might include rental of unused or little used space to other organizations or offering to share the services of your staff (letting others pay a fee to hire the organization's events planner for a specific project, for example.)

### *Cash Surplus*

The need to manage a cash surplus is a challenge that unfortunately does not occur very often for most mid-size to small nonprofit organizations. However in the event that cash flow exceeds expenditures at some point, it can be put to good use, perhaps even generating additional capital along the way. The leadership can decide what the best way would be to invest the additional cash as they consider alternatives such as paying down outstanding loans or credit lines, consider safe, low risk investments or put the funds into a money market which can generate additional interest. Also, bulk purchases of necessary supplies can be made, ultimately resulting in saving the organization money. All in all, these are just the most obvious options that can provide additional financial benefits for an organization that is in the enviable position of having surplus cash on hand.

### 3. Cash Flow Projection Template

**Monthly Cash Flow Projection**

Enter Nonprofit Name Here

Enter Date Here

	Pre-Startup	Month 1	Month 2
<b>1. CASH ON HAND</b> [Beginning of month]		-	-
<b>2. CASH RECEIPTS</b>			
(a) Cash Sales			
(b) Collections from Credit Accounts			
(c) Loan or Other Cash Injection			
<b>3. TOTAL CASH RECEIPTS</b> [2a + 2b + 2c=3]	-	-	-
<b>4. TOTAL CASH AVAILABLE</b> [Before cash out] (1 + 3)	-	-	-
<b>5. CASH PAID OUT</b>			
(a) Purchases (Merchandise)			
(b) Gross Wages (excludes withdrawals)			
(c) Payroll Expenses (Taxes, etc.)			
(d) Outside Services			
(e) Supplies (Office and operating)			
(f) Repairs and Maintenance			
(g) Advertising			
(h) Auto, Delivery, and Travel			
(i) Accounting and Legal			
(j) Rent			
(k) Telephone			
(l) Utilities			
(m) Insurance			
(n) Taxes (Real Estate, etc.)			
(o) Interest			
(p) Other Expenses [Specify each]			
(q) Miscellaneous [Unspecified]			
(r) Subtotal	-	-	-
(s) Loan Principal Payment			
(t) Capital Purchases [Specify]			
(u) Other Start-up Costs			
(v) Reserve and/or Escrow [Specify]			
(w) Owner's Withdrawal			
<b>6. TOTAL CASH PAID OUT</b> [Total 5a thru 5w]	-	-	-
<b>7. CASH POSITION</b> [End of month] (4 minus 6)	-	-	-
<b>ESSENTIAL OPERATING DATA</b> [Non-cash flow information]			
A. Sales Volume [Dollars]			
B. Accounts Receivable [End of Month]			
C. Bad Debt [End of Month]			
D. Inventory on Hand [End of Month]			
E. Accounts Payable [End of Month]			
F. Depreciation			

Your organization can use a template like the one above or even a simple excel spreadsheet to track the cash coming in and going out of the organization on a daily, weekly or monthly basis. The key for any group is that cash flow be accurately recorded and that the report be scrutinized often to uncover trends and changes that might need immediate attention.

An online search turns up the following sites that have cash flow templates available:

- [www.office.microsoft.com/templates/small-business-cash-flow-projection](http://www.office.microsoft.com/templates/small-business-cash-flow-projection)
- [www.exinfm.com/free\\_spreadsheets.html](http://www.exinfm.com/free_spreadsheets.html)
- [www.score.org/buisness-plans-financial-statements-template-gallery](http://www.score.org/buisness-plans-financial-statements-template-gallery)
- [www.vboc-ca/org/forms/cashflow.12months.xls](http://www.vboc-ca/org/forms/cashflow.12months.xls)
- [www.planware.org](http://www.planware.org)

#### 4. Conclusion

Small and mid-size nonprofits do not usually have well developed infrastructures. In fact, they are notorious for ignoring the systems and processes that the for-profit community relies on such as technology, human resources, marketing and finances. Nonetheless, those that do invest in their own internal procedures find themselves in a leadership role in the nonprofit world. While all too many are reluctant to spend the necessary time and money to build from within, preferring to put every resource into achieving their mission, it can be counter-productive to ignore the importance of efficient systems.

This white paper has targeted the way that cash flow projections can add value for the nonprofit organization. It encourages leaders of all size nonprofits to pay attention to their financial systems, especially to their financial situation, their budget, their cash reserves and their cash flow. Staying one step ahead can help the organization sustain itself no matter what the current economic climate is.

## 5. Citations

Some of the data referenced in this white paper were drawn from information from the following sources.

[www.managementhelp.org/nonprofitfinances/index](http://www.managementhelp.org/nonprofitfinances/index) . “All About Financial Management in Nonprofits,” by Carter McNamara, MBA.

“How to Make Cash Flow Projections” by Tim Spilker. [www.tgci.com](http://www.tgci.com)

“How to Prepare a Cash Flow Statement.” [www.googobits.com](http://www.googobits.com)

“The Cash Flow Crunch” by Amy Feldman. [www.inc.com/magazine](http://www.inc.com/magazine)

“Improving Cash Flow.” [www.inc.com/guides/finance](http://www.inc.com/guides/finance)

“Your Nonprofit Needs Cash Flow...” by Arlene M. Spencer.  
[www.thegrantplant.blogspot.com](http://www.thegrantplant.blogspot.com)

“The Nonprofit Starvation Cycle” by Ann Goggins Gregory and Don Howard. Stanford Social Innovation Review. (The Bridgespan Group)

## 6. Meet the Authors

### **Bridget Hartnett**

Bridget Hartnett, CPA, a member of the Firm at Sobel & Co., has more than fifteen years of experience in public accounting which she draws on to provide high level services for clients.

#### Experience in the Nonprofit Niche

Bridget spends most of her time working closely with clients in social services and nonprofit areas, including educational institutions. As a member in the firm's Nonprofit and Social Services Group, Bridget supervises the audit engagements conducted by Sobel & Co. for the Cerebral Palsy Association of Middlesex County, the Youth Development Clinic of Newark and Catholic Charities of the Trenton, Metuchen and Newark dioceses, Freedom House, and C.J. Foundation. In addition, she handles all of the firm's education audits and holds a Public School Auditor's license. Bridget is also responsible for reviewing and overseeing the preparation of nonprofit tax returns.

#### Philanthropic and Social Service Commitment

Bridget carries her commitment to social services beyond the work place to include her personal involvement in several areas, such as at St. Benedict's school in Holmdel where she is always available for volunteering for projects and special events as needed as well as giving her resources and time to various children's charities, such as the New Jersey Chapter of Make-A-Wish, and others. She is also a volunteer with professional business groups in the New Jersey community, including the Monmouth Ocean County Nonprofit Committee and the Western Monmouth Chamber of Commerce where she is Treasurer, and helped to found the successful Young Professionals' Group and currently serves as Co-Chair and founder of their newly formed Nonprofit Committee. Bridget is also an active member of the New Jersey CPA Society's Nonprofit Interest Group.

#### Professional Credentials

As a licensed Certified Public Accountant in New Jersey, Bridget is a member of both the American Institute of Certified Public Accountants (AICPA) and the New Jersey Society of Certified Public Accountants (NJSCPA).

#### Educational Background

Bridget graduated with her Bachelor of Science degree from Montclair State University.

## **Ron Matan**

Ron Matan, CPA, CGMA is Member in Charge of Sobel & Co.'s Nonprofit and Social Services Group. Ron, brings a unique blend of public accounting and business acumen to every client engagement. A key member of Sobel & Co.'s Leadership Team since joining the firm in 1997, Ron works primarily with non-profit organizations, including United States Department of Housing and Urban Development ("HUD") projects, A-133 engagements, and low income housing tax credit programs ("LIHTC").

### Experience in the Nonprofit Niche

As member in charge of the firm's Nonprofit and Social Services Group (A-133 and HUD audits and LIHTC programs), Ron is responsible for the firm-wide quality of this practice area and is the firm liaison for the AICPA's Government (Nonprofit) Audit Quality Center. With over 35 years of experience in public and private industry and accounting experience with all types of nonprofit and social service organizations, Ron brings a unique blend of knowledge and insight to these specialized engagements. Ron is a Certified Tax Credit Compliance Professional and is listed in the Guide which is circulated to all State Agencies Allocating Tax Credits as well as the Internal Revenue Service. He has also taken courses in advanced training for peer reviews and performs peer reviews of other accounting firms.

### Philanthropic and Social Service Commitment

Ron is a member of the Board of Directors of the Neighborhood Health Services Corporation, headquartered in Plainfield, New Jersey, where he serves as Treasurer and Chairman of the Finance and Audit Committees. Ron also serves on the Union County Educational Services Foundation Board. Ron was the former Treasurer and Board Member of Kids Peace Treatment Centers for emotionally disturbed children, located in Bethlehem, Pennsylvania.

### Professional Credentials

Ron is a Certified Public Accountant licensed to practice in New Jersey, New York and Pennsylvania. He is a member of the American Institute of Certified Public Accountants and the New Jersey Society of Certified Public Accountants (NJSCPA). Ron has been elected to PKF North America's Nonprofit Committee, and in June 2004, Ron was appointed to the New Jersey Society of Certified Public Accountants Peer Review Executive Committee. Ron is also a member of the NJSCPA's Nonprofit Interest Group.

### Educational Background

Ron is a graduate of Kings College in Wilkes-Barre, Pennsylvania, where he received a Bachelor of Science Degree in Accounting.

## 7. About Sobel & Co.

Sobel & Co. is a regional accounting and consulting firm located in Livingston, New Jersey that has been providing nonprofit and social service organizations in the New Jersey/New York metropolitan area with audit, accounting, tax and advisory services since its inception in 1956.

The firm is distinctive in its approach to the nonprofit community because of its sincere passion for serving this sector. As it says on the Sobel & Co. website, "We work with the nonprofit sector because we feel good helping those who do good; we have a passion for helping nonprofit organizations achieve their mission of helping the world's most vulnerable."

The firm currently works with more than 185 nonprofit organizations with revenues ranging from \$100,000 to over \$65,000,000. Based on this depth of experience, the professionals in the nonprofit group are keenly familiar with the issues facing nonprofits and they will apply this knowledge to bring added value to every engagement.

As a further demonstration of the firm's commitment to the nonprofit community, several complimentary programs are offered throughout the year. These include quarterly webinars, roundtable discussions and an annual symposium on timely and relevant topics.

We also encourage you to visit our website at [www.sobel-cpa.com](http://www.sobel-cpa.com) and click on the Not-For-Profit niche page. Once there, please browse our resource library where you will find published white papers along with a variety of articles. We provide a Desk Reference Manual for Nonprofits, a Survey of Nonprofit Organizations that contains interesting insights on nonprofits, a wide range of tools and benchmarking data, a monthly e-mail newsletter that offers relevant information to nonprofit organizations and links to other key sites that are valuable for the nonprofit community.

