Nonprofit Risk Management Center

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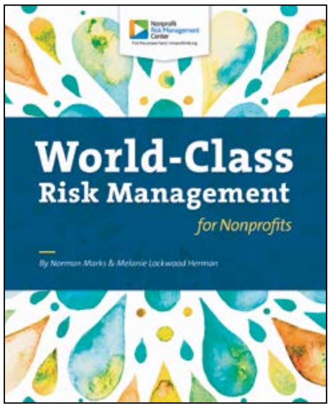
Risk Management ESSENTIALS

Tips, Knowledge and Tools for Nonprofit Organizations



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Examining Fiscal Risk for Mission-Minded Success

By Whitney Thomey

Powerful missions, community advocacy, and life-changing programs can only happen when nonprofits have sufficient financial resources and strong financial management. Sound financial decisions and financial risk management protect critical assets and make it possible for a nonprofit to deliver the services and programs that bring a charitable mission to life. However, there's another reason that nonprofit leaders should keep financial risk top of mind. Organizations must be mindful of how funds and resources are spent and tracked because of three key factors:

1. **Stewardship.** Managing nonprofit financial resources is founded on the premise of managing 'someone else's' money, from institutional to individual funders, corporate contributors, or purchases made by clients, members, and service recipients. As stewards and fiduciaries, nonprofit leaders hold funds 'in trust' for the benefit of others—the people and communities that depend on the nonprofit's work.
2. **Oversight.** In addition to the oversight provided by finance and audit committees, nonprofits are subject to scrutiny from regulatory agencies such as the Internal Revenue Service, and laws ranging from state charitable solicitation statutes, and local/state laws that impose property and sales taxes.

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3. **Ethics.** Ethical leadership of a nonprofit requires that every dollar raised be spent appropriately. Leaders grounded in ethics pay obsessive attention to financial management to ensure that outgoing funds are spent in a manner consistent with the organization's charitable purpose and in support of mission-advancing activities.

NRMC asked a panel of nonprofit finance leaders to share their unique perspectives and insights on a number of pressing financial risk questions. We are grateful to the following financial leaders who generously participated in this interview:

- Holly Raymond – Senior Vice President, Finance & Support Services, Upbring
- Ed Mulherin – Founder & CEO, eCratchit Nonprofit
- Joseph Budzynski – Executive Vice President and Chief Financial Officer, Volunteers of America

NRMC: What's the biggest financial risk facing nonprofits today?

Holly Raymond: I believe the biggest financial risk to nonprofits is forecasting donor behavior emerging from the pandemic. We saw donations slow down across the board and anticipate that foundation giving will be impacted this year. Institutional donor giving tends to lag compared to individual giving. 2020 had so many 'unprecedented' events. As we move out of them, we hope that donors will feel confident enough to give at their historical levels.

Ed Mulherin: I see three top financial risks on the horizon for organizations. First, nonprofits need access to timely, accurate financial information. Funding is a question mark. There's uncertainty around how 2020 will have impacted donor capacity and appetite, and there's an expectation that giving trends will change because of that.

Second, nonprofits must be concerned about their liquidity and, more than ever, because of funding concerns and risks, the size of their operating reserves. Finally, the adequacy of staffing and salaries will continue to be a financial risk for nonprofits. Nonprofit salaries are typically less than in the for-profit sector, and organizations compete in tight labor markets for exceptional and qualified staff.

Joe Budzynski: In my opinion, it's future revenue streams. There has been an uptick in donations, and that's been a direct result of the nonprofit sector stepping up during the pandemic to serve communities. We've also seen various CARES Act stimulus funds coming in and trickling down, which continue to support and amplify revenues from existing funders. In some areas, the funding has doubled or even tripled from pre-COVID levels. However, this extra funding is uneven state-by-state even when it's based on need and the existing social services network.

The considerable risk comes when this Federal funding drops off; then, we'll see the actual impact on state budgets post-COVID. How will the Federal government balance out the trillions of dollars to keep the funds buoyed? What choices are states going to make to continue to fund these various programs and the missions of the nonprofits in the long-term—in the next 2-5 years? There will also be unevenness on a state-by-state basis. You can expect some areas to fare well and others won't.

NRMC: What's the most misunderstood financial risk facing nonprofits today?

EM: I think nonprofits often misunderstand the need for adequate reserves and that it's consistent surpluses over time that build and enhance the Balance Sheet.

JB: Many nonprofit leaders misunderstand the importance of short-term cash flow and consistent, timely payments from providers. In our organization, we often encounter situations where provider payments lag behind the services we provide to our community. States will encourage nonprofits to maintain lines

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"As a nonprofit, we can (and should!) have a positive bottom line. Financial stability helps us be sustainable in perpetuity to continue to work for our mission another day."

of service, even when government funds lag. Eventually, provider payments are behind—by millions of dollars sometimes! When that happens, nonprofits are expected to bankroll essential programs until the funds arrive. Nonprofits often do this despite having thin budgets and inadequate reserves or unrestricted funds.

On the surface, everything looks good: you don't need to execute layoffs, programs and services are "right-sized," but what does the cash flow look like? Is it as you expect, or is there a significant delay from providers? This is often not part of the strategic conversation. It's simple, how long can you continue to fund programs until reimbursement funds arrive? Many nonprofits don't look at funding in that manner.

NRMC: What are the frequently missed (or misunderstood) opportunities to strengthen a nonprofit's balance sheet/ improve financial health?

HR: Organizations will sometimes turn down donations, thinking, "We don't need that gift" because we're in good shape right now. Another fallacy is that continually operating at a deficit means you are more deserving or have more need than other organizations. The risk of this strategy is that continued losses are unsustainable. As a nonprofit, we can (and should!) have a positive bottom line. Financial stability helps us be sustainable in perpetuity to continue to work for our mission another day.

EM: Two things come to mind. First, nonprofit leaders often miss the opportunity to budget for surpluses! When you build a surplus into the budget, it sets a goal for building reserve funds, which can be earmarked for emergency operating expenses or an innovation fund so organizations can safely take those bold opportunities for their mission. Second, I don't think there's enough consideration for nonprofits to enter into merger deals. Looking for the opportunity for like-minded organizations to formally merge has the potential to gain efficiencies that can help congruent missions.

JB: The thing that comes to the top of my mind would be timely and accurate cash forecasting. As nonprofits operate at the speed of business and uncertainty, we all grapple with how to continue to live and

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> "As nonprofits operate at the speed of business and uncertainty, we all grapple with how to continue to live and emerge from COVID; knowing your current cash balances and cash forecasts are super important."

emerge from COVID; knowing your current cash balances and cash forecasts are super important. I get the sense that a lot of nonprofits don't know they need to do this. Many leaders are focused on fighting a daily fire so forecasting isn't top of mind—particularly cash forecasting.

However, you need to make sure you can pay your bills, pay staff, and keep doing what you're doing to fight another day. Something all nonprofits can improve is the health of their balance sheet. No one likes to call it quits, and there's often a tendency to hold on too long. The risk here is that if there's nothing left (the balance sheet is over leveraged, the population you serve has declined, etc.), your organization is no longer attractive as a candidate for a merger.

Finally, I think that the whole COVID experience was a wake-up call to many nonprofits to take a step back and talk about reserves. Many leaders are having long overdue conversations about creating adequate reserves, including emergency funds. It's not a quick fix! It's often a multi-year effort to reach targets. When there's a windfall, you have to be disciplined to put money aside and realize that the impact of a serious downturn will affect more than one financial cycle. Another important, shorter-term strategy is to ensure you have secured lines of credit to help you weather the storm until those reserves are adequately built.

NRMC: What is a common misconception boards and finance committees have about financial management, financial forecasting, or their fiscal oversight role?

HR: I think that nonprofits often think it's relatively easy and straightforward to go out and ask for donations and be awarded grants. In actuality, it is a long, methodical process. Team members need to have dedicated attention and intention and be there to work with the organization long term. I would recommend against starting any long-term initiatives until time has been spent to vet them thoroughly. It takes time to lay the groundwork and for those seeds to bloom into something in the future.

EM: It's tricky to ensure that boards and the finance committee are striking the right balance between too much oversight and not enough. There needs to be support and counsel from the board, and at the same time confidence to allow nonprofit leadership to manage the day-to-day.

NRMC: What are the top signs that the financial house (business model, financial reporting, composition/leadership of the finance team) needs a radical renovation versus some repair work?

HR: If there has been fraud or material misstatements that led to a modified audit opinion of the financial statements, you need a radical renovation of systems and processes. Most other issues require a change in staffing or a detailed review to complete repair work.

EM: In my opinion, if your organization is having chronic cash flow issues, is late on reporting or missing reporting altogether, or if you're experiencing surprises in your finances, then it might be time to consider a radical renovation of who is leading (the organization or the finance team) or how the finance function is structured and operates.

JB: Here are some questions to ask to evaluate your organization's financial health:

- As trends are changing in your space, are you staying on top of them?
- Can your current staff pivot to those changes? If you can't, you run the risk of watching your funding sources diminish or dry up.
- Are you thinking about not just getting through today but how to manage tomorrow better? In other words, do you have reserves and a plan? And do you know when you would use those types of reserves?

The COVID-19 crisis has been a catalyst for many nonprofit leaders to have these conversations and review their financial functions. Many organizations are taking

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> "Nonprofit leaders often miss the opportunity to budget for surpluses! When you build a surplus into the budget, it sets a goal for building reserve funds, which can be earmarked for emergency operating expenses or an innovation fund…"

a look and realizing that we need better forecasting in sync with operations. Keeping these two functions in step provides a better understanding of what lies ahead. Annual budgets and comparing historical budgets to actuals are still important tools, but what's needed right now is a forward look rather than what's in your rearview mirror.

NRMC: Are there not-so-obvious or sometimes overlooked signs that a nonprofit's financial health is improving?

JB: I think there's often a temptation to only look at the bottom line. Nonprofit boards are often staffed from the for-profit sector, and they recognize the benefit of a positive bottom line. Nonprofits are *mission-focused*, and this fact extends out timelines and makes the question of improving fiscal health more complex. It's vital to take into account what an organization is doing and whether the *right things* are happening. Financial dashboards should show strategic metrics and measure outcomes. These dashboards should be showing what impact the organization is having on the population they're serving, along with the financial results. This will help evaluate if your organization is hitting targets you set and whether resources should be allocated differently based on what you want to change in the community.

Because of the nature of mission-focused work, boards should strive to

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> "The adequacy of staffing and salaries will continue to be a financial risk for nonprofits. Nonprofit salaries are typically less than in the for-profit sector, and organizations compete in tight labor markets for exceptional and qualified staff."

consistently ask questions such as: "Are we doing the right thing and maximizing our precious resources to have the best impact? Could we explore a different partnership to leverage resources even if it means we have to give up some control?"

NRMC: What should readers of the Form 990—or financial statements in general—be looking at specifically to best understand the financial health of a nonprofit?

HR: I think it depends on why someone's reading the 990. If you mainly need to understand a nonprofit's financial health, there are two places you should look. First, look for any endowments and related disclosures. Second, to understand overall revenue, you should examine assets and fundraising activities. And while it isn't a primary indicator any longer, you can calculate the functional expense allocation. Finally, if you're interested in joining their team, I recommend looking to see how much they pay their top staff.

EM: Too often, organizations look at their income statements for a single year, when, really, it's best to look at a trend over 5 years and focus on the balance sheet.

NRMC: What are some of the most important lessons managers and boards are poised to learn during tough economic times?

HR: Very simply, not every nonprofit is going to make it through the pandemic. We've seen closed doors and dramatically changed operations. The most important lesson is never to lose sight of your revenue wheel. Ask questions like:

- Are you too heavily weighted in any area?
- How nimble are you when situations require it?
- What will it take to make the tough decisions?

Balance and flexibility are essential. Federal and state funding didn't waver during the pandemic. However, individual donors, events, and foundations have been fickle.

EM: You really can't ever have too much in reserves. Strive for at least 6 months, but more is better. Another sound tactic is to establish a Line of Credit in advance. Setting it up before you need it will ensure that it's available to help you weather tough times.

JB: I think you have to make it a priority when you're building your budget year-over-year that there's enough to cover and protect your employee costs. All nonprofits are labor-intensive; most spend between 50-70% of their total budget on employee compensation and related expenses. Staff should be a priority! They are what keeps the organization alive, and ensure that mission work happens.

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Difficult economic times put a strain on this area of the budget. Often, you'll see hiring freezes, no bonuses or pay increases, and even layoffs. However, the programs and services don't stop, so staff must keep doing the work. Sometimes, especially in the social services sector, these programs are even more vital for a community and require 24/7 program support to clients. It's essential that nonprofit leaders think about how employees are being compensated. Questions like:

- Are all staff being paid a fair and equitable wage?
- Has your organization made DEI a priority?
- What are you asking staff to endure?

How you prepare financially from a recruiting and retention standpoint affects the quality of service you provide and your mission's success.

NRMC: What question about financial risk and health should we have asked you?! What else do you want our readers to know?

EM: I can't emphasize this enough: you don't want to be surprised by your financials! That means nonprofit finance leaders should establish strong budgeting practices by program and by month, and there should be consistent variance analysis to surface anomalies as early as possible. Finally, I recommend using income statement forecasting to help the leadership team understand whether cash flow is strong, stable, or weak.

JB: Looking at the past 12 months as a catalyst, I've learned that it's imperative that the Finance department work more closely with Operations. That relationship is crucial to understanding challenges, thinking through strategy, timing, and implementation, and being nimble to take advantage of opportunities or mitigate losses.

Another thing to be mindful of is the shifts in the price of insurance. Whether you're talking about healthcare or non-healthcare insurance, the costs are crippling. Organizations are becoming numb to the increases. I worry about a hardening market and carriers stepping back and dropping coverages. That creates a huge financial exposure, especially if your organization struggles with having adequate reserves. The way to avoid this is to partner with a good broker who knows who you are, what your mission is, and truly works toward getting your organization appropriate coverages.

Whitney Thomey is Project Manager at the Nonprofit Risk Management Center. She welcomes your follow-up questions about any of the topics covered in this article at 703.777.3504 or Whitney@nonprofitrisk.org.

Additional Reading

- Financial Risk Management: A Guide for Nonprofit Executives
- "Understanding Reserves" (VIDEO) Propel Nonprofits
- "Top 5 Trends Impacting Nonprofits' Fiscal Health in 2021," Concannon Miller
- "Nonprofit Finance in 2021 – setting the new course in the post-pandemic era," Diginomica

TAKE ACTION

The image following depicts common financial risks nonprofits may encounter.

Consider these steps to better understand and address the myriad finance risks your nonprofit faces and embraces.

Uncover

What are the risks?

Sort and Discuss

Examine and categorize risks into ***External, Strategy, and Preventable*** buckets. This will help identify appropriate proactive and reactive responses for each risk.

Act

Determine reasonable steps and initiatives to:

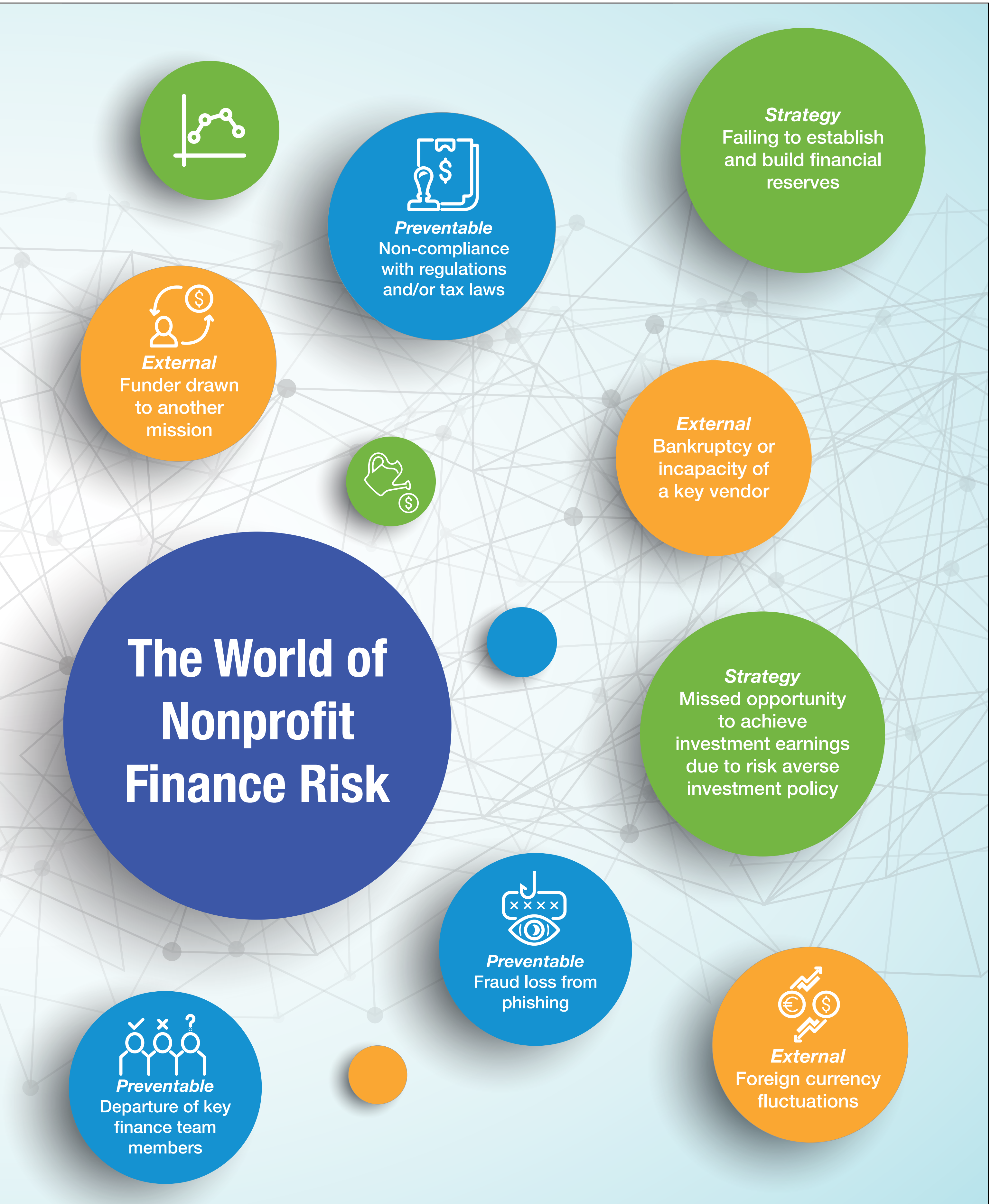
- Monitor how the risk is changing
- Assess our vulnerability
- Build resilience
  Cross-training, contingency plans, etc.
- Ensure awareness and oversight
  Which teams need to know the status of mitigation strategies?
  Who might need to make a decision that would be informed by our understanding of the risk?

Preventable
Falling short of overly ambitious or unrealistic fundraising or other revenue goals

External
Economic downturn

Preventable
Sloppy financial management

Preventable
Poor budgeting and expense forecasting leads to cost overruns



The World of Nonprofit Finance Risk
Strategy
Failing to establish and build financial reserves
Preventable
Non-compliance with regulations and/or tax laws
External
Funder drawn to another mission
External
Bankruptcy or incapacity of a key vendor
Strategy
Missed opportunity to achieve investment earnings due to risk averse investment policy
Preventable
Fraud loss from phishing
External
Foreign currency fluctuations
Preventable
Departure of key finance team members

Heads Up: Why Fortified Fiscal Oversight is Key to Financial Well Being

By Melanie Lockwood Herman

During the past 15 years, I've been honored to serve as a volunteer board member for several organizations. My first board role was for a community-based organization in the small village where I live. I had long admired the nonprofit's historic preservation and conservation mission, and when the invitation to consider board service came, I jumped at the opportunity to serve.

During my first year of service, a disconcerting moment led me to volunteer to assume the role of treasurer. During a board meeting, the incumbent treasurer announced that although he had "a handful of spreadsheets and reports" prepared, he was certain no one on the board wanted to hear him read those documents. He laughed and asked if someone wanted to 'move' acceptance of the financial statements (presumably the papers he was shuffling nervously). Before I could close my gaping jaw, a motion was offered, seconded, and adopted. To this day, I regret not raising my hand to vote "no" or abstain.

Fiscal Oversight is Broken: Here's Why

While my experience was the most egregious example of financial leadership I've ever witnessed, my work as a consultant to numerous nonprofit leadership teams over the years has led me to believe that effective, appropriate financial oversight is both essential and hard to do. Why is it so hard to create an operative oversight function that supports the financial health of a nonprofit? Three culprits come to mind:

1. **Board Members Don't Join to Focus on Financial Health.** The NRMC team has worked with thousands of board members who support and oversee a vast array of charitable missions. During our one-on-one conversations with these dedicated leaders—including Audit and Finance Committee Chairs—we have yet to hear *anyone* say that they were drawn to the nonprofit because they wanted to receive financial reports or serve on the finance committee. The mission and purpose of an organization are what inspire board members to serve. And interestingly, even savvy finance professionals tell us they never expected to be drawn into financial oversight when they agreed to serve. Joining the board was a chance to do something *other than* finance!
2. **Fiscal Oversight Skills and Techniques are Taught, Not Brought.** Nonprofit board members who seem comfortable and skilled

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at fiscal oversight are likely to have learned their skills serving on *another* board. No one emerges from the womb, or college, knowing what questions to ask to probe the weaknesses on a Statement of Financial Position (the Balance Sheet) or wildly unrealistic aspirations on a revenue forecast. Serving on a board is a chance to learn and hone the skills necessary to do the job. It's all on-the-job training!

3. **Effective Fiscal Oversight is an Awkward Dance.** If you have two left feet, or you've been told you lack rhythm, fiscal oversight will be familiar territory. Oversight requires asking questions that seem to poke at what you're being told by the finance and executive staff at the organization. Strong staff members will take those questions in stride and appreciate your care and concern about the organization's financial health.

   Weak leaders will take offense, brush off your questions or create a diversion ("Did I mention we're a finalist for a big grant?"). The most competent staff teams recognize that they can't deliver financial management *and* financial oversight because there is an inherent conflict of interest in wearing both hats. Your accountant can't also serve as your auditor. A chef can't participate in a cooking competition where she's also a judge.

Fix It Before It's Too Late

The ultimate risk of poor financial oversight is a significant downside surprise that the board 'didn't see coming.' When frustrated, sometimes angry board members call NRMC to share tales of financial woe, they most often lay blame at the desk of the CEO. Our training and experience tell us that inadequate oversight was a corresponding if not crucial culprit in many instances.

Unfortunate, mission-crippling financial results can happen to the best-run organizations and under the watch of the most ethical managers. However, many surprises are due instead to a failure to 'mind the store.' As is true with other impending disasters, forewarning can mean the difference between survival and obliteration.

Consider adopting—or adapting—these five strategies to infuse and buttress fiscal oversight in your organization.

1. **Develop and Share Relevant Oversight Questions.** When the board receives a packet of materials in advance of a committee or board meeting, conscientious board members are likely to review those materials and try to identify questions they should ask (if no one examines the packet, you've got an entirely different problem!).

   As a brand-new board member, I remember making notes in the margins of the board packets I received at the 11th hour. Asking questions is a standard component of oversight. But knowing what kinds of questions to ask is a skill that develops with experience. A common occurrence is for board members to ask questions about changes in financial results from one period to the next.

   I recall a frustrated CEO who was asked by a board member to explain why office supplies expense was up by 25% in the past quarter. She responded (a bit impertinently), "Do you mean the increase of $100? Is that what you're asking about?" Instead of crossing your fingers and hoping board members come up with brilliant oversight questions, add suggested questions to your board meeting agenda, or include them at the end of the Finance Committee Report. For example:

> "...many surprises are due instead to a failure to 'mind the store.' As is true with other impending disasters, forewarning can mean the difference between survival and obliteration."

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Case Studies

1

Engagement Goal: Elevating and integrating ad-hoc conversations about risk-taking and risk management into durable planning and decision-making processes

WHO: A national foundation working to strengthen democracy and promote the health, diversity, and resilience of democratic processes and institutions.

Results: The NRMC team worked in partnership with foundation leaders to identify and unpack critical risks. The project culminated with a workshop exploring the topics of risk assessment and risk appetite. The NRMC team will be returning to the organization later this year to facilitate follow-up training for a broader staff team.

2

Engagement Goal: Interim Risk Leadership

WHO: A regional transit agency employing more than 1,200 staff.

Results: The engagement involved leading and motivating staff working in claims management and safety and partnering with the agency's top executives to envision a new structure for the risk team. NRMC's work included managing contacts with the agency's external broker and defense counsel and facilitating the vetting and appointment of a new Third-Party Administrator (TPA). The NRMC team also led the search process for a new risk leader and developed a new risk dashboard to elevate and strengthen risk oversight.

3

Engagement Goal: Development of an engaging website housing custom risk resources for the organization's member agencies

WHO: A national organization of 1,000 affiliated agencies dedicated to fighting poverty in the U.S.

End Result: The NRMC team developed an attractive website featuring two interactive web applications. These applications present content fully customized for the association. The site also has easily accessible web links to NRMC Affiliate Member benefits. These resources help the organization's affiliated agencies develop a deeper awareness of the risks they face and identify practical steps to close gaps in risk practice. More than 95% of the organization's affiliated agencies have used the site to complete a Risk Assessment and demonstrate compliance with national quality standards.

4

Engagement Goal: Thoughtful bidding process to identify and select the best-qualified firm to provide insurance

WHO: A regional public health organization with more than 1,700 employees serving nearly 200,000 consumers.

End Result: The NRMC team facilitated and managed a Broker Selection Process for the agency motivated by the commitment to ensure that insurance dollars were allocated wisely. The NRMC team designed a custom RFP, identified and pre-qualified bidders, reviewed incoming proposals based on the client's criteria, and coordinated interviews with the six finalist firms. At the end of the process, the client selected a new broker and entered into a multi-year broker services agreement.

Heads Up: Why Fortified Fiscal Oversight is Key to Financial Well Being
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- Do the financial results for the past quarter give you confidence that our financial health is improving?
- Which specific financial result gives you the most concern?
- From your perspective, are we on track to meet our financial goals?
- In your view, is spending aligned with our strategic priorities for this year? If not, where are we off?
- Does our current level of financial reserves give you confidence that we could successfully weather a downturn in one revenue category? Multiple revenue categories?

2. **Establish Ambitious Goals Related to Financial Health.** As shared by the panel members in "Examining Fiscal Risk for Mission-Minded Success," inadequate financial reserves represent a significant risk—and a weakness—for many nonprofits. Effective fiscal oversight includes adopting financial goals that provide a buffer against unexpected or unavoidable downturns or financial losses, as well as benchmarks against which to measure progress. While the list of financial goals suitable for your organization may be different from those suited to another nonprofit, there are a handful of goal types that should be considered, at a minimum. These include:

- ***Financial Reserves.*** Whether you call your reserve a 'rainy-day' fund, 'financial reserve,' or something else, most organizations define their target by the days of cash required for core operations. This is sometimes referred to as "number of days of cash on hand." A healthy reserve or rainy-day fund is typically in the range of 6-12 months of cash to cover basic operating expenses, from payroll to rent, utilities, insurance, customary contracted services, and more.

  Calculate "daily cash required" by taking your total costs for the year, subtracting depreciation and other non-cash expenses, and divide by 365.

> "Asking questions is a standard component of oversight. But knowing what kinds of questions to ask is a skill that develops with experience."

- ***Debt.*** If your nonprofit has incurred debt for special projects or to keep the doors open, the board should appreciate and understand the purpose of that debt and the strategies for ensuring prompt repayment and keeping debt expense within reason. A goal related to debt may be in order if borrowing is a customary strategy for making ends meet (e.g., "Pay off the line of credit in 18 months.").
- ***Administrative and Fundraising Costs***. Many nonprofits that rely principally on donations from individuals struggle to keep total fundraising costs at a level that passes muster with charity watchdogs, the media, and the public. Thankfully, the percentage of total expenses devoted to administrative and fundraising is finally declining as the predominant indicator of ethics and efficiency. For too many years, nonprofits have been judged on the reported percentage they spend on 'direct programs and services' versus the true value and impact of services provided. Scant attention was paid to the fact that ineffectual nonprofits may claim to spend "90 cents" or more of each dollar raised on programs.

  In contrast, nonprofits that are changing lives and communities for the better may struggle with fundraising costs because their most loyal donors will only respond to appeals delivered via the costliest fundraising channel, direct mail.

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"Boards should not be permitted to ignore dated or otherwise inadequate compensation structures and claim that "we can't pay people fairly because we're a nonprofit."

- ***Change in Unrestricted Net Assets.*** As shared by Ed Mulherin in "Examining Fiscal Risk," ending the fiscal year with a surplus is a step that must be repeated to build an adequate or healthy financial reserve. Positive, unrestricted net assets should be available for mission-advancing purposes, such as building a reserve, supporting an innovation fund, or paying off debt.
- ***Living Wage and Competitive Benefits***. Less talked about as a financial goal—but of critical importance—is a goal related to paying a living wage to all employees of the organization. While the board should not be involved in determining pay scales, bonus amounts, or the details of benefits plans—except for compensation and benefits for the CEO—the board should have confidence that the organization's commitment to equitable, living wages is real. Boards should not be permitted to ignore dated or otherwise inadequate compensation structures and claim that "we can't pay people fairly because we're a nonprofit."

To reflect on the ambitious goals uniquely suited to your circumstances, ask:

- What mission-advancing move would we make if we had the financial resources to do so? What amount do we need?
- What unnecessary stress or strain do we face that we can attribute to having inadequate reserves? What level of reserves would eliminate or significantly reduce that stress?
- Do we have a clear and compelling compensation philosophy?
- Does that philosophy enable management to create pay scales and competitive benefits that support a living wage for all staff?

3. **Provide Annual Financial Training for the Entire Board.** If your board is typical, a few members understand the structure and terminology of your financial statements, and many others do not. I've attended hundreds of finance committee and board meetings and have yet to hear anyone say, "I really don't understand the story these financial statements are telling. What are the headlines? What do I need to know?" Most board members find it uncomfortable to admit they don't understand the organization's financial statements.

   To 'level' the playing field for your board and help it ascend to the financial oversight role your mission deserves, schedule an annual workshop that explains—in layperson's terms—the critical components of your principal financial statements (Statement of Financial Position, Statement of Activities, Statement of Cash Flows, and Statement of Functional Expenses). Invite and encourage all board members to attend. Consider making it fun by kicking off with a self-scored financial health quiz and great discussion questions sprinkled throughout the training.

4. **Require All Board Members to Serve a Tour on the Finance Committee.** One of the most common mistakes made by those who determine committee assignments is to exempt some or most board members from serving on the board's most active committee, the Finance Committee. Whether your board members serve terms lasting 3 or 4 years and

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What Your Board Needs to Know About Cyber Threats
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> "To 'level' the playing field for your board and help it ascend to the financial oversight role your mission deserves, schedule an annual workshop that explains—in layperson's terms—the critical components of your principal financial statements..."

whether you have term limits, sitting for at least 2 years on the Finance Committee should be required for *all board members*. The participation of non-financial leaders on this committee will lead to meaningful changes and improvements in financial presentations and the addition of much-needed, plain-language explanations of financial developments.

5. **Use a Fiscal Dashboard to Tell Your Financial Story.** One of the most interesting—and challenging—tasks ever undertaken by a finance team or finance committee is constructing a fiscal dashboard that tells the nonprofit's financial story in a concise, visual fashion. An effective dashboard draws attention to the headlines and invites a 30,000-foot view of financial health.

   When building a dashboard displayed on a single page, limit the information to a maximum of 5 chunks, charts, or data sets (visualizations). Remember that a great dashboard should be understandable in five seconds, and the most crucial information should be at the top of the page. Use a simple color scheme and make sure that every word or number is readable without a magnifying glass! Many different types of information can be depicted on a fiscal dashboard. Choose the most relevant information based on your financial goals and current circumstances, such as:

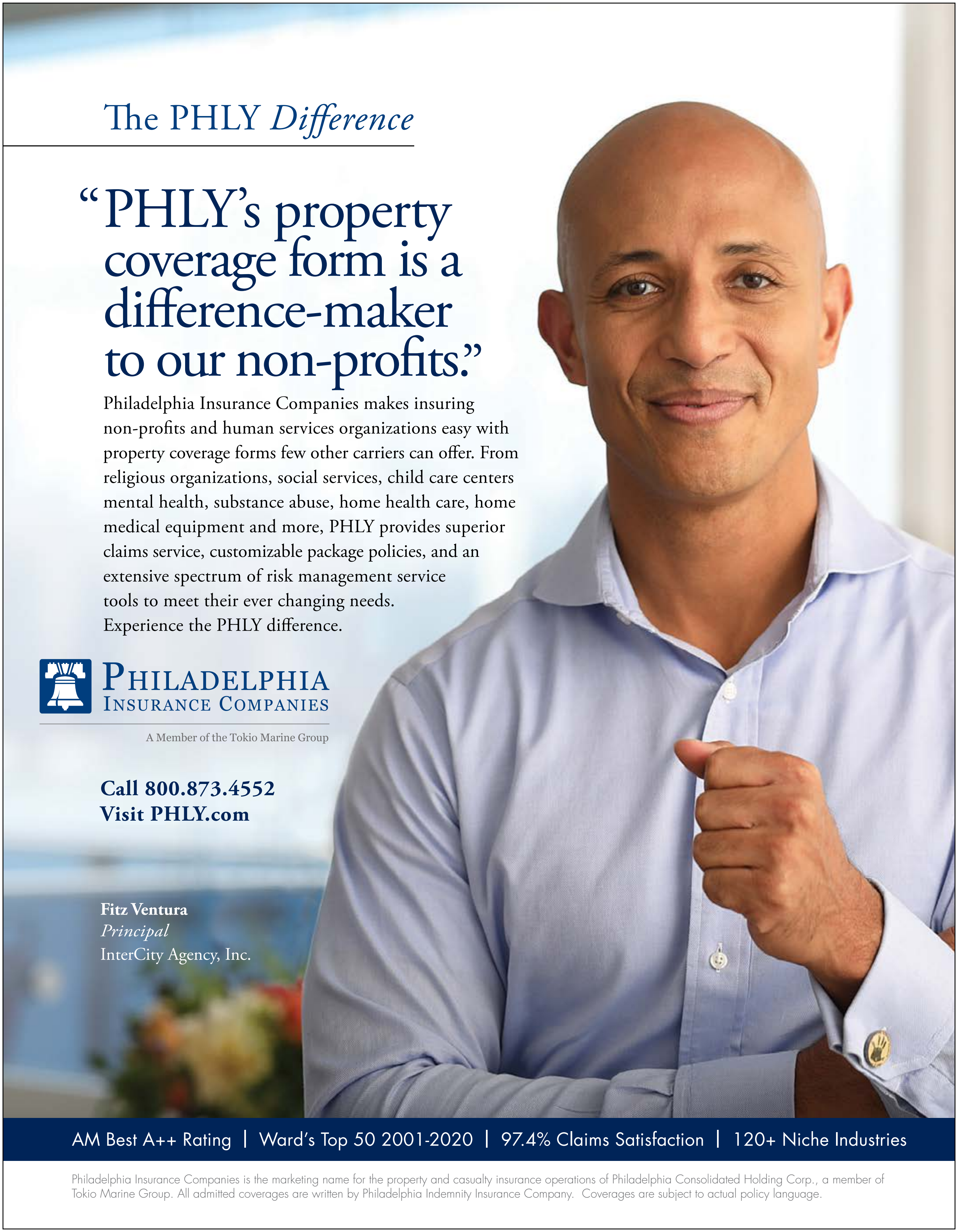
   - Progress towards achieving your financial reserve goal
   - Current financial ratios (cash on hand, debt ratio, etc.)
   - Growth in revenues/growth in expenses (%) year over year
   - Change in unrestricted net assets, year over year
   - Progress achieving diversification of revenue sources
   - Change in reliance on a single revenue stream or principal funder, year over year
   - Key financial goals for the current fiscal year or over a multi-year period

Fortified fiscal oversight is a worthy goal for all nonprofits. Your mission deserves strong financial management practices and thoughtful oversight by leaders who can step back and share insights and perspectives on financial goals and fiscal well-being. When a board develops the skills and confidence to ask tough questions about financial health, managers experience less worry that they are on the journey alone. An active Finance Committee that understands and embraces its oversight role is a priceless asset for a nonprofit mission.

Melanie Lockwood Herman is the Executive Director of the Nonprofit Risk Management Center. She welcomes your questions about fiscal oversight and nonprofit boards and committees at 703.777.3504 or Melanie@nonprofitrisk.org.

Additional Reading

- "Fiscal Responsibility and Oversight: Empower Your Board to Lead," RISK eNews
- "Transparency, Not Whitewash," RISK eNews
- "Take the Fear out of Financial Statements," BoardSource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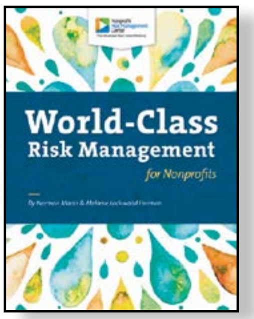

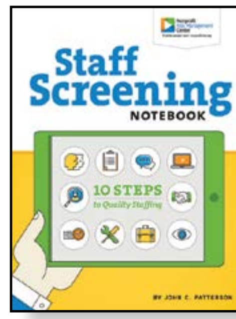

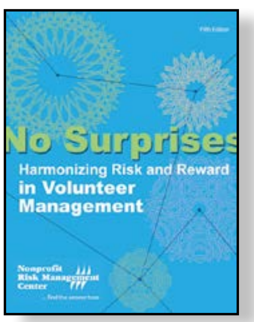

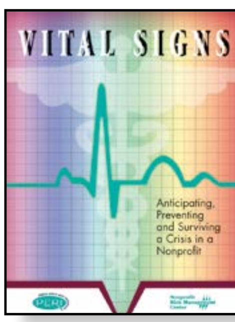

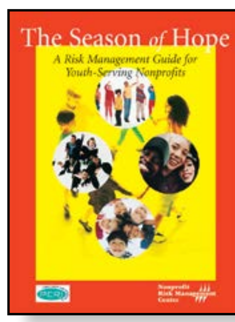

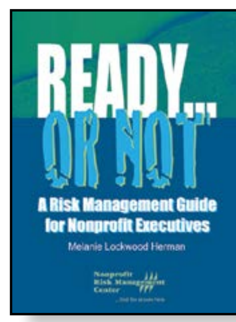

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NEW AFFILIATE MEMBERS

Learn more about NRMC's Affiliate Member program at nonprofitrisk.org/affiliate-membership. NRMC would like to welcome our new Affiliate Members.

American Association of Veterinary State Boards

BBYO

Camp Boggy Creek

Center for Civilians in Conflict

Clearbrook

For Love & Art

Guardian Angels for Soldier's Pet

Jewish Community Relations Council of Greater Boston

Missouri Coalition Against Domestic and Sexual Violence

Missouri United Methodist Foundation

National Association of Free & Charitable Clinics

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