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Tools for Effective Benchmarking

How to Properly Measure and Understand Your Association's Success

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Objectives

At the end of this session you will…

- Understand why Associations use accounting measurements and metrics
- Review several measurements and metrics that can be useful to Associations
- Understand why benchmarking is important
- Learn what benchmarking tools are available

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The Importance of Associations

- Increasingly important economically
  - More than 1.9 million nonprofits registered with the IRS
  - Approximately 100,000 501(c)6 and 1.3 million 501(c)3
- Increasing role in provision of valuable services and member benefits
- Associations perform important social functions by providing employment and volunteer opportunities

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Challenges of the Nonprofit Sector

- Has suffered from notable scandals and negative publicity
- Increased IRS and legislative scrutiny
- The new normal economy

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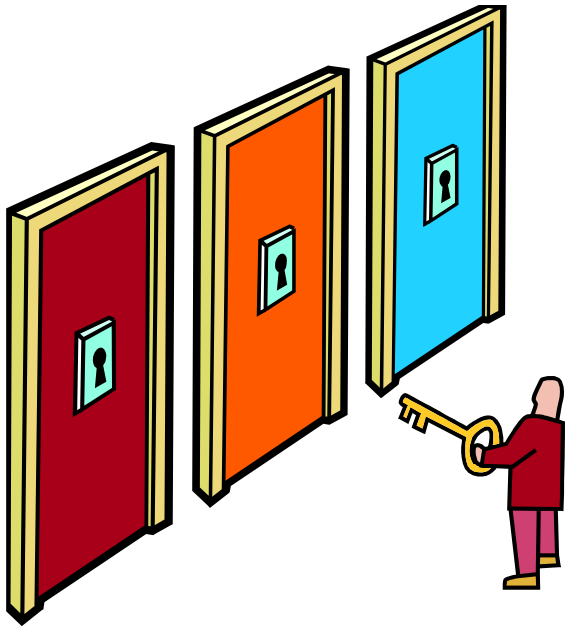
So what does this mean?



- Financial management is more important due to increased scrutiny, economic challenges and increased competition
- Executives and Board members need financial information to make key decisions

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Why use Accounting Measurements and Metrics?

- To help summarize organizational performance
- Provides a snapshot approach that is easy to understand
- Can be used to improve financial decision making
- Used in benchmarking
- Helpful in identifying trends

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Why use Accounting Measurements and Metrics? (Continued)

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Accounting measurements and metrics are most useful if they are:

- Calculated using reliable and accurate information
- Calculated consistently from period to period
- Used in comparison to similar organizations
- Viewed at a point in time and also as a trend over a period of time
- Interpreted using internal and external factors

So What are Some Good Metrics for Associations and What Do They Measure?

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Measurements and Metrics – Days Cash on Hand

$$\frac{\text{Operating Cash}}{\text{Cash Expenses per Day}}$$

- How many days can the organization operate if no additional funds were received before investments would need to be liquidated?

$$\frac{\text{Cash + Investments}}{\text{Cash Expenses per Day}}$$

- How many days can the organization operate if no additional funds were received before requiring borrowed funds?

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Measurements and Metrics – Days Cash on Hand (Continued)

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Cash Expenses per Day

Operating Expenses

(-) depreciation and amortization

(-) in-kind expenses

(-) unusual one-time expenses

Cash Expenses

Divide by 365 to arrive at Cash expenses per day.

Measurements and Metrics – Current Ratio

$$\frac{\text{Current Assets}}{\text{Current Liabilities}}$$

- Measures the financial health of the organization
- Ratio > 1 represents the ability to meet short-term obligations including maturing short-term debt and upcoming operational expenses

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Measurements and Metrics – Aged AR and AP Ratios

$$\frac{\text{Accounts Receivable over 90 Days}}{\text{Total Accounts Receivable}}$$

- As AR becomes older and more delinquent, may indicate potential collection problems and cash flow issues

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

- If this ratio is increasing over time, may indicate the organization has cash flow problems

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Measurements and Metrics – Investments

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Portfolio's Rate of Return -
((S&P 500 Rate of Return x (Equity Portfolio Inv. %)) +
(Bond Rate of Return x (Bond Portfolio Inv. %)))

- Measures portfolio return for the Organization against overall market
- Are we underperforming?
- Use of alternative investments

Measurements and Metrics – Debt Ratio

$$\frac{\text{Total Debt}}{\text{Total Assets}}$$

- Measures the proportion of assets to debt
- High values may indicate potential for future liquidity issues
- High Values = Highly Leveraged
  - Could reduce capacity for future borrowings

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Measurements and Metrics – Debt Ratio (Continued)

$$\frac{\text{Total Debt}}{\text{Unrestricted Net Assets}}$$

- Should only consider unrestricted net assets in this calculation
- Can also use total liabilities rather than total debt
- Measures how much the organization is relying on funding from others
- High Values = Highly Leveraged
  - Could reduce capacity for future borrowings

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Measurements and Metrics – Net Assets

$$\frac{\text{Temporarily Restricted Net Assets}}{\text{(Cash + Investments + Pledges Receivable)}}$$

- Useful in determining if an organization may be spending restricted cash for purposes other than the intended purpose
- This ratio should be < 1 (lower is better)

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Measurements and Metrics – Income Reliance Ratio

$$\frac{\text{Income Source}}{\text{Total Income}}$$

- Analyze proportion of income streams to total income
  - Membership dues
  - Meetings and events
  - Individual /Corporate contributions
  - Sponsorships
  - Publications
  - Certifications
  - Dividends and interest
- What does the trend look like?

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Measurements and Metrics – Earned Income Ratios

$$\frac{\text{Earned Income}}{\text{Total Income}}$$

- Measures relationship of earned income to all income
- Organizations with a higher percentage of earned income tend to have more autonomy and flexibility

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

- Measures proportion of operating expenses which are covered by earned income
- Self-sufficiency

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Measurements and Metrics – Expense Allocation Ratio

$$\frac{\text{Expense Source}}{\text{Total Expenses}}$$

- Similar to the Income Reliance Ratio, analyze proportion of expense categories to total expenses
  - Membership
  - Meetings and events
  - Publications
  - Certifications
  - Management/Governance
- What does the trend look like?

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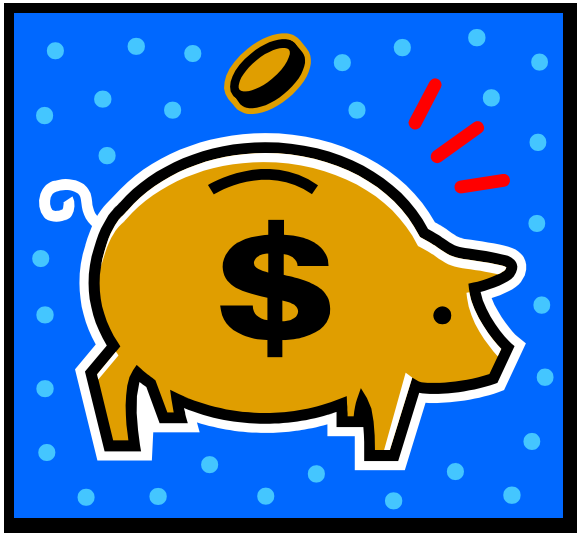
Measurements and Metrics – Savings Indicator

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

- Measures the rate of savings
- Simple way to determine if organization is adding to or using up its net assets base
- Should be considered in combination with adequacy of resources indicators



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Measurements and Metrics – Other Financial Ratios

- CEO wages as a percent of total expenses
- Personnel costs as a percent of total expenses
- Benefit costs as a percent of total expenses
- Benefit costs as a percent of total compensation
- Cost per Member
- Revenues per FTE
- Expenses per FTE
- Total Compensation per FTE
- Investments as a percent of total assets
- Occupancy as a percent of total expenses
- Meetings expenses as a percent of total expenses

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Measurements and Metrics – Program Service Expenses

$$\frac{\text{Program Service Expenses}}{\text{Total Expenses}}$$

- Measures relationship of program expenses to all expenses
- Can vary widely from industry to industry and by the size of the organization
- BBB Wise Giving Alliance → standard of 65%
- Charity Navigator → standard of 66.7%

- Conversely, one can also look at the support services as a percent of total expenses

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Measurements and Metrics – Fundraising Efficiency

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

- Calculates how much the organization spends to generate $1 in charitable contributions
- Charity Navigator gives highest rating to those with less than $0.10
- Charity watch indicates $0.35 is reasonable for most charities

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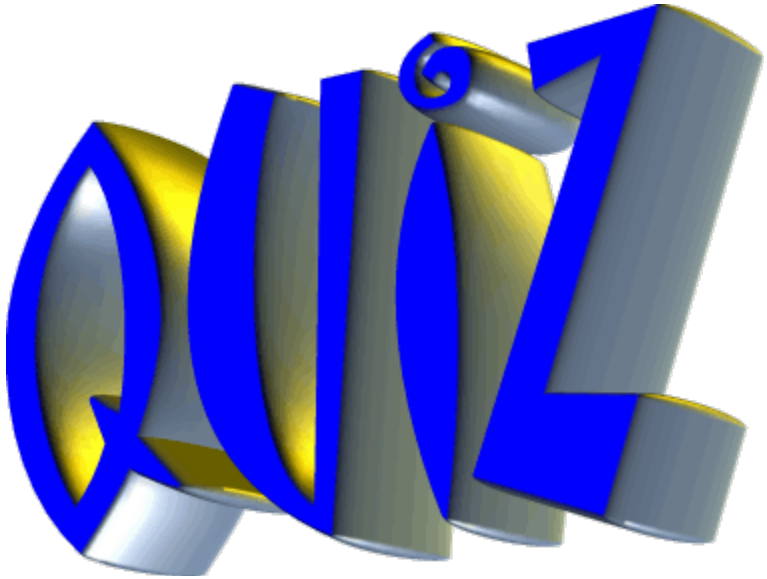

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True or False?

1. An Association's excellent reputation will be included as an asset on the balance sheet

   FALSE

2. An Association's large member base is specifically included in the calculation of the expense allocation ratio.

   FALSE

3. An unqualified or disengaged Board of Directors is the denominator to the days cash on hand ratio.

   FALSE

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Measurements and Metrics – Non-Financial

- Don't forget about non-financial measurements as well!
  - Members
  - Attendees
  - Continuing Education Hours delivered
  - Number of Certificants
  - Board members
  - Employees
  - Volunteers
  - Service area / market share
  - Other mission related measurements
- Very important to factor in non-financial aspects of the Association when analyzing financial measurements

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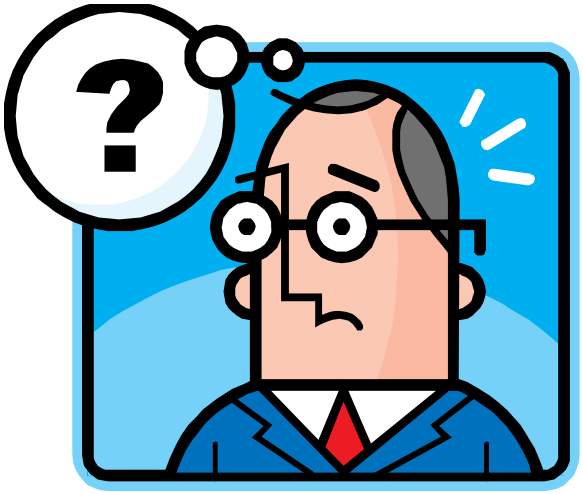
So how do we use this information to help our organization?



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Why Benchmark?

- Because numbers are meant to be compared!
- Because the most effective measures of financial health represent relationships!
- As a way to share and collaborate, stimulate conversation and reflection, and take pulse of environmental trends.
- To get what you want!!!

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Why Benchmark? (Continued)

- Benchmark when you want to…
  - Compare like attributes from similar organizations
  - Make better-informed decisions
  - Answer the question “how do I compare?”
  - Take pulse of your financial health
  - Obtain a single version of the truth

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5 Key Questions to Consider when Benchmarking

#1 Are available financial resources sufficient to support our mission?

#2 How are our resources used, and are they being used efficiently and effectively?

#3 How are we performing on a relative basis?

#4 What are problem areas we can try to solve?

#5 What areas of superior performance or accountability can we discover?

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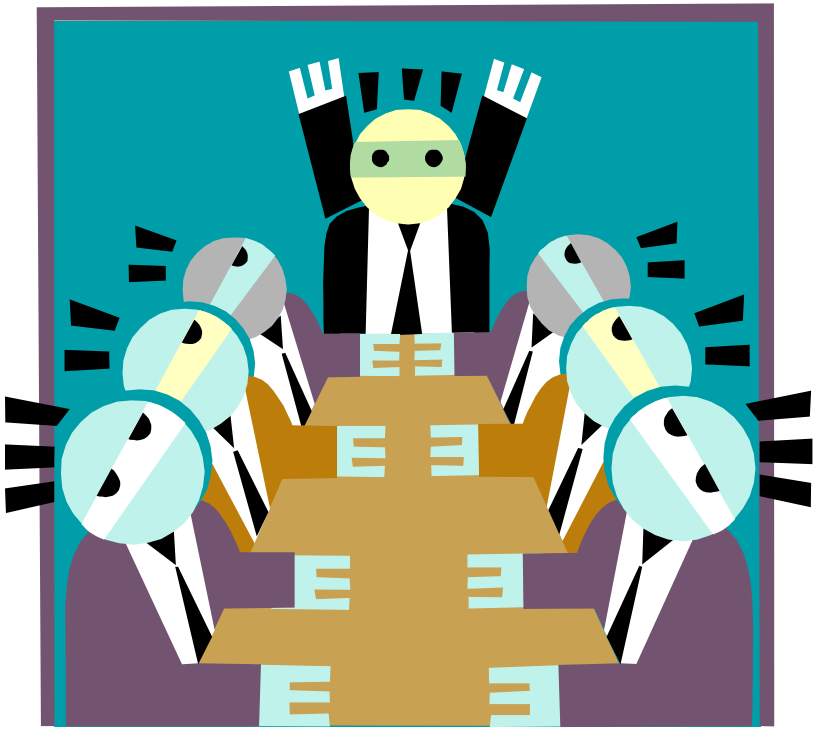
In the Boardroom



Board Meeting Presentations

- Provide a quick snapshot of the current financial status
  - ◊ Discuss detailed statements and comparisons to budget through the finance committee
- Provide a summary report of key issues related to the finances of the organization
  - ◊ Use a “Financial Dashboard”
  - ◊ Communicate measurements and metrics in an efficient and effective manner
  - ◊ Color coded

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What Tools are Available – Benefits/Limitations

- Find a peer group of similar organizations and work with them to compile data on a regular basis.
- GuideStar – Lots of free information stemming from filed Federal Form 990s
- FinancialSCAN

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Using Guidestar to Gather Benchmarking Data…

http://www.guidestar.org/rxg/analyze-nonprofit-data/index.aspx

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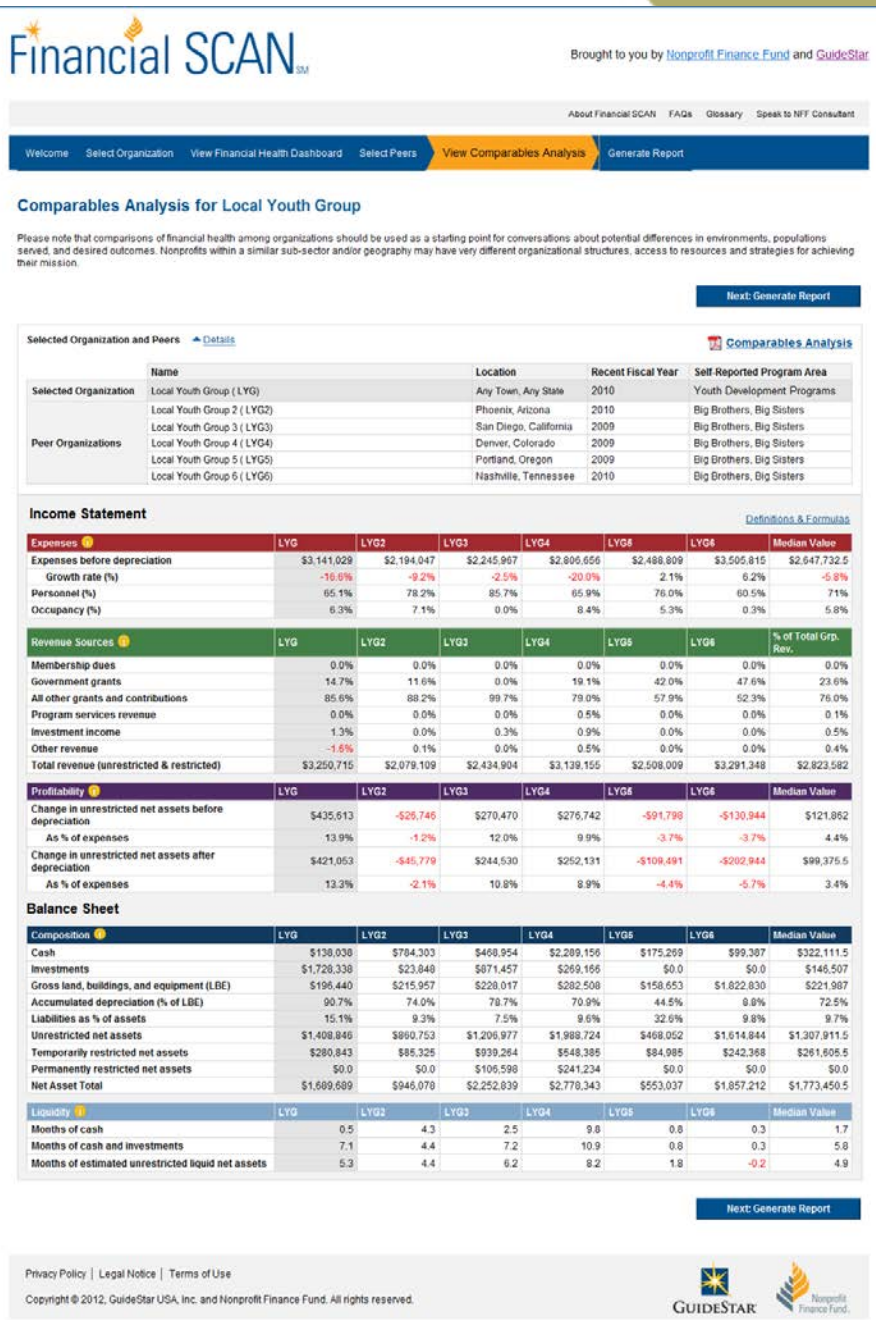

Financial SCAN℠

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Welcome | Select Organization | View Financial Health Dashboard | Select Peers | View Comparables Analysis | Generate Report

Comparables Analysis for Local Youth Group

Please note that comparisons of financial health among organizations should be used as a starting point for conversations about potential differences in environments, populations served, and desired outcomes. Nonprofits within a similar sub-sector and/or geography may have very different organizational structures, access to resources and strategies for achieving their mission.

Next: Generate Report

Selected Organization and Peers ▲Details — Comparables Analysis

	Name	Location	Recent Fiscal Year	Self-Reported Program Area
Selected Organization	Local Youth Group (LYG)	Any Town, Any State	2010	Youth Development Programs
Peer Organizations	Local Youth Group 2 (LYG2)	Phoenix, Arizona	2010	Big Brothers, Big Sisters
	Local Youth Group 3 (LYG3)	San Diego, California	2009	Big Brothers, Big Sisters
	Local Youth Group 4 (LYG4)	Denver, Colorado	2009	Big Brothers, Big Sisters
	Local Youth Group 5 (LYG5)	Portland, Oregon	2009	Big Brothers, Big Sisters
	Local Youth Group 6 (LYG6)	Nashville, Tennessee	2010	Big Brothers, Big Sisters

Income Statement

Definitions & Formulas

Expenses	LYG	LYG2	LYG3	LYG4	LYG5	LYG6	Median Value
Expenses before depreciation	$3,141,029	$2,194,047	$2,245,967	$2,806,656	$2,488,809	$3,505,815	$2,647,732.5
Growth rate (%)	-16.6%	-9.2%	-2.5%	-20.0%	2.1%	6.2%	-5.8%
Personnel (%)	65.1%	78.2%	85.7%	65.9%	76.0%	60.5%	71%
Occupancy (%)	6.3%	7.1%	0.0%	8.4%	5.3%	0.3%	5.8%

Revenue Sources	LYG	LYG2	LYG3	LYG4	LYG5	LYG6	% of Total Grp. Rev.
Membership dues	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Government grants	14.7%	11.6%	0.0%	19.1%	42.0%	47.6%	23.6%
All other grants and contributions	85.6%	88.2%	99.7%	79.0%	57.9%	52.3%	76.0%
Program services revenue	0.0%	0.0%	0.0%	0.5%	0.0%	0.0%	0.1%
Investment income	1.3%	0.0%	0.3%	0.9%	0.0%	0.0%	0.5%
Other revenue	-1.6%	0.1%	0.0%	0.5%	0.0%	0.0%	0.4%
Total revenue (unrestricted & restricted)	$3,250,715	$2,079,109	$2,434,904	$3,139,155	$2,508,009	$3,291,348	$2,823,582

Profitability	LYG	LYG2	LYG3	LYG4	LYG5	LYG6	Median Value
Change in unrestricted net assets before depreciation	$435,613	-$26,746	$270,470	$276,742	-$91,798	-$130,944	$121,862
As % of expenses	13.9%	-1.2%	12.0%	9.9%	-3.7%	-3.7%	4.4%
Change in unrestricted net assets after depreciation	$421,053	-$45,779	$244,530	$252,131	-$109,491	-$202,944	$99,375.5
As % of expenses	13.3%	-2.1%	10.8%	8.9%	-4.4%	-5.7%	3.4%

Balance Sheet

Composition	LYG	LYG2	LYG3	LYG4	LYG5	LYG6	Median Value
Cash	$138,038	$784,303	$468,954	$2,289,156	$175,269	$99,387	$322,111.5
Investments	$1,728,338	$23,840	$871,457	$269,166	$0.0	$0.0	$146,507
Gross land, buildings, and equipment (LBE)	$196,440	$215,957	$228,017	$282,508	$158,653	$1,822,830	$221,987
Accumulated depreciation (% of LBE)	90.7%	74.0%	78.7%	70.9%	44.5%	9.8%	72.5%
Liabilities as % of assets	15.1%	9.3%	7.5%	9.6%	32.6%	9.8%	9.7%
Unrestricted net assets	$1,408,846	$860,753	$1,206,977	$1,988,724	$468,052	$1,614,844	$1,307,911.5
Temporarily restricted net assets	$280,843	$85,325	$939,264	$548,385	$84,985	$242,368	$261,605.5
Permanently restricted net assets	$0.0	$0.0	$106,598	$241,234	$0.0	$0.0	$0.0
Net Asset Total	$1,689,689	$946,078	$2,252,839	$2,778,343	$553,037	$1,857,212	$1,773,450.5

Liquidity	LYG	LYG2	LYG3	LYG4	LYG5	LYG6	Median Value
Months of cash	0.5	4.3	2.5	9.8	0.8	0.3	1.7
Months of cash and investments	7.1	4.4	7.2	10.9	0.8	0.3	5.8
Months of estimated unrestricted liquid net assets	5.3	4.4	6.2	8.2	1.8	-0.2	4.9

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