

Nonprofit Risk Management Center
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The Deep End: Nonprofit Finance and Audit Committees

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What is financial risk management?

The concepts, policies, and systems that enable an organization to manage without undue exposure to significant financial losses arising from those factors.”

Source: *Financial Risk Management: A Guide for Nonprofit Executives*

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Goals for sound financial management

- **Ethical Conduct**
- **Accountability**
- **Transparency**
- **Enlightened and Involved Leadership**
- **Sustainability**

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Responsibility for financial risk management

- Board of Directors
 - Duty of care
 - Be reasonably informed, participate in decisions, act in good faith
- Staff
 - Keep board informed of essential matters
 - Engage board in considering financial challenges, opportunities and operations

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Orienting yourself and others to the issues

- Understand nonprofit financial statements
- Understand the finances and the budgets
- Review historical information

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Internal Controls

Designed to provide reasonable assurance regarding the achievement of objectives in three categories:

1. operations
2. financial reporting
3. legal compliance

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Role of the Finance Committee

- oversees preparation of annual budget and financial statements.
- oversees administration, collection, and disbursement of financial resources.
- advises board on making significant financial decisions.

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Role of the Audit Committee

- selects auditor
- approves scope and fees
- reviews auditor's other involvement
- ensures direct line of communication
- reviews adequacy of internal controls
- reviews adequacy of financial reports

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Role of the Audit Committee

continued

- reviews disputes between auditor and management
- reviews published financial statements
- investigates matters brought to its attention during the course of the audit

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Necessity of Establishing an Audit Committee

- improves organizational accountability
- required by some states
- recommended by the Panel on the Nonprofit Sector

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Audit Committee vs. Finance Committee

<ul style="list-style-type: none"> • Finance - ensures that budgets and financial statements are prepared. 	<ul style="list-style-type: none"> • Audit - has <i>oversight</i> for ensuring that reports are received, monitored, and disseminated appropriately.
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Audit Committee vs. Finance Committee

<ul style="list-style-type: none"> • Finance - monitors financial transactions. 	<ul style="list-style-type: none"> • Audit - makes sure things are done according to policy and with adequate controls.
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Audit Committee vs. Finance Committee

- Finance – provides guidance about actions that can be taken.
- Audit - ensures that independent oversight occurs.

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Finance and Audit Committees' Structure

- Leadership
- Membership
- Qualifications
- Meeting formats

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7 characteristics of a financially healthy nonprofit

1. Sufficient income to ensure stable programming.
2. Internal source of cash or ready access to cash in times of shortfall.
3. Income-based rather than budget-based spending.
4. Positive cash fund balance.
5. Accumulated surpluses that are sufficient to cover the current year's deficit.
6. Established (or has plans to establish) an operating reserve to finance growth and cash shortfalls.
7. Board and management holding themselves responsible for the financial stability of the organization.

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7 Red Flags

- failure to report or inaccurate financial reporting
- failure to meet minimum legal and regulatory requirements
- failure to budget responsibly
- failure to track income and expenses on a timely basis
- ineffective tracking of restricted funds
- large income losses
- ineffective internal controls

And don't forget...

- failure to track staff time – allocate personnel time to key programs

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Other resources from the Center

Financial Risk Management:
A Guide for Nonprofit Executives

New Software Tool:
My Financial Management Plan
www.myfinancialmanagementplan.org

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Next month's Webinar
March 3, 2010 2 p.m. eastern

Ethics and Conflict of Interest Policies

Explore the role of ethics and conflicts of interest policies to strengthen the foundation of a nonprofit.

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Any questions?

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