

Financial Questions Every Board Member Should Ask

Although board members typically do not manage the day-to-day activities of the nonprofit, they do act as stewards and have fiduciary financial responsibilities. As a board member, you must act in good faith and make informed decisions. In order to do that, you will require answers to the following questions. If an organization is resistant to answering these questions, it may indicate a red flag.

Know the answers to these questions:

What is the Organization's Current Cash Position? How Many Days of Cash on Hand?

Cash on hand is good indicator of the solvency of the organization and represents the amount of cash readily available to the nonprofit - usually in the checking account. A benchmark to strive for is 3 to 6 months of operating expenses.

What Are the Key Sources of Revenue?

What is the mix of unrestricted temporarily restricted and permanently restricted net assets? Understanding the makeup of revenue for the organization (e.g. government contracts, fee-for-service, donations, grants) helps you understand the key stakeholders and the stability or vulnerability of your revenue.

- Does the bulk of revenue come from a single donor or government agency?
- What if the donor passed away suddenly or there were a cut in government funding?
- Although there are funds on a balance sheet, if they are restricted, they are not available to fund operating expenses.
- Insufficient unrestricted assets limit the organization's ability to respond quickly to organizational needs.

Is there an Operating Reserve?

In addition to cash on hand, many nonprofits create an operating reserve fund that represents a “rainy day” fund – a source that could pay operating expenses in the event that expected revenue is not received. It is generally measured in how many days, weeks, or months the organization could continue to operate with no new revenue. Many nonprofits strive for a 3-to-6-month operating reserve.

Is there Currently a Line of Credit? Has It Been Recently Activated?

A line of credit allows the organization to borrow money over a very short term, helping to bridge a revenue gap. Most banks require some type of collateral (i.e., future promise of state or federal funding or real estate) and frequently tie the interest rate to some national indicator (e.g., prime rate plus one percent). Best practice is for nonprofits to secure a line of credit before it is needed, so that it can be activated quickly to plug a revenue gap.

Is there an Endowment? If so, how is It Managed?

If a nonprofit has an endowment, board members should understand how the fund is invested and managed and how much goes back into the general operations of the nonprofit.

- Is it invested in a broad range of securities with a trustworthy investment firm?
- Is the organization using funds from principal to support its operations or just interest?
- Does the board annually approve the spending policy from the fund?

Are there Financial Policies that Safeguard the Organization from Fraud and Embezzlement?

Fraud and embezzlement can be a very real threat to any nonprofit. Not only do fraud and embezzlement drain precious funds from your organization, but they can create a public relations nightmare, causing donors and others to question your ability to safeguard your funds. No one person in the organization should have complete and unchecked access to your funds. Is there a board committee tasked with overseeing policies related to fraud prevention?

Is there a Whistleblower Policy that Encourages Employees to Expose Possible Fraud?

The Sarbanes-Oxley Act of 2002 requires that every organization implement policies that encourage both employees and volunteers with the organization to report suspected fraudulent activities without fear of repercussion from the organization. In other words, an employee should feel free to report suspected fraudulent activity about his boss or another employee without fear of losing his job. The IRS Form 990 specifically asks you to report on your whistleblower policy.

Is there a Year-End Financial Review or Audit? Are these Documents Shared with the Full Board?

Laws regarding required audits or financial reviews differ by state. The board should be aware of what the legal thresholds are for the state. Even when an audit is not required, the board can decide to establish having an audit as the best practice for the organization.

Are Annual IRS Filings Reviewed by the Board Prior to Filing?

An annual IRS Filing (the Form 990) is required of all nonprofits. Once the Form 990's are filed, they become public documents. Guidestar.org is one of the most popular sites makes the 990 forms of nonprofits available for viewing. It is good practice for all board members to be aware of the information contained in this public filing.

Are Regular Financial Reports Provided to the Board in a Timely Manner?

One of a board member's key roles is to provide financial oversight to the organization, so regular review of recent financial information is vital. Clear financial statements communicate the overall picture and allow board members to raise questions and make informed decisions.

Does the Board Assist in Developing and Approving an Operating Budget for the Coming Year?

Board members should understand the financial position of the organization and review financial information at every meeting. As part of the board's oversight and planning role, the operating budget for the coming year should be approved by the full board prior to implementation.

While asking financial questions may feel awkward, it will show that you take your fiduciary responsibilities as a board member seriously.