Governance and Finance:

How do they go together?

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Overview of session

- Role of the board of directors
- What financial information should board members get?
- When should they get it?
- **What should they be looking for?**
- Role of the board vs. role of manager
- Resources

Effective boards must:

- Protect the interests of both members and the cooperative corporation (*fiduciary duty*)
- Build an influential team, capable of opposing management when necessary
- Serve as trusted advisors to management
- Monitor and oversee management

Fiduciary duty: Protect the interests of both the members and the co-op

- Build a culture of education and openness
- Board members must understand and be able to oversee:
  - mission, vision, values of the cooperative
  - financial statements and can ask good questions
  - the budget
  - the cooperative bylaws and policies

What information do board members need in order to oversee the finances of the cooperatives?

3 Basic Financial statements

- Income Statement – should receive monthly
- Balance Sheet – should receive monthly
- Cash flow Statement – prepared annually as part of an audit; should be produced more frequently when cash is tight

What other financial information might a board want to receive?

- Financial ratios and analysis – quarterly, or more often as needed
- Explanation of significant deviations from budget
- Annual budget
- Industry performance standards for comparison
- Private meeting with their auditor, if applicable

The Income Statement – *a view of activity over a period of time*

Revenues –Expenses = profit/loss

Also called Profit and Loss (P and L). . .

The Income Statement

+ Revenues (sales)

+ Other income

- Cost of Goods Sold (direct care hours)

= Gross profit

- Operating expenses (fixed and variable)

- Other expenses

= Net profit/(loss)

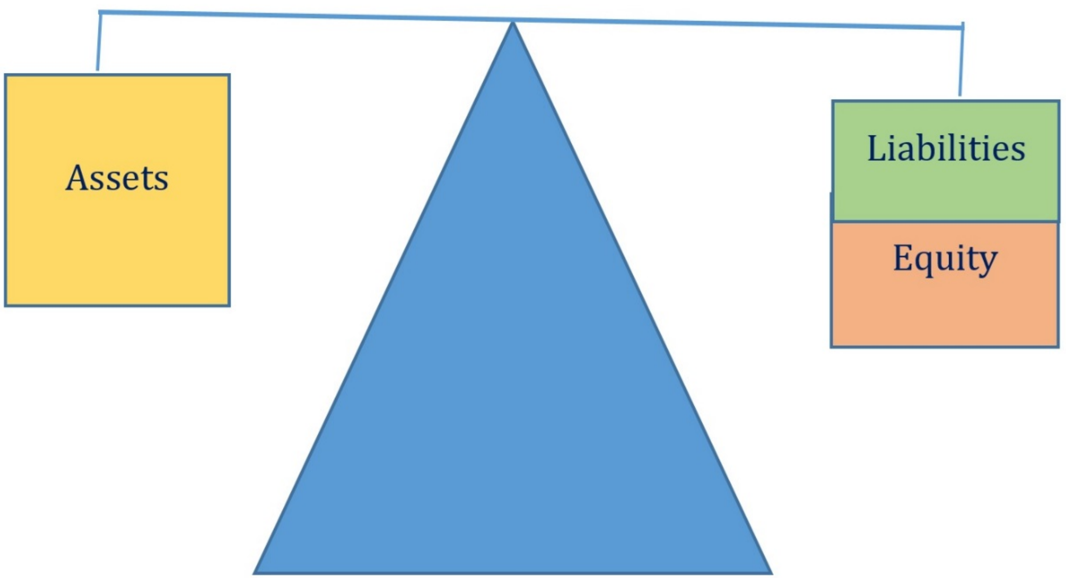
A word about expenses . . .

- Profit margin is X cents on a dollar of sales
- At 5% profit, it is usually easier to save $100 ($1.92 per week) in expenses than to find $2,000 in new revenues
- Fixed expenses (like management, training coordinator) go down as a percentage of sales as a company grows
- For us, gross margin might be different than industry average because we may choose to pay caregivers more

Things to track . . .

- Look at period and year-to-date
- Compare to this time last year
- Compare to budget (with explanations of significant deviations)
- Compare by customer or revenue source
- Cash vs. accrual accounting (compare apples to apples)
- Are there any odd sources of revenue or expenses you don’t understand?

The Balance Sheet – *a "snapshot" in time*



The Balance Sheet -- Assets

Cash

Other current assets (accounts receivable etc.)

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= Total current assets+

Fixed assets (equipment, furniture etc.)+

Other assets

____

=Total Assets

The Balance Sheet – *what you owe and what you own*

Current liabilities (payroll, accounts payable etc.) +

Long term liabilities (bank loans, etc.)

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= Total Liabilities

The Balance Sheet - *and what you own*

Paid in capital (from members)+

Member accounts (qualified and unqualified distributions of earnings to members) +

Retained earnings (earnings from previous years not allocated to members) +

Earnings YTD

= Total equity (net worth)

Things to track . . .

- Ask for the balance sheet! It is just as important as the income statement
- Are accounts receivable or accounts payable growing in unexplained way (*are you getting paid and paying your bills*)?
- Is there sufficient cash cushion?
- Is equity positive?
- Compare to previous year – any unexplained differences?
- Are there assets or liabilities you don't understand?

The Cash Flow Statement

- Cash from operating activities (earnings, non-cash items, purchase of inventory or other assets etc.
- Cash from investing activities (property, equipment, investments in other companies etc.)
- Cash from financing activities (loan distributions, loan repayments, member shares sold)

Things to track . . . "*Cash is what pays the bills*"

- Where is your cash actually coming from?
- Is it where you expect?

Some ratio tools you can use

- Current ratio (current assets/current liabilities)
- Debt:Equity ratio (what you owe vs what you own)
- Days accounts payable
- Days accounts receivable/ Aging of Rec.
- Working capital (may need more with growth)
- Revenue/client (over time and **by source**)
- Client mix (and where you are making $)
- Hours/client (over time)
- Mileage per client (over time)

The role of the board and the role of managment

- You are on the same team
- Management should support the board in making sound decisions
- Management handles operations
- Board makes policy decisions
- Board hires, evaluates and fires management

The board must build its own team

- Represent members
- Make sure that all voices on the board are heard
- Orient new board members
- Board development & evaluation

What’s the alternative?

“Then, gentlemen, it is the consensus of this meeting that we say nothing, do nothing and hope it all blows over before our next meeting.”

"Then, gentlemen, it is the consensus of this meeting that we say nothing, do nothing, and hope it all blows over before our next meeting."

Some Resources

- Networks
- Other co-ops
- Outside board member, finance committee member or advisor to the board
- Consultants, specialists
- Democracy At Work Institute website
- University of Wisconsin Center for Cooperatives website