

Managing Cash Flow

While standard nonprofit financial reports – the budget, income statement, and balance sheet – provide important management information, these statements alone do not tell whether there is enough cash on hand to pay for an unexpected heating repair, to take on a new program opportunity, or even to cover payroll next month. For this, effective cash flow management is essential.

WHY MANAGE CASH FLOW

Every organization experiences ups and downs in cash flow because the timing of when money is received often doesn't match when payments are due. Common causes of cash flow shortages are:

- Timing of donations and grants
- Reimbursement-based contracts
- Timing of disbursement, such as advance payments
- Changes in revenue sources or payment schedules
- Operating with a deficit (expenses exceed revenue)
- Unexpected or unplanned events

The cost of these shortages can be very high, including:

- Late fees, penalties, and finance charges
- Damaged relationships with vendors and contractors
- Lost opportunities for new mission-building activities
- Time spent worrying about and trying to resolve cash flow problems after they occur.

WHEN TO MANAGE CASH FLOW

While cash flow management is always a useful tool, it is particularly important to diligently manage cash flow when your organization is undergoing significant financial changes, such as:

- Developing and implementing new programs
- Recovering from or facing deficits
- Adding or cutting back on programs or staff

- Experiencing changes in sources and structure of funding

By understanding cash flow and planning ahead, we can avoid problems and shortages, provide stability to our organizations, and take advantage of opportunities to purchase capital assets and build organizational capacity. Managing cash flow is not a one-time activity. Projections should be updated and reviewed regularly. The frequency will depend on how closely the organization's cash flow needs to be monitored.

HOW TO MANAGE CASH FLOW

The earlier you anticipate cash flow issues, the easier it is to address them. The most effective way to manage cash flow is to develop and maintain cash flow projections that look forward 12 months.

Nonprofits Assistance Fund has developed a cash flow projection template, an Excel spreadsheet that can be downloaded at www.nonprofitsassistancefund.org. The template provides a general framework with built-in calculations. As with all financial reports, the usefulness of cash flow projections hinges on the accuracy of the information used.

When developing projections:

- Start with an accurate cash balance
- Base projections on realistic budget assumptions

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- Reflect the expected timing of receipts and payments, don't just divide by 12
- Pay particular attention to when you expect to receive grants and use conservative assumptions for unidentified grant funds
- Be careful about including grants that are restricted for use in a future time period
- Check your payroll schedule (remember, if you have biweekly payroll there will be two months a year when you must pay three payrolls)
- Note any lump sum payments, such as payments for insurance, printing, payroll taxes, etc.
- Break lump sum payments into smaller, more frequent payments
- Delay new programs or events
- Delay staff additions and/or salary increases
- Borrow on a line of credit or bridge loan

2. Manage the amounts (deficits)

Increase cash receipts:

- Increase fees and prices
- Increase services that generate revenue
- Raise additional or emergency funds
- Rent out or sublet excess space
- Sell under-used assets

Reduce cash disbursements:

- Scrutinize expenses for temporary or permanent reductions
- Solicit in-kind goods and services to replace budgeted items
- Reduce staff salaries or hours, or layoff staff
- Close facilities or reduce programs or services

Once you have a cash flow projection, you are then able to:

1. Plan the use of cash
2. Prepare to avoid problems
3. Respond to changes and adjust plans

CASH FLOW MANAGEMENT STRATEGIES

When you anticipate cash flow shortfalls, there are a number of strategies that can help prevent them. As a first step, assess whether the cash flow shortfall is a problem with timing or is an indication of a deficit. The strategies used to solve the cash flow problem should match the source of the shortfall.

1. Manage the timing

Speed up receipt of income:

- Negotiate earlier receipt of grants or contract revenue
- Shorten the terms you allow for accounts receivable
- Improve collection efforts for past due receivables
- Introduce new payment options, i.e. credit cards or automatic payments
- Accelerate or expand fund drives

Slow down payments:

- Delay significant expenditures
- Negotiate longer terms with vendors

HOW TO AVOID CASH FLOW PROBLEMS

- Develop realistic, well-considered budgets each year
- Consistently operate with the goal of a surplus of income over expenses
- Build internal cash reserves over time
- Plan early and often
- Be aware of cash flow and budget assumptions and react to changes
- Maintain good relationships with vendors, contractors, and bankers