

Urban Land Conservancy Financial Management for Nonprofits Considering MTNC

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Nonprofit organizations considering a location in a Multi-Tenant Nonprofit Center (MTNC) need a clear understanding of their financial position in order to evaluate the MTNC opportunity, meet the requirements of the MTNC sponsor/developer and contribute to a viable MTNC. This White Paper lays out some issues to consider for nonprofits and basic information on how to understand financial statements.

A multi-tenant nonprofit center (MTNC) exists to provide an opportunity for nonprofits to realize cost savings and operational synergy. MTNC developers design cost-efficient facilities to be financially sustainable and benefit nonprofit tenants by passing on reduced costs. Given that there are two levels of mission-driven activity (the MTNC and nonprofit tenants), there is an acute need for sound fiscal management.

The MTNC developer, like any landlord, wants tenants who will be able to pay their rent on time. Like any landlord, an MTNC reserves the right to terminate a lease if the terms are not met. However, the charitable status of nonprofit tenants and the nurturing mission of the MTNC make it highly desirable to avoid eviction proceedings by strict tenant screening.

Financial Implications of MTNC

A nonprofit organization considering locating in an MTNC needs to know the financial implications of such an arrangement. The lease is a contractual arrangement between two nonprofits and, in some cases, could be more complex than typical leases.

Tenants will want to consider:

- All-in costs (see below)
- Facility amenities
- Lease term (ability to sub-lease and terminate early)
- Potential for meaningful synergy with other nonprofits
- Capacity of landlord to manage MTNC

MTNC developers will want to consider:

- Tenant's credit history
- Tenant's financial health and ability to pay rent
- Tenant's ability to afford common costs
- Tenant's ability to contribute to MTNC synergy

Nonprofits need to understand their financial position as well as their financial statements to (1) decide if MTNC is a good option for their organization and (2) to fulfill the requirements of the MTNC developer who is looking for creditworthy tenants.

In general, nonprofits generate two types of financial statements: audits and interim (internally prepared) statements. Nonprofit managers need to have a basic command of both reports and be able to explain the financial health of their organization. Audits are prepared by outside certified accountants who are knowledgeable about GAAP (Generally Accepted Accounting Principles) and FASB (Financial Accounting Standards Board). An audit is an independent verification of an organization’s financial management systems and is completed by examining a set of transactions within a certain period of time.

Interim statements are financial statements produced in-house by staff or contractors on a monthly or quarterly basis. They often do not include all the adjustments made in an audit which is normally completed once a year.

Both an audit and interim financial statements should include a Statement of Financial Position (Balance Sheet) and a Statement of Activities (Income Statement). Nonprofit managers should have a command of the basic information these reports provide. The following are basic examples of each.

| Statement of Financial Position | | ABC Nonprofit, Inc. |
|---------------------------------|----------------------------------|---------------------|
| Date | | 12/31/2009 |
| <u>Assets</u> | | |
| Cash | | \$25,027 |
| Accounts Receivable | | \$16,125 |
| Other Assets | | \$50,950 |
| | Total Assets | \$92,102 |
| <u>Liabilities</u> | | |
| Accounts Payable | | \$1,445 |
| Accrued Payroll | | \$11,010 |
| | Total Liabilities | \$12,455 |
| <u>Net Assets</u> | | |
| Unrestricted | | \$54,647 |
| Temporarily Restricted | | \$25,000 |
| Permanently Restricted | | \$0 |
| | Total Net Assets | \$79,647 |
| | Total Liabilities and Net Assets | \$92,102 |

Statement of Financial Position is always a snapshot of financial health on a given day

This nonprofit is in good shape. Assets are \$92,102 and liabilities are \$12,455, so it has a cushion of net assets of \$79,647.

Net Assets are the difference between what you own (assets) and what you owe (liabilities). The bigger the Net Assets the better.

A temporarily restricted net asset could be a grant that is earmarked for a special purpose and won't be counted in Total Assets until it is used accordingly.

Total Assets – Liabilities = Net Assets
Liabilities + Net Assets = Total Assets

| Statement of Activities | | ABC Nonprofit, Inc. |
|-------------------------------|--|------------------------|
| Date | | Year Ending 12/31/2009 |
| <u>Revenues</u> | | |
| Foundation Support | | \$64,250 |
| Government Grants | | \$50,000 |
| Individuals | | \$8,345 |
| Special Event | | \$12,835 |
| Total Revenues | | \$135,430 |
| <u>Expenses</u> | | |
| Staff salaries/taxes/benefits | | \$95,883 |
| Accounting Fees | | \$3,344 |
| Legal | | \$619 |
| Insurance | | \$3,747 |
| Meetings | | \$476 |
| Office | | \$1,195 |
| Phone | | \$1,408 |
| Postage | | \$688 |
| Rent | | \$11,400 |
| Travel | | \$1,127 |
| Utilities | | \$904 |
| Other | | \$621 |
| Total Expenses | | \$121,412 |
| Net Revenues | | \$14,018 |

Statement of Activities or Income Statement shows the revenues and expenses for a period of time, usually 12 months.

When considering a MTNC, a nonprofit will want to compare its current costs for rent, utilities, phone, insurance, office supplies etc.

Revenues exceed expenses by \$14,018 for the period. This is good and shows the organization can manage its budget and not spend more than it takes in.

Nonprofit managers will need to be able to review their Statement of Financial Position and understand whether they have sufficient net assets to make a move to a MTNC. If revenues were to falter, could the nonprofit continue to meet its rental obligation to the MTNC? Can it tap into unrestricted net assets, or reserves, to cover shortfalls?

Nonprofit managers will also need to be able to explain their Statement of Activities and describe their sources of revenues and types of expenses. A nonprofit with a deficit position (expenses exceed revenues) will need a clear explanation of why this happened and how it will be remedied in the future. A pattern of repeated operating deficits over several years may indicate that a nonprofit has not managed its budget adequately and could be a higher risk to a MTNC developer.

The key issue for both the nonprofit tenant and the MTNC developer is that both parties understand the financial statements. Communication is central to a positive landlord-tenant relationship in MTNC.

Nonprofit tenants will want to evaluate the costs and benefits for their organization. Nonprofits considering an MTNC need to be sure they also understand all the costs involved and how they compare to alternative locations. There are also non-quantifiable aspects to different offices, such as the layout or floor plan, location, and amenities. Nonprofits should systematically compare the following:

| | Current Location | MTNC |
|---------------------------------------------------------------------------------------------------------------------------|------------------|-----------------------------------------------|
| Rent | \$x | Higher? Lower? Same? |
| Other occupancy costs: parking, utilities, phone, cleaning, IT | \$x | Higher? Lower? Same? |
| Square footage | X square feet | More? Less? Same? |
| Floor Plan | X | More/less efficient floor plan? |
| Location | X | Better? Worse? For whom? |
| Amenities (conference rooms, special event space, kitchens, training areas, reception areas, shower/gym, shared services) | X | Better? Worse? What is the cost differential? |

In general, rental rates are calculated on a per square foot (p.s.f.) basis. Nonprofits in the metro Denver area can expect to pay \$4-\$5 per square foot for many basic office spaces (perhaps an older building not recently renovated) up to \$15-\$20 per square foot for higher-end, more luxurious space. These are very rough approximations and are offered only as general guidelines. Per square foot amounts will vary depending on the location, quality of the space and amenities offered. This can often be captured in the classification of: Class A, Class B, and Class C office space with Class A being the most luxurious and Class C being the most basic.

Monthly rent is calculated by multiplying the per square foot rate (ex. \$6 p.s.f.) by the amount of space rented (ex. 1,000 square feet) and dividing by twelve months.

$$\$6.00 \text{ p.s.f.} \times 1,000 \text{ square feet} = \$6,000/12 \text{ months} = \$500 \text{ per month}$$

Some items may have costs that would be shared in a MTNC, such as IT support or a receptionist. Nonprofits should be very clear, before moving, on how costs are shared in a MTNC. For instance, are costs divided evenly among all tenants? Or are they divided on a pro rata basis, so for example, a tenant with the smallest office pays the least and the tenant with the largest office space pays the largest share?

Final considerations

Nonprofits considering a MTNC want to be sure they are part of a highly functioning operation. Synergy among nonprofits cannot be achieved if all parties are not meeting their financial obligations to the MTNC. As a tenant in a MTNC, nonprofits will want assurances that the other participating nonprofits can also meet the financial obligations they commit to and not create a burden that others must absorb.

When looking to locate in a MTNC, nonprofits should carefully examine their own financial situation and decide if the benefits of a MTNC outweigh the costs. Nonprofits should be prepared to submit requested information so the MTNC developer can evaluate their suitability for the facility.

Nonprofits with a solid understanding of their financial status will be best prepared to determine if a MTNC enhances their mission, AND, will be better candidates for a MTNC because they will have greater clarity around their financial abilities.