FINANCE COMMITTEE REPORT
Enrico Hernandez
March 4, 2017
St. Louis, Missouri

It is with great pleasure that I present the report of the Finance Committee to the Executive Council (EC) in anticipation of its March 4, 2017 meeting. I am honored to serve as a thought partner to the governance body of the Fraternity.

This report will discuss the following topics:

- brief review of non-profit financial accounting,
- finance committee meetings convened since the October EC meeting,
- financial results as of 1/31/2017,
- opportunities
- red flags for the EC.

Financial Accounting In-service

To understand the Fraternity's financial position at any given point in time as well as the interim financial reports provided by staff, it is imperative to understand the difference between accrual and cash basis accounting. Accrual basis accounting is a method of accounting that recognizes revenues when earned and expenses when incurred regardless of when cash is received or paid. Cash basis accounting is a method of accounting in which revenues and expenses are recognized and recorded when received, not necessarily when earned.

It is also important to understand the distinction between an accrual basis budget and a cash basis budget. Both types of budgets need to be developed to facilitate financial oversight. Accrual basis budgets are based on accrual basis accounting principles. Cash basis budgets are essentially cash flow budgets that are based on the cash basis of accounting. Like the Statement of Cash Flows which provides information on cash receipts (inflows) and cash payments (outflows) during a period of time, the cash flow budget will help staff, the EC and the Finance Committee plan the cash needs of the Fraternity. When businesses need cash to meet operating cash needs, they use operating reserves or obtain bridge financing. The Fraternity ought to consider doing the same, as this is considered an industry best practice.

Thus, a surplus on an accrual basis does not necessarily translate to a surplus on a cash basis. This is especially true when our chapters have large accounts receivable balances. In other words, when there is a cash deficit, strategic fraternity programs, infrastructure investments, and staff should not necessarily be cut to meet cash needs. Rather, all efforts of the EC, the Finance Committee, and the staff should focus on collecting past due accounts receivable balances from Chapters.

In addition, the GAC should refrain from entertaining motions to the balance the Fraternity's budget unless it is made clear to which budget it refers. This would require the appropriate non-profit financial acumen on the part of the delegates to the GAC, which is not an option likely to exist. Instead, the Fraternity should have – as the Executive Council has approved – a Finance Committee populated by Brothers having expertise in non-profit finance, accounting and financial management.

Finance Committee Meetings

Two finance committee meetings via teleconference have been held since the last EC meeting. One meeting was held on November 11, 2016 and another was held on January 20, 2017. Items discussed were infrastructure challenges surrounding financial reporting, and interim financial report formats. It needs to be noted that these meetings were historic in the life of the Fraternity in that never in its history have the Fraternity's interim financial statements been made public to those outside of staff and the EC. Best practices dictate that non-profits should issue interim financial statements to report on budget execution.

It also should be noted that the financial reports, at the time, were a work-in-progress in that the ending balances from FY 15-16 were not yet available to staff and that a process to reconcile Patriot (our membership management software) accounts receivable data with QuickBooks (our accounting system) accounts receivable data, had not yet been established. As of the January financial reports, both challenges have been resolved due to the efforts of Amanda Baldwin and Brother Mark Guidi.
In addition, the Finance Committee has requested that the following reports be issued by staff for each meeting:

1) Statement of Financial Position (Balance Sheet)
2) Statement of Activities (Income Statement) with month and YTD actual-to-budget variances
3) Statement of Cash Flows
4) 18-month Rolling Cash Flow Forecast (to be presented to the EC on 3/4/2017 by Br. Guidi)
5) Accounts Receivable Aging
6) Accounts Payable Aging

By issuing and reviewing these statements, staff and the Finance Committee will collaboratively be able to inform the EC of the financial condition of the Fraternity and ensure the long-term viability and sustainability of our beloved Fraternity.

Financial Reporting

Interim financial statements were issued by staff as of 1/31/2017. Based on those statements, I present the following key financial metrics (on an accrual YTD basis) as of 1/31/2017:

1) Operating revenues: $1,983,570
2) Operating expenses: $ 836,118
3) Operating surplus: $ 1,147,451
4) Operating cash increase from 6/1/17 to 1/31/17: $22,897
5) Accounts receivable balance: $1,486,993
6) Accounts payable balance: $472,525
7) Deferred Revenue balance: $30,750

Key financial ratios are:

Ratios	Phi Psi Currently	Benchmarks
Current ratio	3.14	2.0 – 4.0
Quick ratio	3.08	2.0 – 4.0
Days cash on hand	93	N/A – Higher the number the better
Days in accounts receivable	348	Ideally ~30 days
Average payment period or days in A/P	235	60 days or less

As stated above, we need to work on lowering the Days in Accounts receivable; 348 days is too high. This is adversely affecting the Days in Accounts payable.

I have attached a short primer that defines the above ratios. **Appendix B**

Opportunities

The following opportunities will be discussed in future meetings of the Finance Committee:

1) The need to develop program budgets whereby resources and results are identified with fraternity programs and expenses characterized by activity.
2) Organizational slack – **Appendix C**.
3) Establish an operating reserve in addition to the Permanent Fund to fund innovation, capacity building, and cash flow needs.
4) Adopt financial benchmarks that will allow us to compare ourselves to other fraternities of similar size.

Red Flags

1) As stated above, the Days in accounts receivable ratio is too high. I recommend that the EC, the Finance Committee, and the staff concentrate all efforts to collect outstanding chapter balances.

Fraternally submitted,

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Chair, Finance Committee