Introduction

What is the purpose of this assessment and what are its components?

The purpose of an early warning sign, symptom, or system is to alert decision makers of an impending negative circumstance. Early warnings are supposed to provide us with time to react, to change course, to intervene and thus avoid or ameliorate that negative consequence. From an environmental perspective, the far-reaching implications of COVID-19 crisis remain unknown – but the disruption to organizations and communities is undeniable.

What are the early warning signs that a nonprofit organization should be considering significant options, beyond incremental planning? These options might include major restructuring and/or consolidation with other entities. What we know is that major restructuring and consolidation take time. Too often nonprofit leadership maintains optimism that things will get better, or that some saving grace will emerge, for far too long. The failure to anticipate the need for major change has led in many instances to bankruptcy or precipitous closure with substantial injury to communities, staff, clients, partners, and donors as well as the loss of deep experience and tacit knowledge.

The purpose of this tool is to provide nonprofit leadership with some metrics and a methodology to provide an early warning that major change should be initiated. It has two parts: the first is a set of financial metrics that can easily be drawn from audits. The second is an exercise to consider the core of an entity. During a period of retrenchment, when it becomes necessary to shrink, a prime consideration is the determination of what should survive as resources disappear. Once the preferred core is identified, leadership must assess its viability and a set of metrics is used to help with that assessment.

About This Report

- The following pages capture the selections and notes submitted online by the organization’s designated participant(s).
- Please also retain a copy of the Financial Indicators Pre-Work for your reference and future use.
Part 1: Financial Metrics – Warning Signs

Negative results for any one of these criteria should get leadership’s attention. In the current environment, a set of three negative results, in any combination, should cause a “stop and think” occasion and initiate deeper conversations about the entity’s future. In the current environment, indication of significant financial vulnerability could spell real trouble with a precipitously short time frame if an existing major revenue stream is disrupted.

A checkmark indicates that the Warning Sign was noted by the participant(s).

<table>
<thead>
<tr>
<th>Category</th>
<th>Key Financial Ratio or Trend</th>
<th>Warning Sign?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deficit Patterns</td>
<td><strong>12-month Change in Revenue</strong> – Have you experienced a reduction of total revenue greater than -20% within a 12-month period?</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Operating Deficit Trend</strong> – Do you have an operating deficit greater than -10% for 2 out of 3 years?</td>
<td></td>
</tr>
<tr>
<td>Net Asset Trend</td>
<td><strong>Change in Net Assets</strong> – Have you experienced a reduction in net assets (ratio of less than 1) from last year to this year?</td>
<td></td>
</tr>
<tr>
<td>Financial Runway</td>
<td><strong>Defensive Interval</strong> – Reflects how many months the organization could operate with its cash on hand, assets convertible to cash, and cash due, if no additional funds were received. Do you have a defensive interval of less than 4 months?</td>
<td></td>
</tr>
<tr>
<td>Liquidity</td>
<td><strong>Debt Ratio</strong> – Does your total debt exceed 50% of your total assets in either of the past two years? (A high debt ratio indicates future problems with liquidity or reduced ability to borrow funds.)</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Accounts Payable Aging Indicator</strong> – (Indicates approximately how many months it takes an organization to pay its bills.) Does your organization take longer than three months to pay its bills and have an operating deficit greater than -10%?</td>
<td></td>
</tr>
<tr>
<td>Overhead</td>
<td><strong>Fundraising Ratio</strong> – Does your ratio of fundraising expense to fundraising income exceed 30%?</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Administrative or Management Cost Ratio</strong> – Does your percentage of management expenses to all other expenses increase over a period of two or more years, or is it projected to increase to more than 30%?</td>
<td></td>
</tr>
<tr>
<td>Revenue Mix</td>
<td>Is there a pattern of decline in multiple revenue streams?</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Is there a projected, major unplanned decline (greater than 25%) in a revenue stream that accounts for more than 30% of total revenue?</td>
<td></td>
</tr>
<tr>
<td><strong>Total Number of Warning Signs</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Three or more financial Warning Signs should set off a deeper discussion of viability and scenario planning. An organization with no Warning Signs may also want to consider their positioning as they may be able to use the downturn as an opportunity to grow.
Part 2: Considering the Core of the Entity

For those with Warning Signs, leadership should recognize that the entity will be more vulnerable in the expected turbulent period. How should that discussion be framed?

The first scenario to consider is whether the entity can shrink and re-organize, and still remain viable. A bit of imagination is required as leadership may not know with complete certainty what the lost revenue will be or what parts of the entity are at risk. In general, there are four models for designing the part of an entity that remains after major loss. Leadership may or may not have the ability to choose freely among these options, depending upon the nature of funds lost. The options are:

- Option 1: The entire organization but on a smaller scale.
- Option 2: Retain those elements of the organization that are most adaptable or innovative under conditions of uncertainty.
- Option 3: Retain the one, two, or three programs most essential to consumers.
- Option 4: Retain the one, two or three programs that survive the cuts chosen by funders.

Based on scenarios appropriate to your organization, you may want to conduct the exercise below with more than one option and to hold this discussion with multiple stakeholders in the room to avoid optimistic bias. The scoring on this exercise is also subjective. Again, this is about critical thinking and preparedness, not necessarily an exercise to yield a definitive strategy but rather to guide the next set of questions.

Chosen Scenario to Explore

- Option 1: The entire organization but on a smaller scale.
- Option 2: Retain those elements of the organization that are most adaptable or innovative under conditions of uncertainty.
- Option 3: Retain the one, two, or three programs most essential to consumers.
- Option 4: Retain the one, two or three programs that survive the cuts chosen by funders.

Rationale Provided:
## Core Viability

Participant(s) scored each condition below on a scale of 1-5, where 5 is as strong as possible.

<table>
<thead>
<tr>
<th>In your chosen scenario, on a scale of 1-5, to what extent will you have...</th>
<th>Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current stable funding, as indicated by revenues that have exceeded expenses for each of the last three years?</td>
<td></td>
</tr>
<tr>
<td>High appeal to groups providing future support, whether consumer fees, grant funds, state or federal contracts?</td>
<td></td>
</tr>
<tr>
<td>Market demand from a large consumer base that is not expected to shrink?</td>
<td></td>
</tr>
<tr>
<td>Measurable, reportable program outcomes?</td>
<td></td>
</tr>
</tbody>
</table>

### Section Total

### Rationale Provided:

## Competitive Market Strength

Participant(s) scored each condition below on a scale of 1-5, where 5 is as strong as possible.

<table>
<thead>
<tr>
<th>In your chosen scenario, on a scale of 1-5, to what extent will you have...</th>
<th>Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Good location(s) and logistical delivery system?</td>
<td></td>
</tr>
<tr>
<td>Large reservoir of consumer loyalty and the assurance that consumer choice will continue to govern consumer decisions in the future?</td>
<td></td>
</tr>
<tr>
<td>Dominant and growing market share of the target consumers currently served?</td>
<td></td>
</tr>
<tr>
<td>Superior quality coupled with the ability to account for quality?</td>
<td></td>
</tr>
<tr>
<td>Stable staffing (annual turnover rate less than 10%)?</td>
<td></td>
</tr>
<tr>
<td>A refined understanding of what competencies will be required to provide these services in the future and identified sources and resources to acquire them?</td>
<td></td>
</tr>
<tr>
<td>Superior ability to communicate with consumers and other stakeholders?</td>
<td></td>
</tr>
<tr>
<td>Cost effective services and the ability to demonstrate this?</td>
<td></td>
</tr>
<tr>
<td>A solid track record for securing grants, contracts, and donations to support this programming?</td>
<td></td>
</tr>
</tbody>
</table>

### Section Total

### Rationale Provided:
Market Coverage and Cost of Competition

Section responses by participant(s) are reported below.

**COVERAGE** – Choose only one of the following based upon whether consumers have alternatives if your organization closes.

- There are 0 to 1 alternative for consumers.  *(10 points)*
- There are 2-4 alternatives for consumers.  *(0 points)*
- There are 5+ alternatives for consumers.  *(0 points)*

**COST OF AGGRESSIVE COMPETITION**

If there are 2 or more alternatives for consumers, what is the estimated investment required to aggressively compete in the market? Choose a range below ONLY IF you have the available resources.

- $25,000 or less
- $25,001 to $50,000
- $50,001 to $100,000
- $100,001 or more

If you do not have the funding available, how much do you estimate that you will need to raise in order to aggressively complete in the market?

- ____________

*(10 points if funding is available. 0 points if funding needs to be raised.)*

<table>
<thead>
<tr>
<th>Section Total</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th><strong>Part 2: Results and Considerations</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Likely Outcome</strong></td>
</tr>
<tr>
<td>---------------------</td>
</tr>
<tr>
<td>The scenario you explored is likely to be viable.</td>
</tr>
<tr>
<td>In the scenario you explored, your organization is still likely to struggle. Consider partnering with another organization.</td>
</tr>
<tr>
<td>In the scenario you explored, the core entity is still likely to fail. Consider a merger or a consolidation under another organization.</td>
</tr>
</tbody>
</table>

**YOUR TOTAL SCORE**