Nonprofit Business Analysis

Codman Academy Charter Public School and Codman Academy Foundation

by Nonprofit Finance Fund
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December 2007

This report was made possible with funding from an anonymous foundation.

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NFF AND THE NBA

- In 2005, Nonprofit Finance Fund (NFF) celebrated 25 years of service. We are a national Community Development Financial Institution providing financing and advice to nonprofits to help them meet their missions in times of growth and change. We also conduct research and advocacy for capital-wise nonprofit funding & management practices.

- NFF has six local/regional offices and serves nonprofits elsewhere nationally via our National Alliances office.
  - We are headquartered in New York City.
  - On the web: www.nonprofitfinancefund.org.

- Nonprofit Business Analysis (NBA) is our signature advisory service.
  - Our approach is to use a financial lens to help clients understand how financial history and business structure can inform future plans and decisions.

Nothing written in this report or communicated verbally should be construed as an offer by NFF to provide financing or other services to your organization.

MISSION

- The mission of Codman Academy Public Charter School (CACS) is "to prepare students for full participation in the intellectual, economic and civic life of our society, by ensuring their full preparation and access to further education, the skills and vision to undertake a rewarding career, and the motivation and character needed to engage deeply and productively in community life. We view parents and community members as integral partners in this endeavor."

Source: Codman Academy Public Charter School website.

BACKGROUND & RECENT DYNAMICS

- CACS received its charter from the States of Massachusetts' Department of Education in 2001 and opened its doors in the fall of that year. The school is located on the site of the Codman Square Health Center.
- CACS was created in response to a strong community need for a college preparatory, small high school in the Codman Square/Four Corners area. CACS is Dorchester's first charter high school.
- Codman Academy's student body has grown rapidly since its founding class of 29 ninth graders in 2001; in 2007, the school served 110 students.
- During fiscal year 2007, CACS purchased land adjacent to its existing location for the proposed expansion of the school and the Health Center. Leadership is estimating that the capital project will reach $10 MM.

SUMMARY: FINANCIAL OBSERVATIONS

1. Since opening its doors in FY2002 CACS has grown quickly both in terms of its budget and its balance sheet.
2. As the school has increased the number of students and therefore the income it receives from tuition, earned revenue has grown from 36% of total revenue in FY02 to 73% in FY07.
3. Growth in total contributed income has not kept pace with that of earned. However, the composition of raised funds *has* changed; government contributions have declined while support from individuals and foundations has quadrupled.
4. CACS posted post-depreciation operating surpluses in every year from FY02 to FY07. However, these results have been smaller each year as expense growth has outpaced that of revenue.
5. CACS' balance sheet is very liquid, with cash and equivalents representing 65% of total assets at FYE2007.

SUMMARY: FUTURE CONSIDERATIONS

1. Financial preparedness
2. Manage to “full cost” of business
3. Conservative project projections and “Plan B”
4. Further investment in fundraising capacity
   a) Annual subsidy requirements
   b) Idea of comprehensive capital campaign
5. Appropriateness of board-designating cash

Financial Structure Analysis

FINANCIAL OBSERVATIONS

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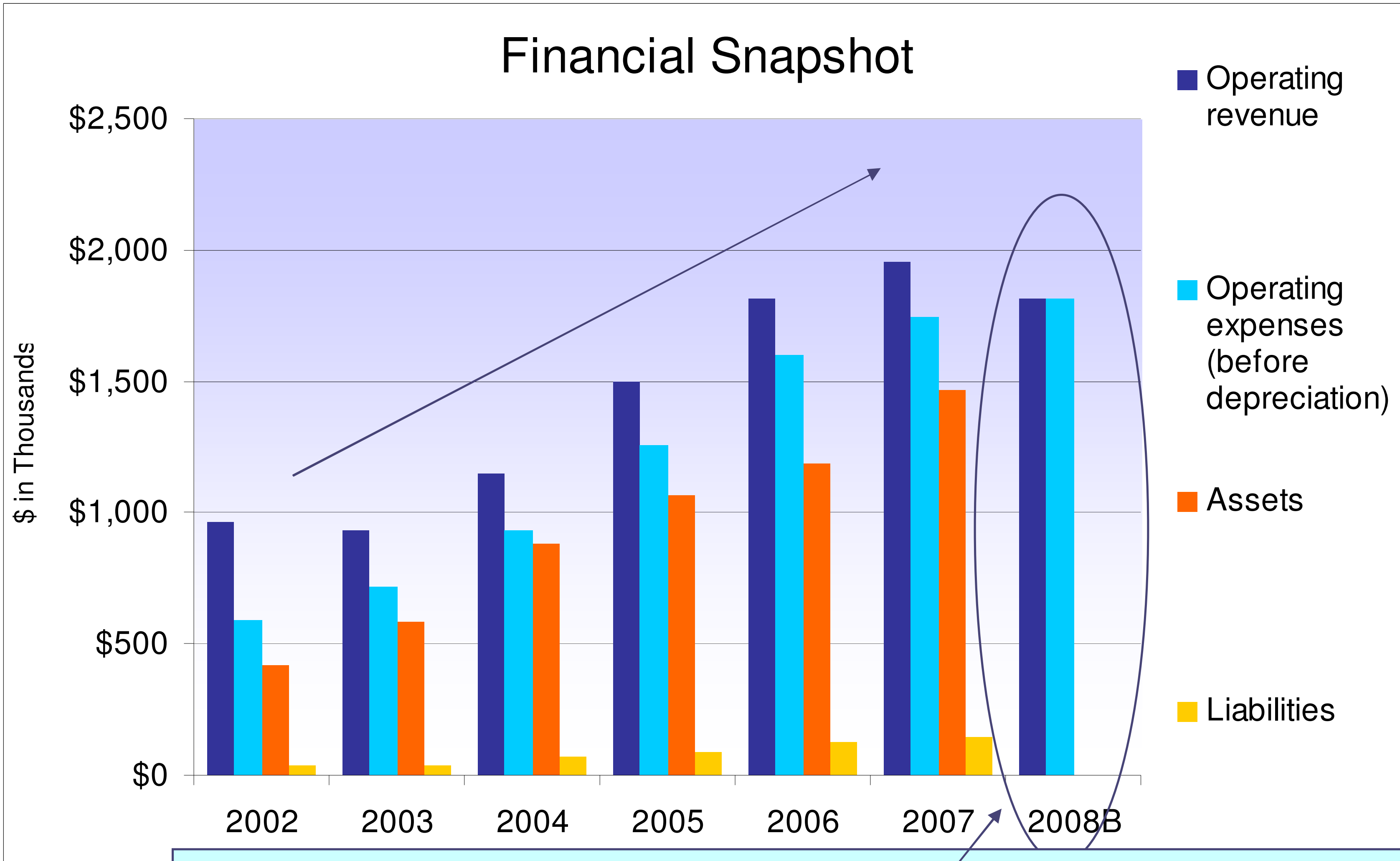
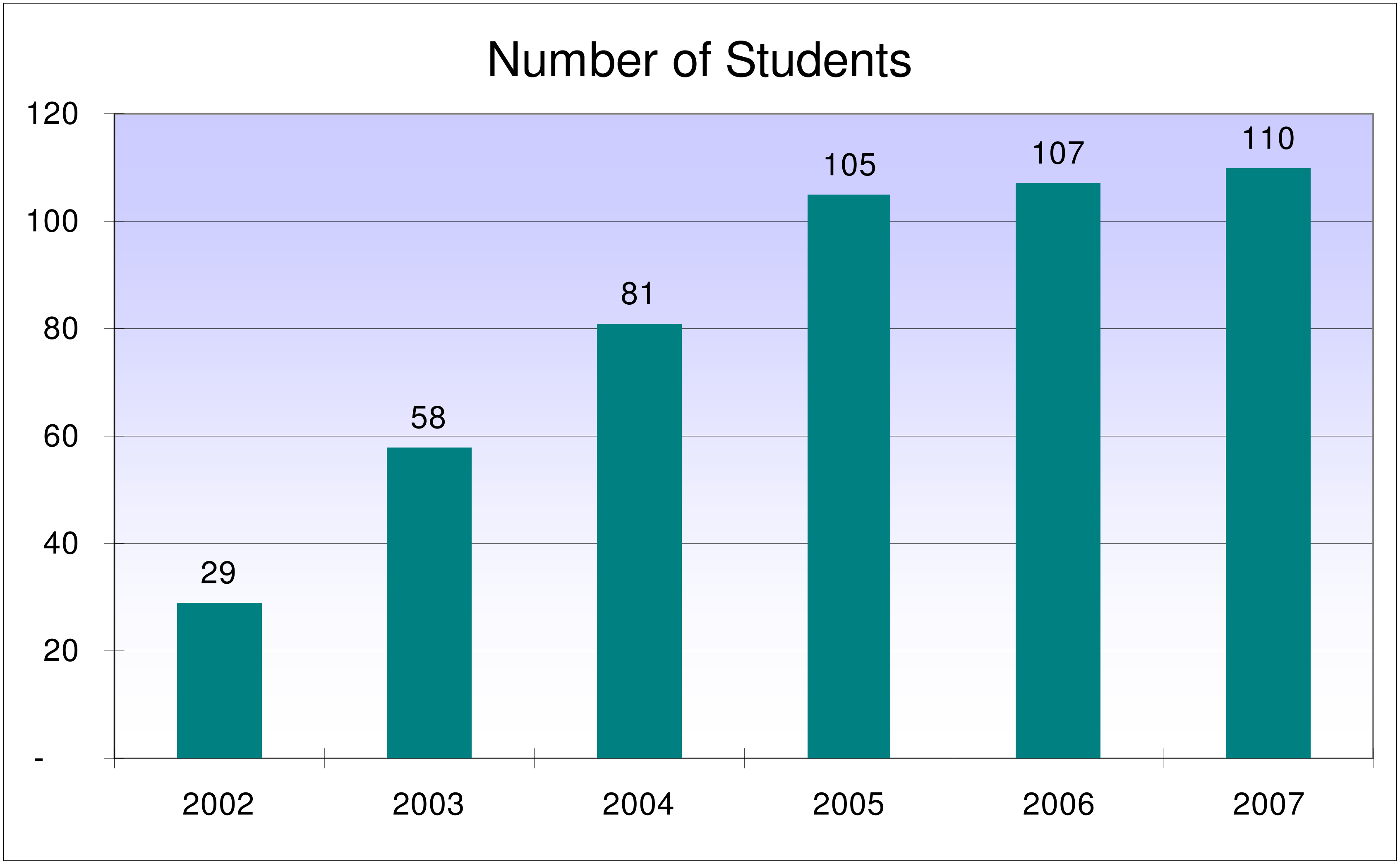
TOTAL REVENUE HAS MORE THAN DOUBLED SINCE THE SCHOOL OPENED IN FY02. FOR FY08, MANAGEMENT HAS BUDGETED CONSERVATIVELY, PROJECTING A $96,000 DEFICIT.



While leadership has budgeted a $96,000 deficit for FY08, the financial trend over the past six years indicates that leadership budgets conservatively but *manages* to a surplus.

FOR THE 2007 SCHOOL YEAR, CACS' STUDENT BODY WAS 110, JUST 10 SHY OF ITS CHARTER CAP. THE PROJECTION FOR 2008 IS 115.



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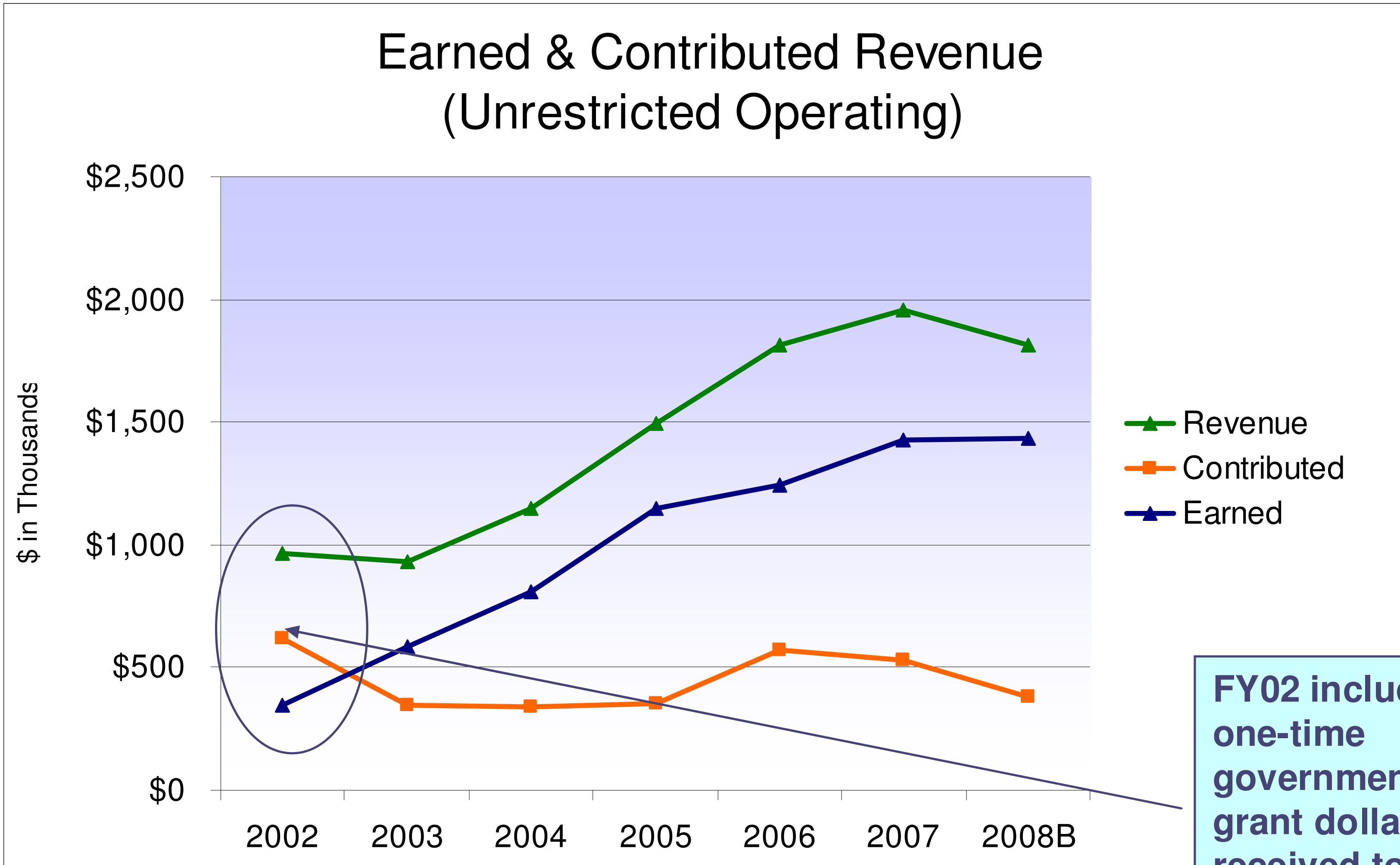
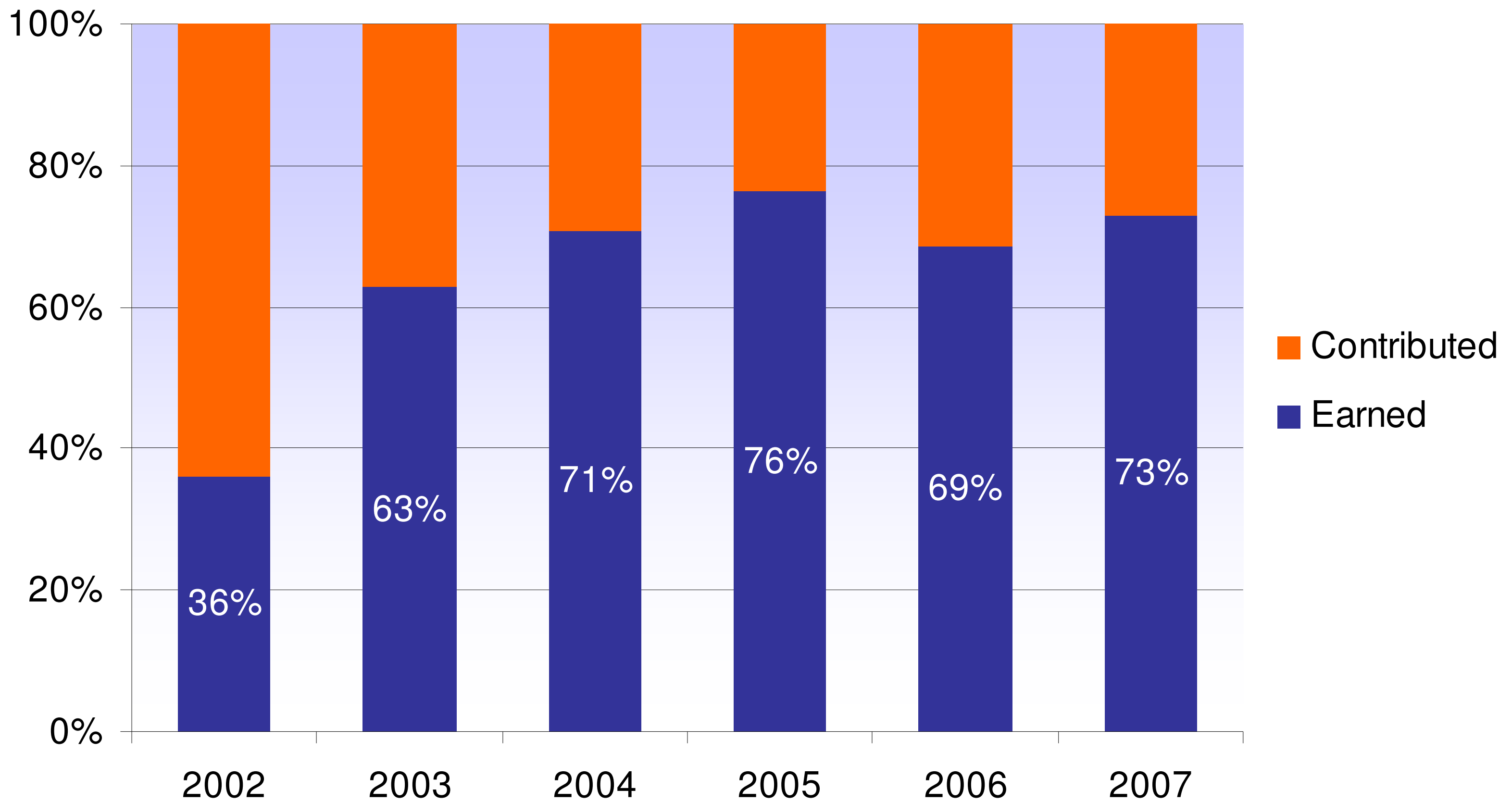
EARNED INCOME FROM TUITION IS PRIMARY DRIVER IN OVERALL REVENUE GROWTH. CONTRIBUTED INCOME HAS BEEN LARGELY FLAT.



FY02 includes one-time government grant dollars received to defray start up costs.

TUITION MAKES UP SLIGHTLY LESS THAN ¾ OF TOTAL REVENUE, MEANING THAT FOR EVERY DOLLAR CACS BRINGS IN FROM THE STATE, IT RAISES BETWEEN 30 AND 40 CENTS IN "SUBSIDY".

Unrestricted Operating Revenue Composition



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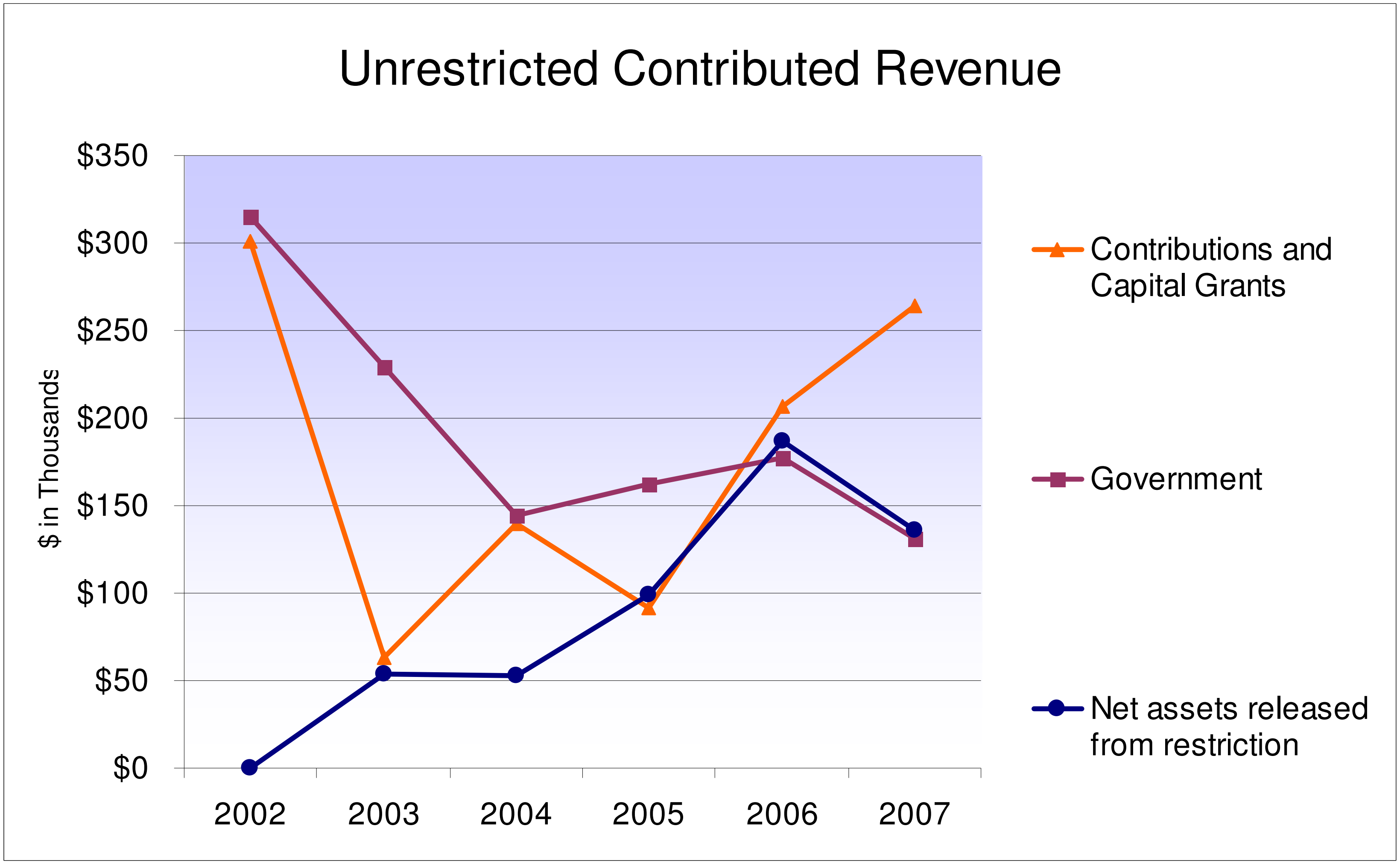
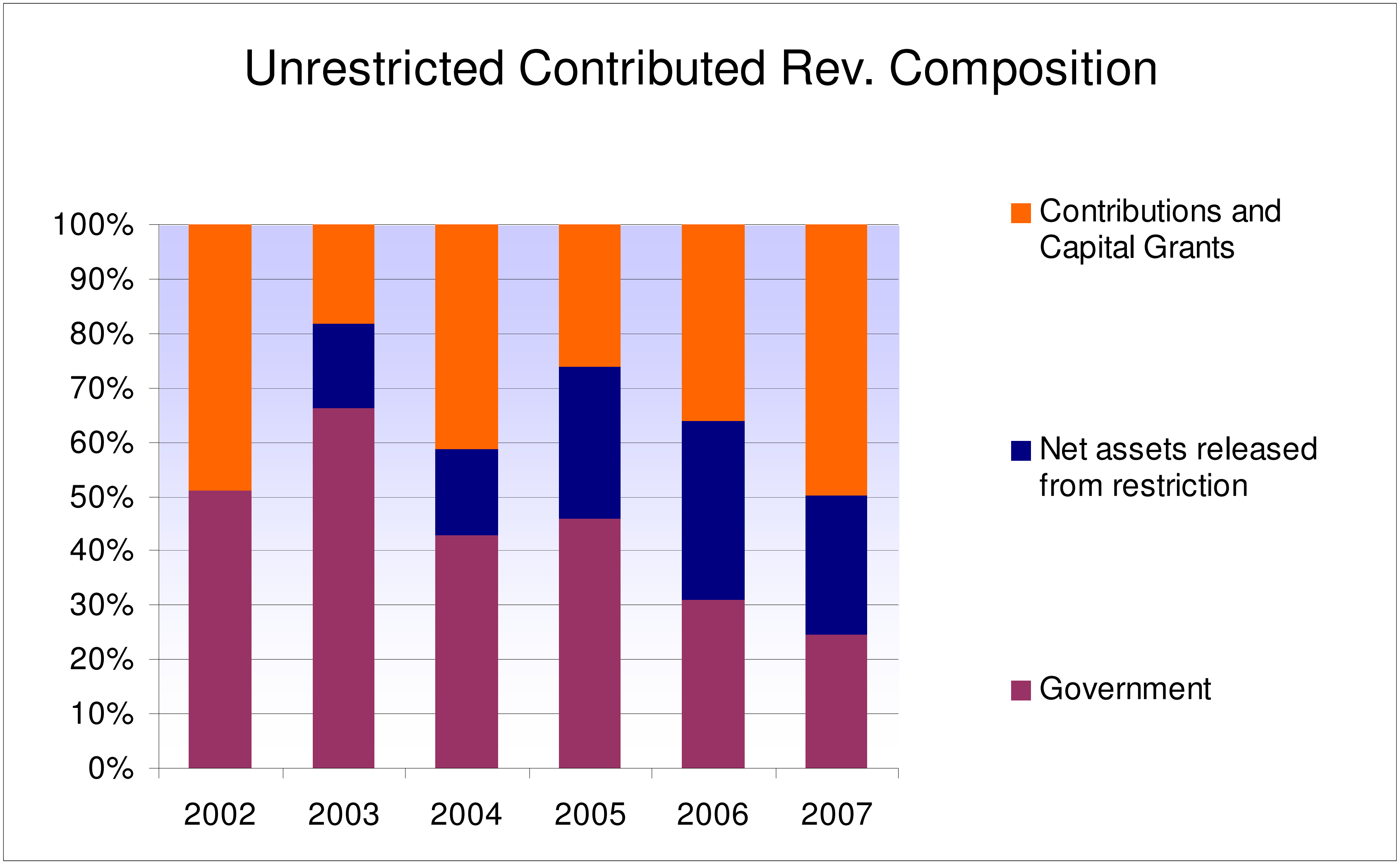
THE COMPOSITION OF RAISED FUNDS HAS CHANGED. MANAGEMENT FORECASTS GOVERNMENT FUNDING LEVELING OFF AT AROUND $100,000. CONCERTED EFFORT HAS GONE INTO INCREASING FOUNDATION GIFTS AND “ANNUAL FUND” CONTRIBUTIONS.



AS A PERCENTAGE, NON-GOVERNMENT CONTRIBUTIONS REPRESENTED AROUND 75% OF TOTAL RAISED DOLLARS IN FY07, COMPARED WITH ONLY 50% FIVE YEARS EARLIER.



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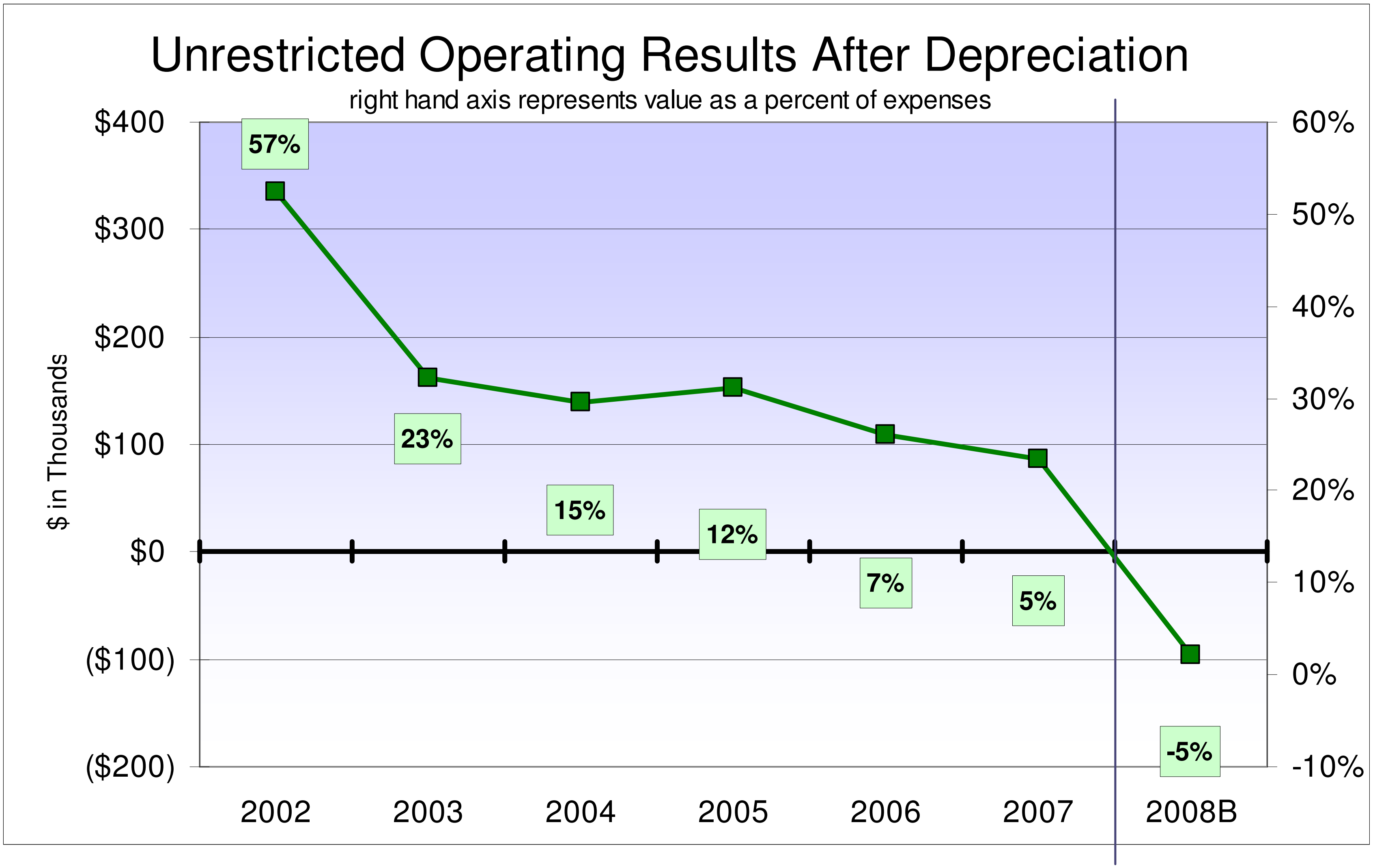
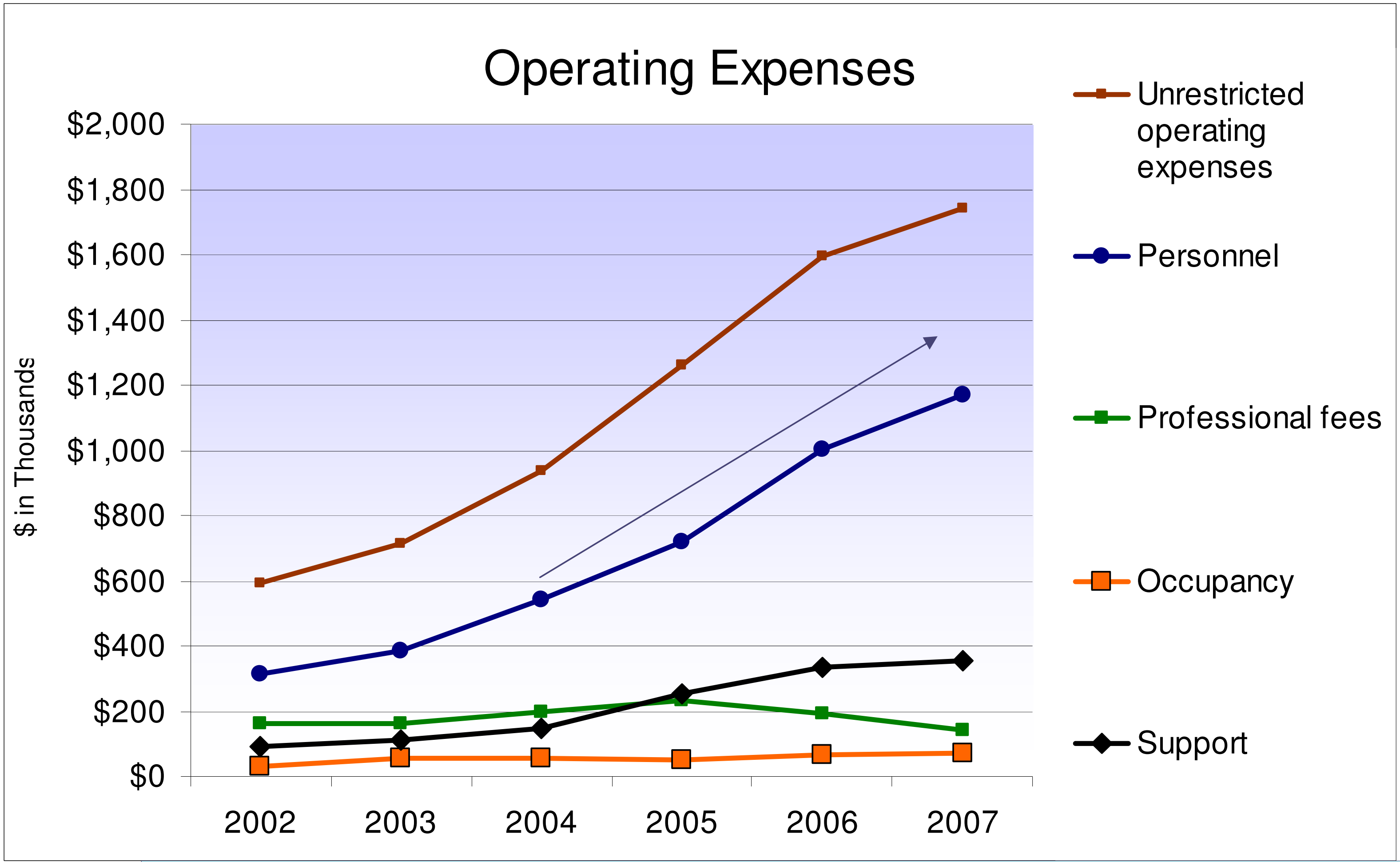
OPERATING SURPLUSES HAVE RANGED FROM 57% OF TOTAL EXPENSES IN CACS' FIRST YEAR OF OPERATION TO 5% IN THE MOST RECENT AUDITED YEAR.



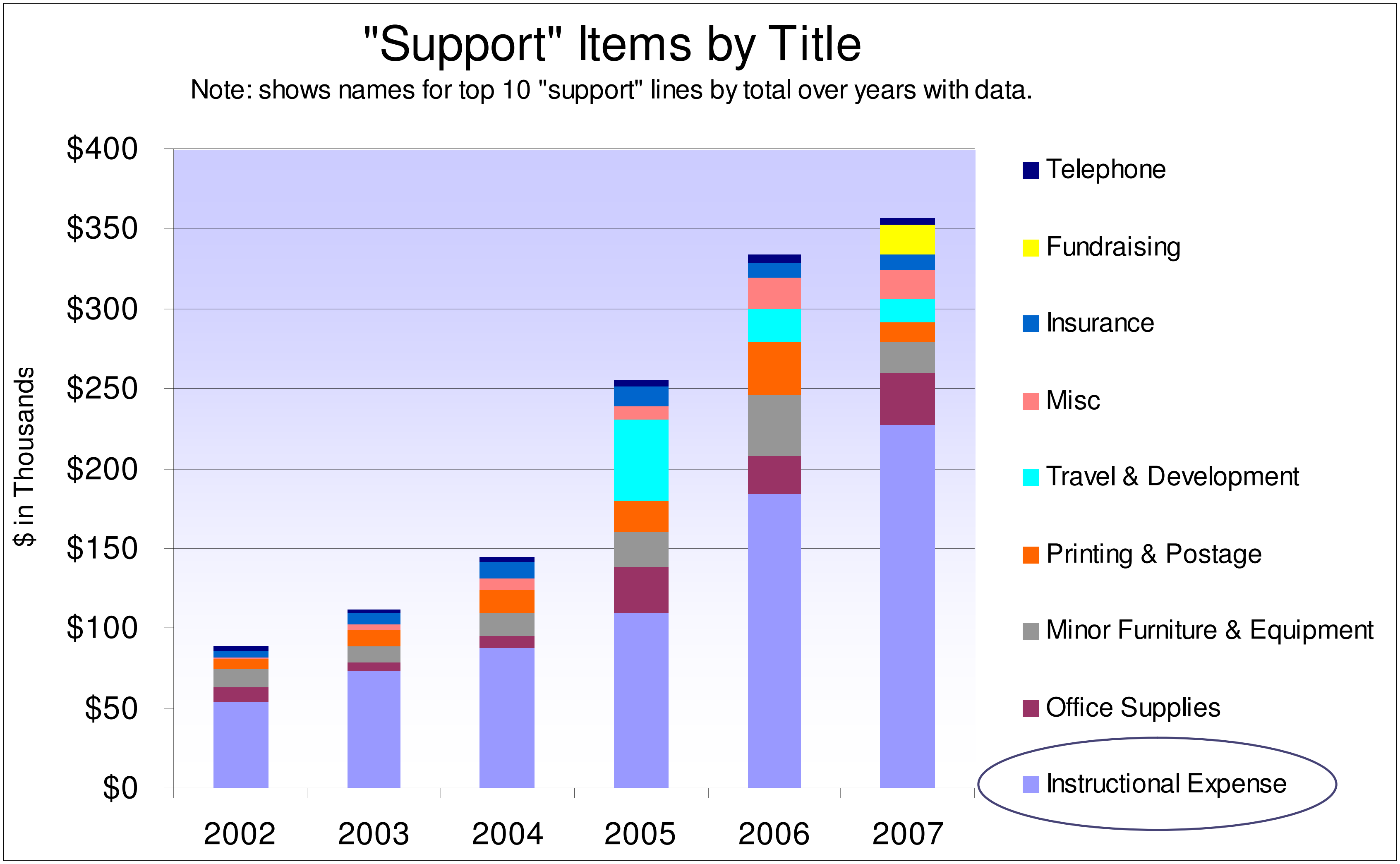
To arrive at CACS' bottom line, NFF has included all operating contributions but attempted to exclude capital grants that are one-time in nature.

AS CACS HAS RAMPED UP OVER THE PAST FIVE YEARS, EXPENSES HAVE GROWN EVEN FASTER THAN REVENUE. AS WITH VIRTUALLY ALL SOCIAL SECTOR ORGANIZATIONS, "PEOPLE" COSTS ARE THE PRIMARY DRIVER OF EXPENSES.



Management believes that the primary reason the school has not been able to realize more economies of scale as it has grown, is that it has had to cover increasing costs in special education without any additional tuition from the State. This is seen in the steep growth curve in personnel.

PROGRAM OR “SUPPORT” COSTS HAVE ALSO GROWN. WHILE CLEARLY VARIABLE, INSTRUCTIONAL EXPENSE, RELATES TO EXPEDITIONARY LEARNING ACTIVITIES (HUNTINGTON, BMOP ETC.) AND IS CORE TO CACS’ MISSION AND PHILOSOPHY.



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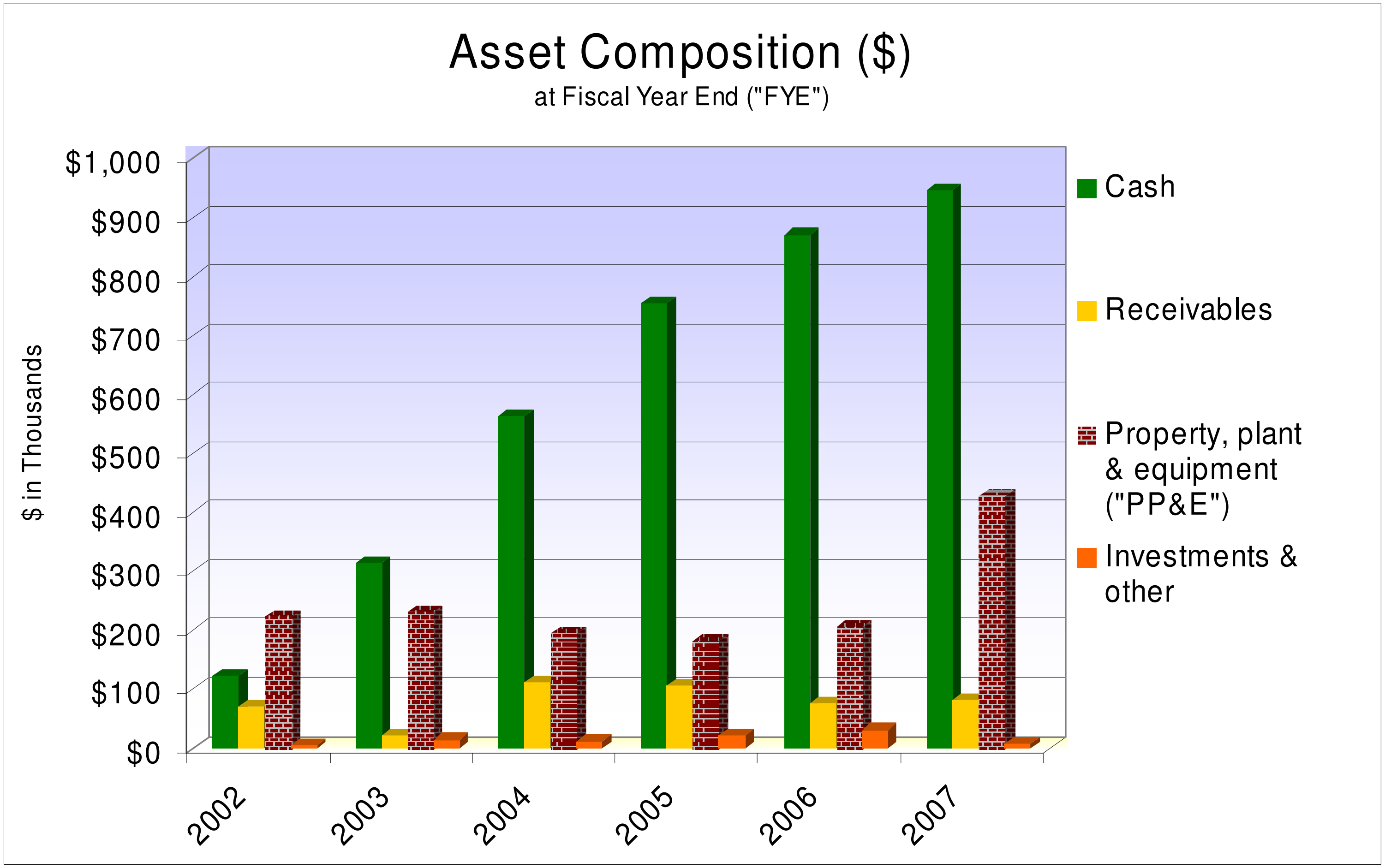
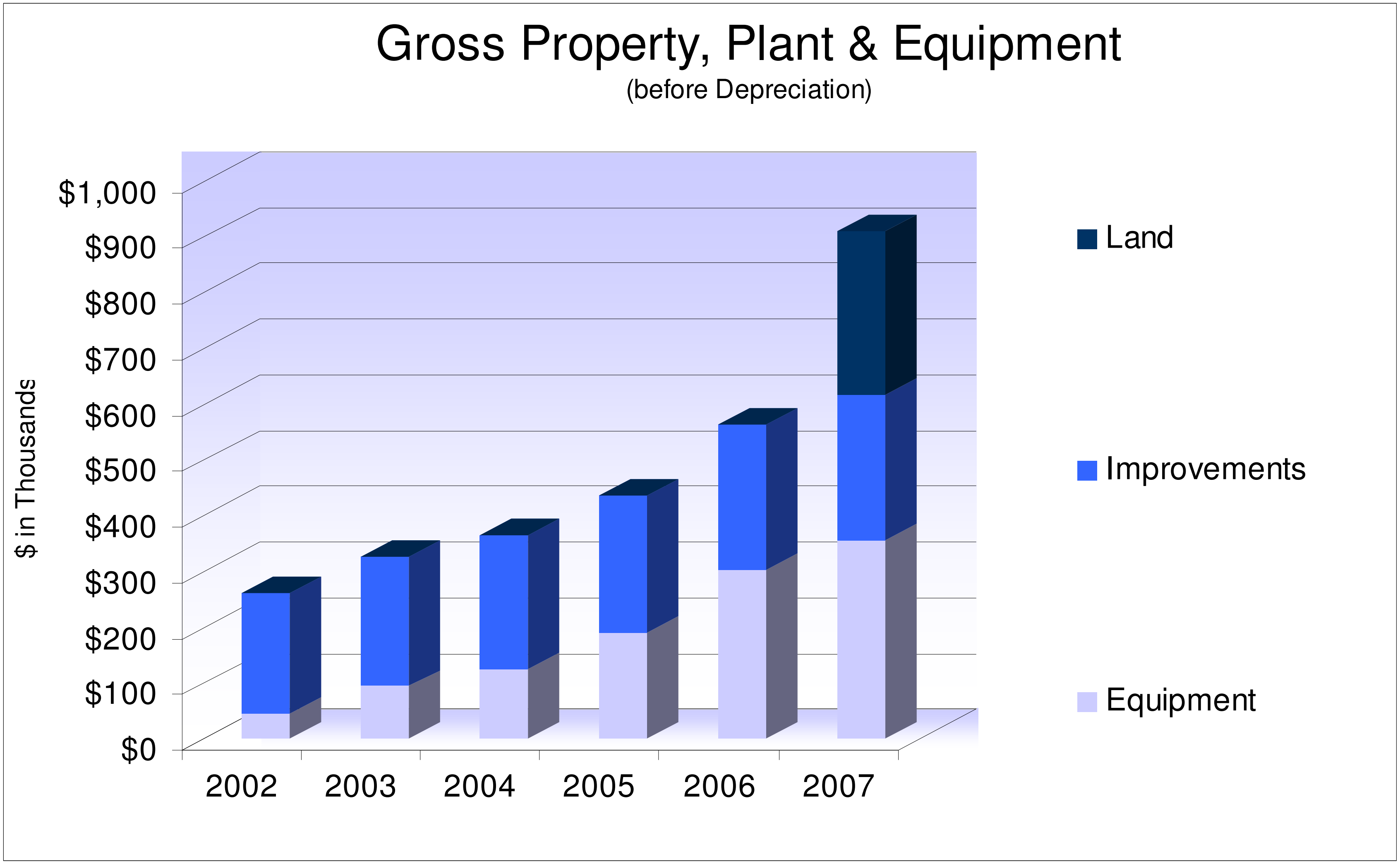
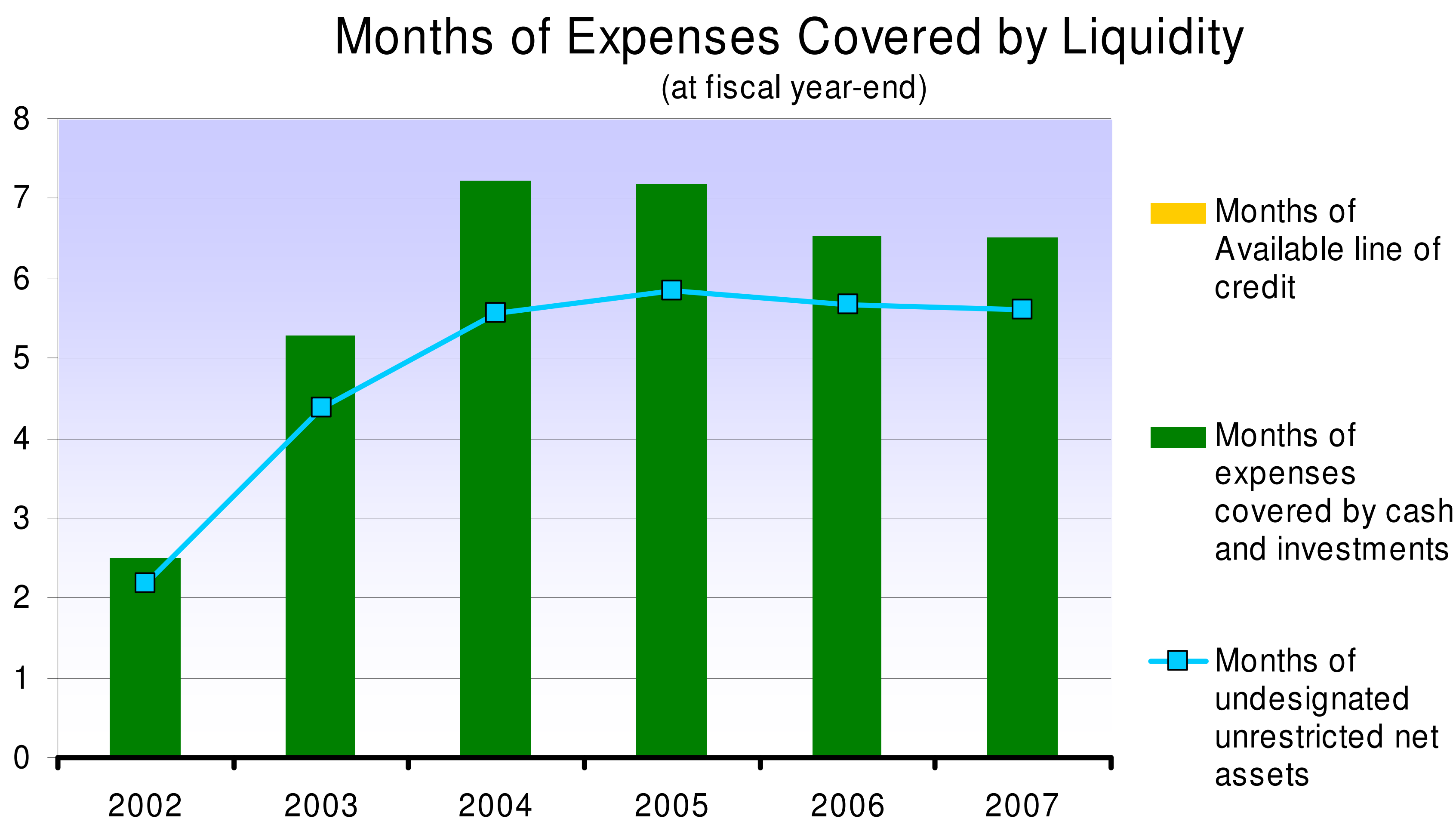
GROWTH ON THE BALANCE SHEET HAS TAKEN PLACE ALMOST ENTIRELY IN CASH.



GROWTH IN FIXED ASSETS HAS BEEN MODEST EXCEPT IN FY2007 WHEN CACS INVESTED ALMOST $300,000 IN THE SITE FOR THE SCHOOL'S EXPANSION.



AT FYE07, CACS HAD OVER SIX MONTHS IN CASH AND INVESTMENTS. "LIQUID" NET ASSETS WERE SIMILARLY STRONG.



NFF sometimes measures liquidity by how much of net assets are liquid and therefore potentially available to management. By this measure, as well as by the more conventional months of cash, CACS has good liquidity, indicating it could weather a short-term crisis if it had to.

Future Considerations

SUMMARY

NFF defines facility project success as <u>not only getting a building built but also having a financially healthy organization for years after the project's completion</u>.

Before embarking on its planned facility project, NFF encourages CACS to plan for potential financial and organizational implications by considering the following:

1. Financial preparedness
2. Manage to "full cost" of business
3. Conservative project projections and "Plan B"
4. Further investment in fundraising capacity
    a) Annual subsidy requirements
    b) Idea of comprehensive capital campaign
5. Appropriateness of board-designating cash

1. ASSESS FINANCIAL PREPAREDNESS

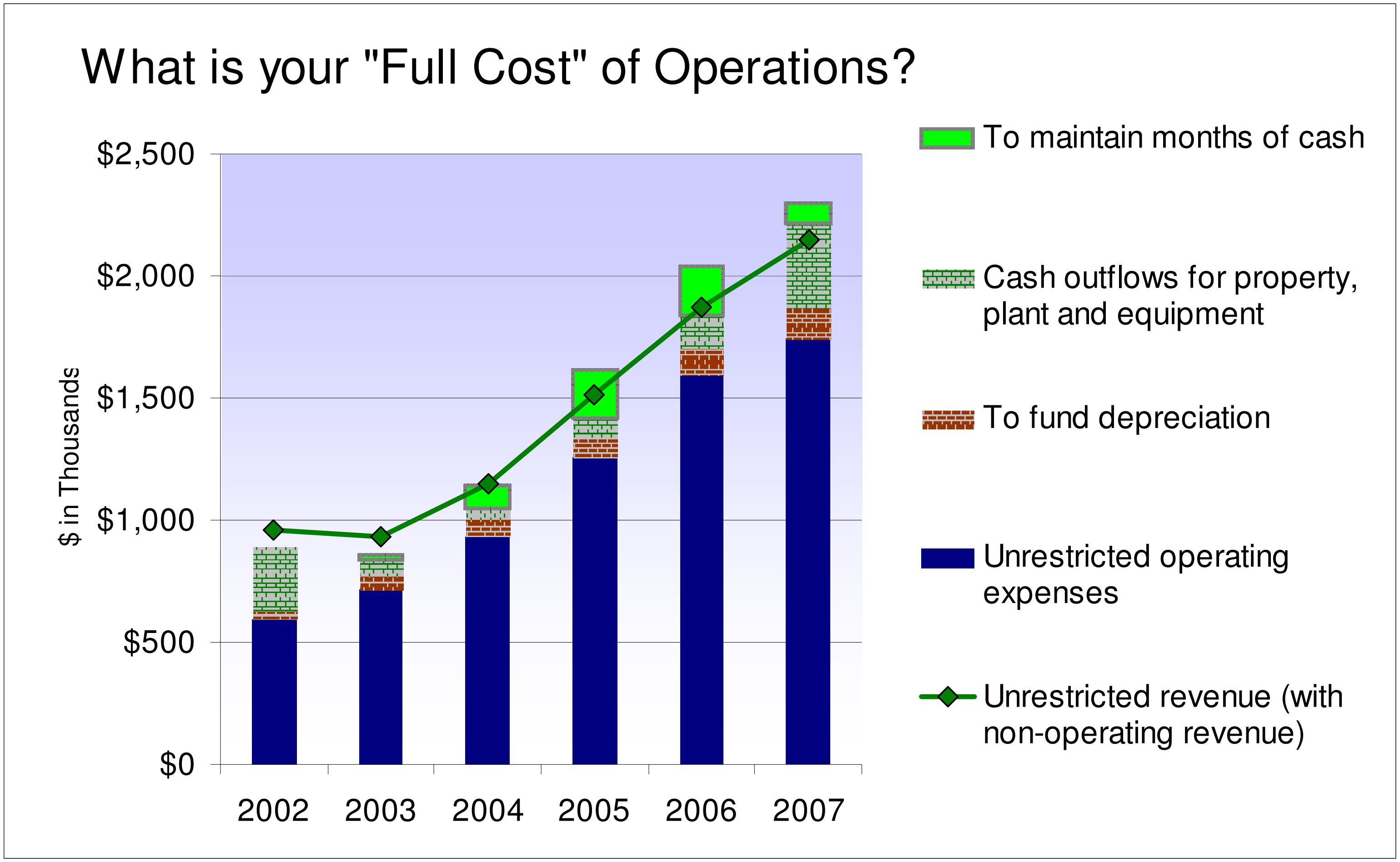
NFF encourages its clients to assess their financial readiness to execute a facility project smoothly. As a first exercise, we urge management to identify and look out for the following common warning signs:

1. History of declining operating results or deficits
2. Major sources of funding that are instable/insecure
3. Unrestricted net assets and cash that are close to zero and leave no "cushion" or reserve for setbacks/deficits
4. History of cash flow problems
5. Difficulty meeting payroll and paying bills promptly
6. Difficulty in predicting (and having the record keeping/reporting systems in place to assess) how the year will end financially
7. Trouble understanding and explaining audit

Based on the preceding analysis of CACS finances, the organization does not appear to display any of these warning signs.

2. MANAGE TO FULL COST OF BUSINESS.

CACS HAS DONE AN EXCELLENT JOB OF COVERING FULL COSTS AND GENERATING CASH TO INVEST IN OPERATIONS AND PROVIDE CUSHION FOR THE UNFORESEEN. NFF ENCOURAGES LEADERSHIP TO CONTINUE TO EMBRACE THIS DISCIPLINE POST-PROJECT.



3. PREPARE A CONSERVATIVE PROJECT BUDGET

As it prepares its project budget, CACS leadership may want to contemplate the following scenarios and to consider how the organization might mitigate the potential risks that they pose:

1) Cost overruns:

- In NFF's experience, the all-inclusive costs for a capital project (including soft costs, staff down-time, relocation costs, interest expense, etc.) can easily run substantially higher than originally estimated.
- NFF generally recommends a 15% contingency.

2) Operational impact:

- It is also our experience that, after a project, an organization's operating budget can take a hit of as much as 10% due to one or more of the following:
  - Lower revenue from contributions because donors give to capital campaign
  - Lower earned revenue due to curtailed programming as staff focuses on project
  - Additional staff needed while current staff implements project

3. REMEMBER PLAN B

- A project of the scale and scope CACS is considering requires extensive organizational and financial planning. NFF encourages the organization's staff and board to assess collectively all options with respect to the development and usage of the space, as well as the timing of construction.

- Many organizations run into trouble when they try to take too large a step or take a step too soon. In order to determine the scope of the project, assess how much of a facility change the organization can sustain without making drastic changes in programming.

- ***Having alternatives or a contingency plan will help reduce risk.***

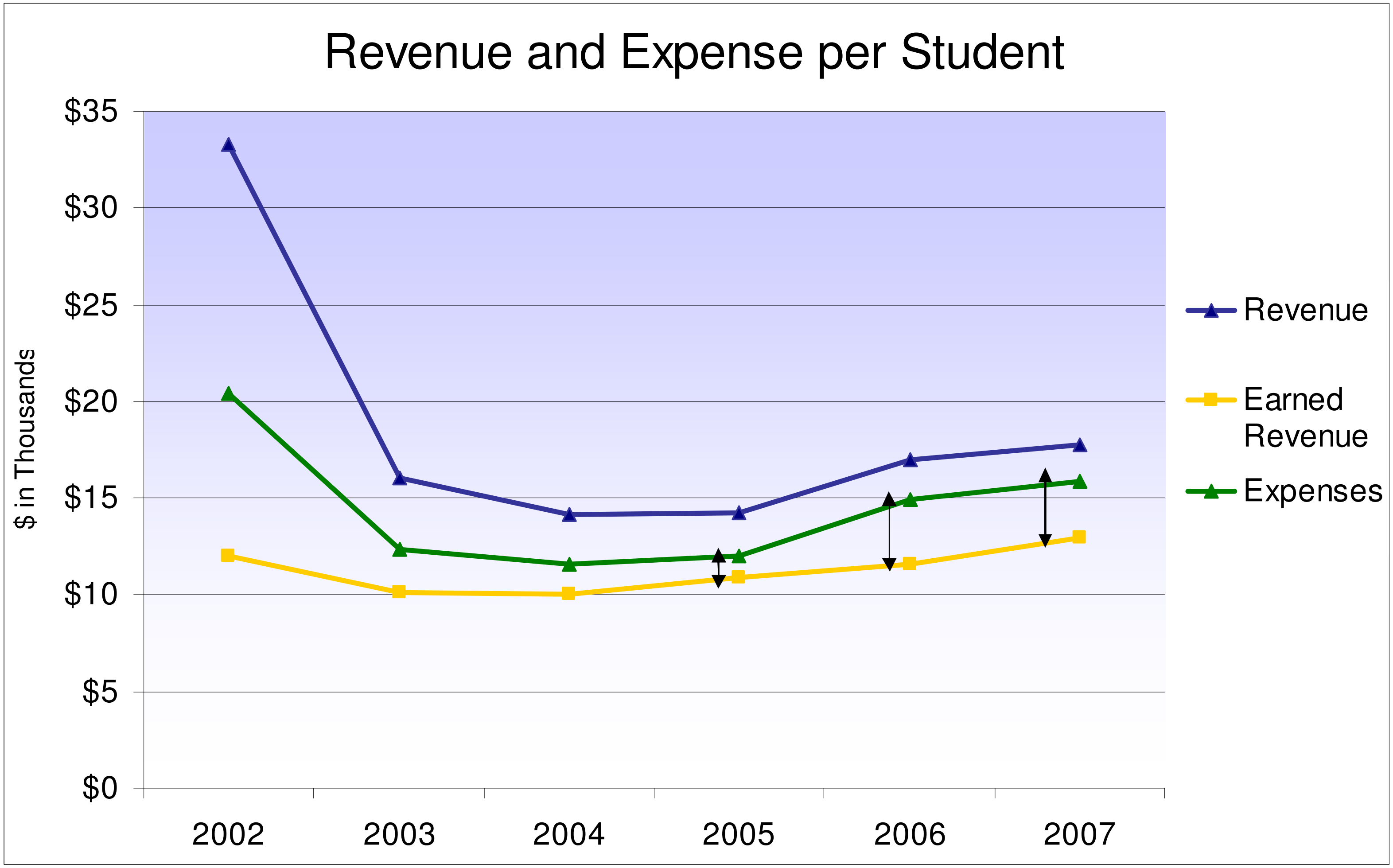
- ***It is always better to postpone a project than to proceed with unmanageable risks.***

4. FURTHER INVESTMENT IN FUNDRAISING CAPACITY

- As we spoke about during our face to face meeting, an important aspect to future success will rest on CACS' mindful balancing of project and annual fundraising.

- For many nonprofits, a capital campaign can represent an opportunity to enhance significantly its organizational fundraising culture. As organizations grow, the executive director can no longer shoulder sole responsibility and investing in fundraising departments as well and increasing the fundraising capacity of the board becomes more and more important. As such, CACS may want to think about the following:
  - What additional investments in the development department (staff, or consultants if full-time support is not economically feasible) may be necessary to provide more reliable and diverse contributed revenue?
  - How can CACS expand its early efforts to cultivate individuals through annual appeals, marketing, board development, etc.?
    - Please note that in NFF's experience, foundations often serve to seed the growth of new programs but become a lesser source of support once an organization matures.
    - Financial support from 100% of the Board can send a powerful message to potential funders about Board members' commitment to the organization.
    - The organization may also want to consider cultivating new Board members who can contribute or attract greater financial resources

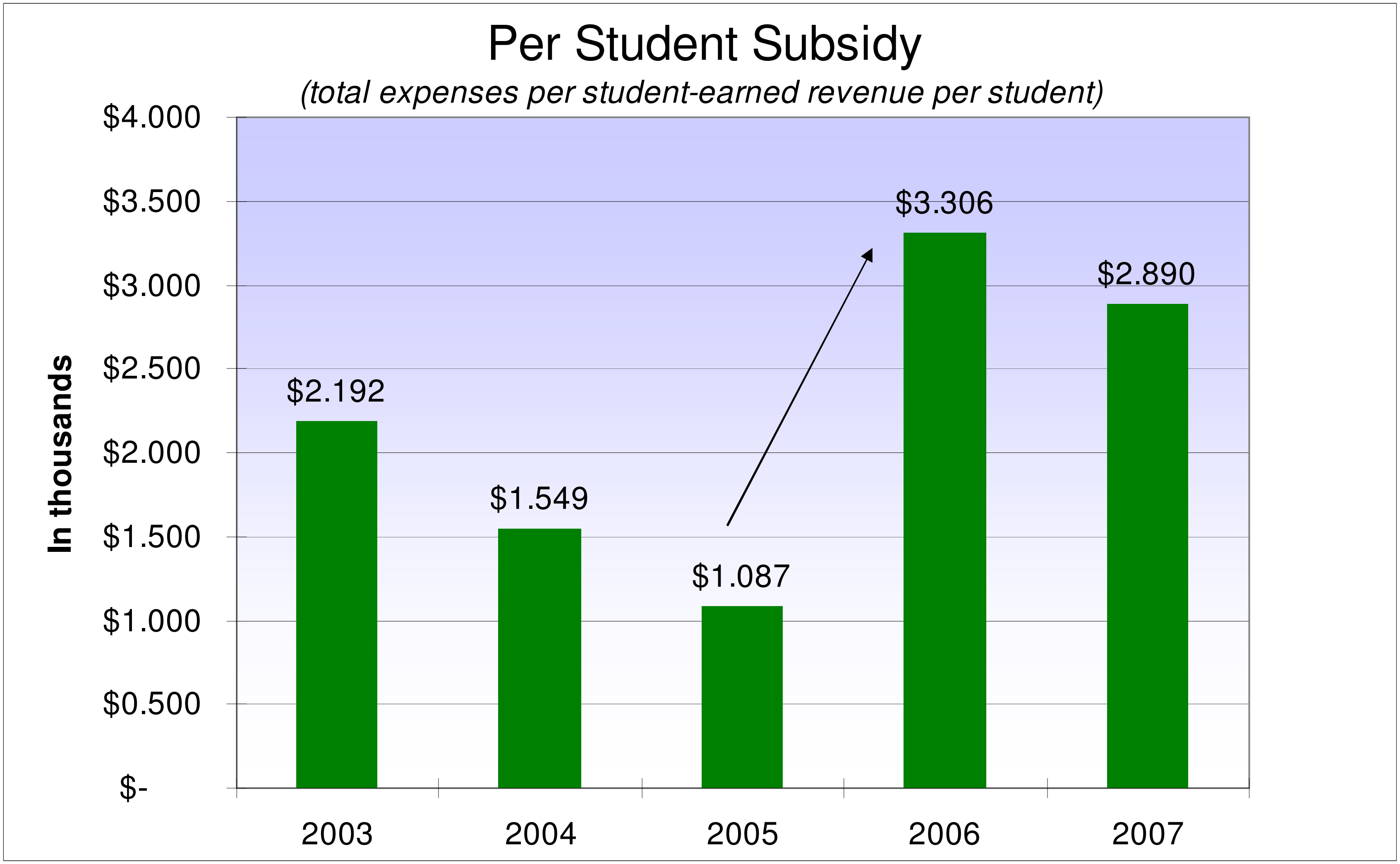
<u>4. FURTHER INVESTMENT IN FUNDRAISING: ANNUAL SUBSIDY</u>
IN ADDITION TO PROJECT FINANCING, FUNDRAISING INCOME WILL LIKELY HAVE TO OFFSET INCREASED PROGRAM COSTS, E.G THOSE RELATED TO SERVING STUDENTS WITH SPECIAL NEEDS.



FY06 and 07 show that per student expenses have grown faster than per student earned revenue.

4. FURTHER INVESTMENT IN FUNDRAISING: ANNUAL SUBSIDY

AFTER ACHIEVING CERTAIN ECONOMIES OF SCALE IN THE EARLY YEARS, CACS IS FACING A GROWING "SUBSIDY" GAP PER STUDENT.



4. FURTHER INVESTMENT IN FUNDRAISING: EXPLORE IDEA OF COMPREHENSIVE CAPITAL CAMPAIGN

Increasingly, NFF works with clients that look to off set some of the risk inherent in a large capital project by thinking about their capital campaign more comprehensively.

- For example, CACS could choose to increase its capital campaign goal to incorporate some or all of the following:
  - A larger contingency
  - The potential one-time impact on operations (lost income or new expenses)
  - Financing fees and interest during project and principal payments post project
  - Any deficit that could occur post-project until operating revenue catches up with expanded operating expenses (i.e. growth capital to cover necessary investments in staff, infrastructure, etc.).
  - Board-designated cash reserve for program investments, facility needs, rainy days, etc.

- The board and management have collective responsibility for achieving the capital campaign goal.
  - Continuously monitor progress of campaign goals against plan and be proactive about implementing a Plan B if goals are not met.

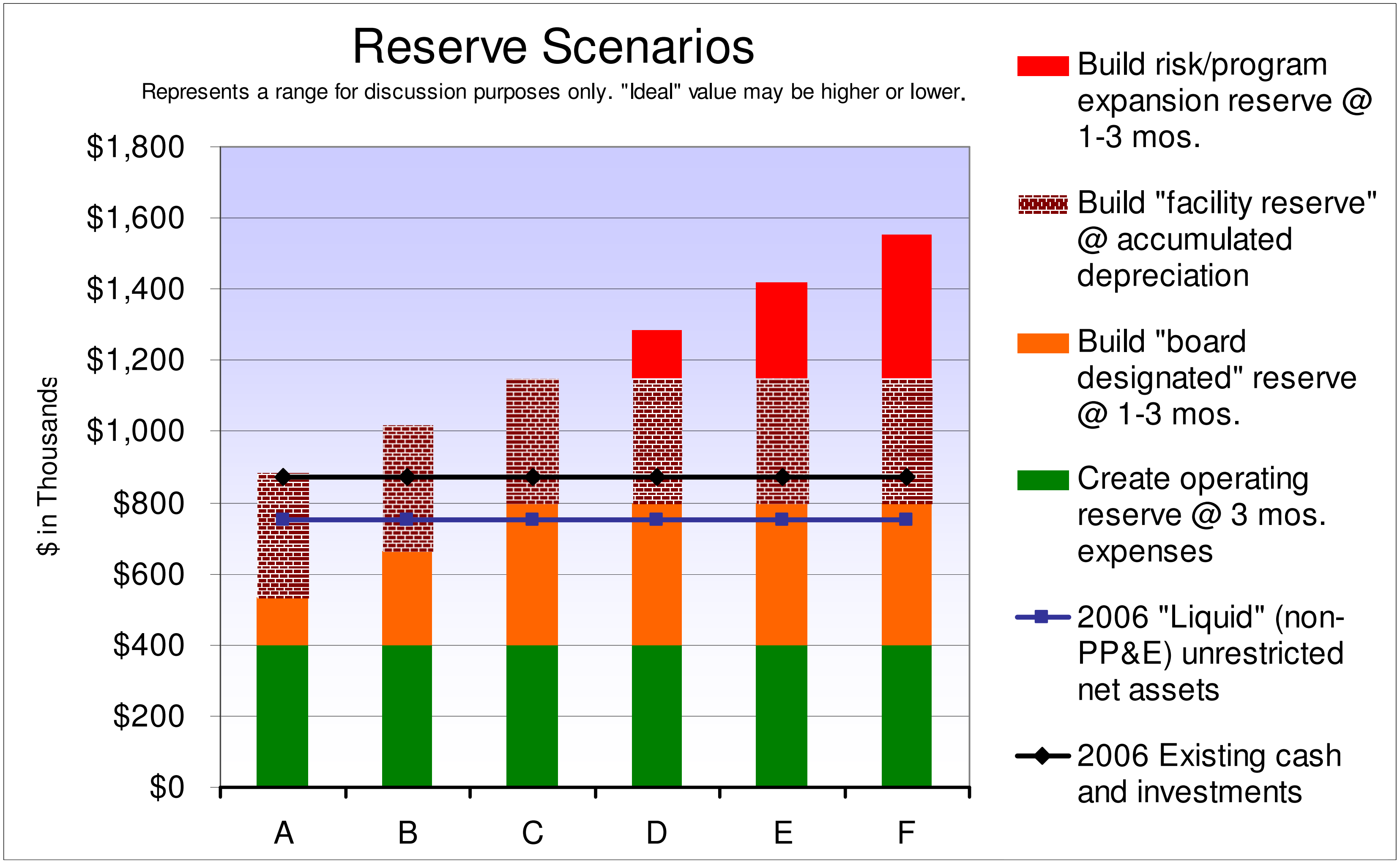
5. APPROPRIATENESS OF BOARD DESIGNATING CASH

- Board designated reserves are useful as funds are monitored but not rigidly restricted; allowing the organization to an unexpected event.
  - In NFF's view, a permanently restricted endowment should only be actively built if a nonprofit has **excess** fundraising capacity.

- Some reserves that may be appropriate for the organization, in light of its infrastructure needs and growth plans, include:
  - An internal line of credit reserve to bridge funding delays
  - An infrastructure reserve for future facility/equipment needs, initial investment in new administrative staff, etc
  - An "opportunity" or program-enhancement reserve
  - A long-term investment reserve

- The "appropriate" reserve type and size are uniquely specific to each organization's individual needs and goals, and risk tolerance
  - Draft language for a board designated reserve policy is provided in this report in Appendix G.

5. APPROPRIATENESS OF BOARD DESIGNATING CASH
BELOW ARE A VARIETY OF RESERVE SCENARIOS AS A WAY TO HELP CACS FRAME A POTENTIAL CONVERSATION WITH THE BOARD ABOUT DESIGNATING SOME OF ITS CASH



APPENDICES

A: Statement of Financial Position
B: Statement of Activities
C: Statement of Cash Flows
D: NFF Triangle
E: NFF Conventions
F: Report Methodology
G: Board Designated Reserves

APPENDIX A – STMTS OF FINANCIAL POSITION

Dollars in thousands
12/19/07 10:00 AM

	Audit Jun-30 2002	Audit Jun-30 2003	Audit Jun-30 2004	Audit Jun-30 2005	Audit Jun-30 2006	Draft Audit Jun-30 2007
	$ 000	$ 000	$ 000	$ 000	$ 000	$ 000
ASSETS						
Cash and equivalents *	123	314	564	754	871	946
Grants and pledges receivable	70	22	112	81	51	81
Accounts receivable	-	-	-	-	-	-
Other current assets	4	14	12	21	31	9
Total current assets	196	351	687	856	952	1,035
Other long-term investment	-	-	-	-	-	-
Grants and pledges receivable	-	-	-	25	25	-
Net fixed assets (property, plant & equipment)	224	231	197	183	208	428
Other long-term assets	-	-	-	-	-	-
Total long-term assets	224	231	197	208	233	428
Total Assets	420	582	885	1,064	1,186	1,464
LIABILITIES						
Accounts payable	12	1	18	40	66	67
Accrued salaries & benefits	24	36	53	52	64	81
Other current liabilities	-	-	-	-	-	-
Deferred revenue	-	-	-	-	-	-
Short-term debt (incl current portion of LT debt)	-	-	-	-	-	-
Total current liabilities	36	37	71	92	130	148
Long-term debt	-	-	-	-	-	-
Other long-term liabilities	-	-	-	-	-	-
Total long-term liabilities	-	-	-	-	-	-
Total Liabilities	36	37	71	92	130	148
NET ASSETS						
Undesignated	107	261	433	613	753	813
Board designated	-	-	-	-	-	-
Unrestricted - property, plant & equipment	224	231	197	183	208	428
Total unrestricted net assets	331	492	631	796	962	1,241
Temporarily_restricted	53	53	183	176	94	75
Permanently_restricted	-	-	-	-	-	-
Total Net Assets	384	545	814	972	1,056	1,316
Total Liabilities and Net Assets	420	582	885	1,064	1,186	1,464

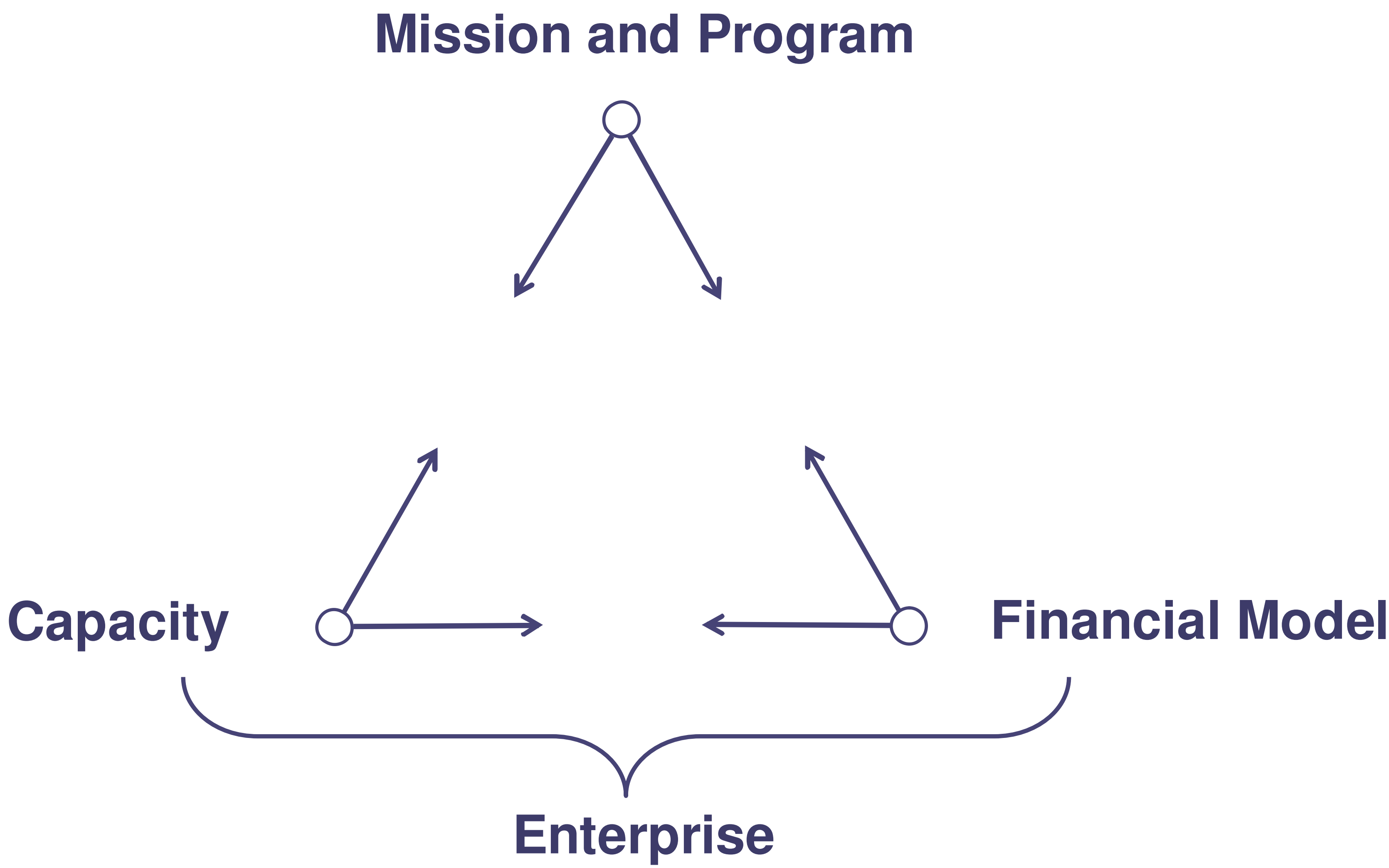
APPENDIX B – STATEMENTS OF ACTIVITIES

Dollars in thousands 12/19/07 11:30 AM	Audit Jun-30 2002	Audit Jun-30 2003	Audit Jun-30 2004	Audit Jun-30 2005	Audit Jun-30 2006	Draft Audit Jun-30 2007	Budget Jun-30 2008B
	$ 000	$ 000	$ 000	$ 000	$ 000	$ 000	$ 000
Unrestricted Operating Revenue							
Earned revenue							
Investment income	1	3	7	14	33	49	15
Government_earned	-	-	-	-	-	-	-
Program	347	584	804	1,131	1,210	1,375	1,421
Other earned	-	-	-	-	-	-	-
Earned operating revenue	348	587	810	1,145	1,243	1,424	1,436
Contributed revenue							
Trustees and Individuals	-	-	-	-	-	-	-
Contributions and Capital Grants	301	63	139	92	207	264	280
Government	315	229	144	162	177	131	100
Special events (before related expenses)	-	-	-	-	-	-	-
Net assets released from restriction	-	53	53	99	186	136	-
Pass-through (operations)	-	-	-	-	-	-	-
Contributed operating revenue	616	345	336	353	571	531	380
Unrestricted operating revenue	964	932	1,147	1,498	1,814	1,956	1,816
Unrestricted Operating Expenses							
Personnel	313	384	540	718	1,004	1,172	1,308
Professional_fees	161	163	196	234	193	142	20
Occupancy	29	56	55	52	66	71	71
Support	89	112	144	256	334	357	414
Interest	-	-	-	-	-	-	-
Pass_through_operating_expense	-	-	-	-	-	-	-
Unrestricted operating expenses	592	714	936	1,259	1,597	1,742	1,812
Unrestricted operating surplus/(deficit)	372	218	211	238	217	214	4
Depreciation	38	57	72	86	107	127	100
Unrestricted operating surplus/(deficit) after depreciation	335	161	139	152	110	86	(96)
Temporarily Restricted Assets							
Temporarily restricted assets received	53	53	183	105	160	310	-
Temporarily restricted assets released	4	(53)	(53)	(112)	(242)	(329)	-
Unrealized net gain (loss) on investment	-	-	-	-	-	-	-
Realized net gain (loss) on investment	-	-	-	-	-	-	-
Increase (decrease) in temporarily restricted net assets	57	(0)	130	(7)	(82)	(19)	-
Change after temporarily restricted activities	392	161	269	145	28	68	(96)
Unrestricted Non-Operating Activities							
Unrealized net gain (loss) on investment	-	-	-	-	-	-	-
Realized net gain (loss) on investment	-	-	-	-	-	-	-
Net gain (loss) on disposition of assets	-	-	-	-	-	-	-
Total non-operating revenue	(4)	-	-	14	55	193	-
Total unrestricted non-operating expenses	-	-	-	-	-	-	-
Net increase (decrease) from in-kind capital contributions	-	-	-	-	-	-	-
Change in net assets from unrestricted non-operating activities	(4)	-	-	14	55	193	-
Change after non-operating activities	388	161	269	158	83	260	(96)
Change in net assets	388	161	269	158	83	260	(96)

APPENDIX C – STATEMENTS OF CASH FLOWS

Dollars in thousands	Audit	Audit	Audit	Audit	Draft Audit
12/19/07 4:15 PM	Jun-30	Jun-30	Jun-30	Jun-30	Jun-30
	2003	2004	2005	2006	2007
Cash Flow from Operating Activities					
Net assets	161	269	158	83	260
Depreciation	57	72	86	107	127
Net increase (decrease) from restatement(s)	-	-	-	-	-
Net increase (decrease) from in-kind capital contributions	-	-	-	-	-
Other permanently restricted net assets	-	-	-	-	-
Total non-operating revenue	-	-	(14)	(55)	(193)
Total non-operating expenses	-	-	-	-	-
Unrealized net loss (gain) on investment	-	-	-	-	-
Realized net loss (gain) on investment	-	-	-	-	-
Disposition of assets	-	-	-	-	-
Operations before depreciation (with temporary restricted revenue)	218	341	231	135	195
(Increase)/decrease in operating assets:					
Grants and pledges receivable	48	(90)	6	30	(5)
Accounts receivable	-	-	-	-	-
Other current assets	(11)	3	(10)	(9)	22
Increase (decrease) in operating liabilities:					
Accounts payable	(11)	17	22	26	1
Accrued salaries & benefits	12	16	(1)	12	17
Deferred revenue	-	-	-	-	-
Other current liabilities	-	-	-	-	-
Change in operating assets & liabilities	38	(54)	17	59	35
Net cash provided (used) in operating activities	256	288	248	194	229
Cash Flow from Investing Activities					
(Increase)/decrease in:					
Net fixed assets (property, plant & equipment) after depreciation	(64)	(39)	(72)	(132)	(347)
Other long-term assets	-	-	-	-	-
Investments after sale/write down (purchase/write up)	-	-	-	-	-
Net cash provided (used) in investing activities	(64)	(39)	(72)	(132)	(347)
Cash Flow from Financing Activities					
Increase (decrease) in:					
Other permanently restricted funds	-	-	-	-	-
Total non-operating revenue	-	-	14	55	193
Total non-operating expenses	-	-	-	-	-
Net change (decrease)/increase					
Other long-term liabilities	-	-	-	-	-
Funded Debt	-	-	-	-	-
Net cash provided (used) by financing activities	-	-	14	55	193
Net increase (decrease) from restatement(s)	-	-	-	-	-
Net increase (decrease) in cash	191	249	190	117	75
Cash at beginning of year	123	314	564	754	871
Cash at end of year	314	564	754	871	946

APPENDIX D: THE NFF TRIANGLE



APPENDIX E: FINANCIAL ANALYSIS CONVENTIONS

Unrestricted operating activities reflect the organization's true year-over-year financial performance. Using readily available information from our client, NFF focuses its analysis on:

- Unrestricted grants & earned revenue;
- Net assets released from restriction for operations;
- Operating expenses: staff, occupancy, consultants, etc.; and
- Before and after depreciation expenses.

– Our analysis does **not** include in operations:
  - Pass-through funding or expenses (e.g., re-grant program);
  - In-kind revenue and expenses (e.g., donated legal services);
  - Temporarily restricted receipts;
  - Permanently restricted receipts (e.g., endowment);
  - Funds received for a capital campaign;
  - Net assets released from restriction for capital expenditures; or
  - Realized and unrealized gains and losses on investments.

Key Term: "Undesignated Unrestricted Net Assets" or "Liquid Net Assets" represent NFF's estimated amount of unrestricted net assets NOT invested in PP&E. Theoretically this is the liquid amount of unrestricted net assets available for operations.

APPENDIX F: REPORT METHODOLOGY

- Analyzed five years of financial audits (2002-2007)
- Analyzed five years of IRS Form 990 (2001-2005)
- Examined FY 2008 budget and year to date
- Reviewed publicly available material including website
- Held initial meeting on December 7, 2007 with:
  - Meg Campbell, Head of School
  - Rhonda Cutler, Director of Development
  - William Walczak, President Board of Trustees
  - Thomas Quirk, Treasurer Board of Trustees

Note: Years in this document refer to Fiscal Years, which end 6/30.

APPENDIX G: BOARD RESERVES

- Board designated reserves are useful as funds are monitored but not rigidly restricted; allowing the organization to an unexpected event.
  - In NFF's view, a permanently restricted endowment should only be actively built if a nonprofit has **excess** fundraising capacity.

- Some reserves that may be appropriate for the organization, in light of its infrastructure needs and growth plans, include:
  - An internal line of credit reserve to bridge funding delays
  - An infrastructure reserve for future facility/equipment needs, initial investment in new administrative staff, etc
  - An "opportunity" or program-enhancement reserve
  - A long-term investment reserve

- The "appropriate" reserve type and size are uniquely specific to each organization's individual needs and goals, and risk tolerance
  - It is important to maintain 1-3 months of cash outside of reserves to meet daily & seasonal working capital needs (i.e. meet payroll, pay vendors, etc.)

For more help from NFF, contact:

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Visit our website for additional information:
www.nonprofitfinancefund.org