winter 2011 · issue 10

Leadership Education and Development Newsletter

LEADer

A publication designed to promote visionary and forward-thinking discussions between and among NCGA's Western Corridor co-op leadership

A Study Guide for Co-op Leaders

Monitoring the Co-op's Financial Health

Inside This Issue

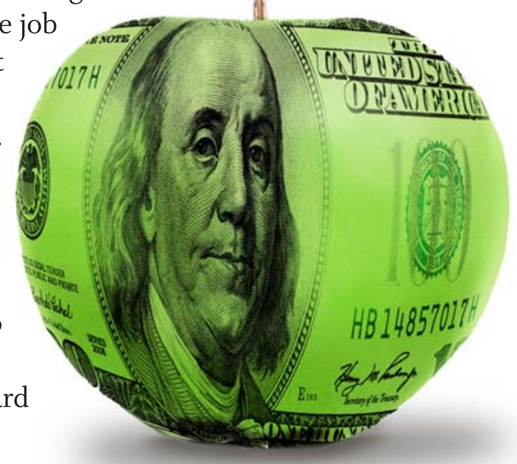
Study Guide

Financial Reports and Trends

Healthy Food, Healthy Finances

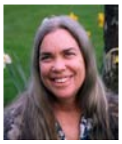
Monitoring financial statements comes with the job of being on a co-op board. Whether you relish the quarterly review of the financial statements, dread that agenda item, or couldn't care less, it is an important board responsibility.

Some of us only learn to read financial statements and to understand what they can and cannot tell us about the co-op's health and future potential by serving on a board. So for those who don't step into the job with deep financial analysis skills or experience, we're here to say: Don't sweat this one. It's not even close to being the trickiest or most difficult part of the job of the board. Important? Yes. But it is one that all directors willing to spend the time can learn to master.



This issue of the *LEADer* will help you and your board better monitor your co-op's financial health. We hope the articles help directors and management develop some common agreements and understandings about what the board should be paying attention to—the overall picture and trends—as well as specifics and details. That's not to say that the details aren't important. They often provide insight into what's behind the trends. But start with the big picture (the forest), and with time you'll learn how to understand the details (the individual trees). We offer this issue and a couple of tools in hope that they help the entire board with this role.

Board Effectiveness Support Team (BEST)



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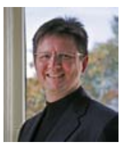

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ask the BEST
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More about the LEADer

A publication designed to promote visionary and forward-thinking discussions between and among NCGA's Western Corridor co-op leadership

- The *LEADer* is published quarterly and is distributed to directors and leaders of Western Corridor co-ops.
- The *LEADer* is now available to all interested co-op leaders at no charge, thanks to the generosity of NCGA's Western Corridor members. You can find information about the LEAD program and an online subscription form at *http://www.cgin.coop/leader*.
- We welcome your reactions, suggestions, and contributions, as well as questions for us to answer in future issues. Send comments or questions to *askthebest@ncga.coop*.
- The next issue will be available in spring 2011. That issue will focus on the board's important role in evaluating the general manager's performance.
- For more information about NCGA, the Western Corridor, upcoming western regional board training events, the *LEADer*, or the BEST, contact:

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The *LEADer* Is Online and Available to ANYONE!

The *LEADer* is available to all interested co-op leaders. This issue and all back issues are available online at *http://www.cgin.coop/leader*. Western Corridor co-ops can have new issues sent directly by e-mail; contact Karen Zimbelman at *kz@ncga.coop*.

Making Peace
with Financial Statements

by Philip Buri

Very few people in the co-op world love financial statements. And the rest of us are more than happy to let these few people do the work. Yet we all have the ability to use financial statements to govern our co-ops. The trouble is psychological, not technical. What could be more fraught with subconscious angst than math *combined* with money? That's what financial statements are—math and money. Put that way, I'm surprised we haven't had more trouble over the years.

In this month's edition of the *LEADer*, we dig deep into our collective unconscious to make peace with financial statements. Our pitch to you is simple: financial statements gauge your co-op's health, kind of like a thermometer. Once you learn how to read your co-op's temperature, you'll know whether things are okay, slightly off, or really sick. Financial statements come with a host of intimidating acronyms, mysterious ratios, and bewildering numbers. But in the end, they all tell you whether your co-op is healthy or not.

How do we make peace with financial statements? We suggest a few steps. First, accept the psychological landscape. We join co-ops and run for the board with great intentions but often no formal financial training. Reviewing financial statements takes us back to high school algebra and its inevitable baggage. We give you permission to feel anxious and queasy.

Second, think of a time when you developed a working relationship with finances. I keep track of my checking account balance and know that if it is in a general range, I'm okay. Above a certain amount and I can splurge a bit. Below a certain amount and I'm buying $5 bottles of wine. Your goal is to develop that same relationship with *a limited group* of numbers on your co-op's balance sheet. The hope is that you can take a quick look at a few monthly numbers and know whether the co-op is okay, sort of flush, or in a hole.

Third, the challenge is to find the *meaningful* numbers. Remember the few people who love financial statements? They love all the numbers in every shape, form, and spreadsheet. They are like car buffs who understand how every part works under the hood and revel in their complexity. The rest of

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Making Peace with Financial Statements

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us do not need to know these things to drive a car and keep it working. We just need to know the really, really important stuff.

Fourth, your general manager has either mastered this material or knows someone who has. Each month, your GM looks at a few key indicators to judge the working health of the co-op. These typically include your sales revenues, labor expenses, margins, and net income (among others). Wait. Come back. I promise we will cover these concepts in the pages to come. All you need to know now is that you don't need to master everything on the financial statements. You just need to know where to look for the good stuff.

Fifth, experience helps. As with your personal finances, learning co-op finances is an acquired skill. Over time you will see that some numbers stay relatively stable month to month. When they jump out of line, you'll want to know why. Other numbers bounce wildly from day to day. What you really want to know is what the long-term trend looks like. Again, this is simply a matter of perspective, something you acquire over time.

So take a deep breath and join us as we descend into the rings of co-op finances. Like any journey through forbidding territory, it will require courage, intuition, and luck. But at the other end of this journey is a golden vision: you will pick up your co-op's monthly financial statements, look at five key lines, and say, "Looks good." And mean what you say.

FYI
CoCoWhat??

Over the course of the last decade, food co-ops have been sharing financial data through a system called CoCoFiSt, which stands for common cooperative financial statements. CoCoFiSt has evolved into a sophisticated financial database. A worker co-op called CoopMetrics manages it for a variety of co-op sectors (housing co-ops, purchasing co-ops, and others). CoCoFiSt takes quarterly financial information from all participating food co-ops and presents it in a variety of ways for comparisons and benchmarking. Managers can see comparisons to peers (regionally or by size). They can access tools that help with budgeting, identifying opportunities for improvement (top quartile), and quantifying trends. Coming soon: an easily generated report that shows a co-op's financial performance compared to its peers, which managers can share (confidentially) with boards.

Eight Key Financial Indicators

for Co-op Boards to Monitor

by Lucinda Berdon and Paige Lettington

Watching these indicators will also help you better monitor the normal, related fluctuations of business cycles and isolate changes that need more attention.

How the heck do you get the overall picture of a co-op's financial health? Let's look at the main tool in the manager's tool kit—key indicators.

Key indicators are the core financial measures that all managers use to monitor financial performance and to identify trends. We propose that boards focus their review on the following eight key indicators, all of which are pretty common in the cooperative grocery world and offer at least a starting point in assessing your co-op's financial status. In diving into these indicators, you'll want to understand:

- What each indicator tells you. Which part of the financial picture does it help clarify? What are the general benchmarks for good (or better) financial performance? What factors influence this number—make it get better or get worse?
- Overall trends. A single quarterly financial statement with less than desirable results is not a disaster. In any business, financial performance will fluctuate depending on the season, the economic climate, the local market, and any number of internal or external situations. However, having three or more consecutive quarters with poor performance, especially when it was not anticipated, does indicate that something is amiss and worth keeping an eye on.

By looking at these indicators over time, you'll be able to see what is changing and how the co-op's actions and results impact the indicators. Keep in mind that positive and negative trends are

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Eight Key Financial Indicators

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Great Stuff Food Co-op

Quarterly Financial Statements as of September 30, 2010

Income Statement	Quarter Ending 9/30/09	Quarter Ending 9/30/10
Sales	3,000,000	3,300,000
Cost of goods sold	1,905,000	2,046,000
Gross margin	1,095,000	1,254,000
Total expenses	1,085,000	1,221,000
Other income/expenses	3,000	5,000
Net surplus (profit)	**7,000**	**28,000**

Balance Sheet	Quarter Ending 9/30/10
Assets	
Current assets—cash	600,000
Current assets—all others	150,000
Fixed assets	250,000
Other assets	10,000
Total assets	**1,010,000**
Liabilities	
Current liabilities	250,000
Long-term liabilities	310,500
Total liabilities	**560,500**
Equity	
Member investment	252,500
Retained earnings	155,000
Net income (YTD)	42,000
Total equity	**449,500**
Total liabilities and equity	**1,010, 000**

not necessarily good (or bad) indicators in and of themselves. Your analysis of the trend (is it a good trend or a bad one) will depend on your goals, as well as the overall context. For instance, watching cash go down over six quarters may seem like a bad thing in isolation, but if you know the co-op plans to use cash for some much-needed improvements, it's no longer a red flag.

Watching these indicators will also help you better monitor the normal, related fluctuations of business cycles and isolate changes that need more attention. For instance, if sales are up 15 percent, you can expect dollars spent on labor and operational expenses to also be higher. On the other hand, if sales are down 5 percent, those same expenses should also decrease. The level of income needs to support the level of expenses. That's why we use ratios to monitor performance. On the income statement, all items are expressed as a percentage of sales. Rather than looking at individual dollar amounts, look at the percentages on your budget and compare them to your quarterly, year-to-date, and rolling quarter information.

Some boards establish red flag warning signals. These can be deviations of a set percentage or dollar amount, depending on what you're looking at. One co-op has a red flag warning for anything that deviates 10 percent from budget, up or down. For instance, if your budget for labor is 23 percent of total income, 10 percent of that would be a 2.3 percent variance. So if your co-op's labor all of a sudden jumps up to 25.5 percent of total income, find out from the GM what the reasons are. If the deviation is less than 10 percent, you probably don't need to worry about it unless it trends upward for two or more consecutive quarters. Consider establishing red flags for your own co-op and experiment with the results.

To assist in your review of these eight key indicators, we offer (above) very simplistic financial statements from a fictional co-op.

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Eight Key Financial Indicators Reference List

Indicator	What Is It	Where to Find It	What to Look For	General Benchmark	Preferred Trend	Red Flag	Great Stuff Food Co-op
Sales and sales growth	Total revenues collected through operation of normal business activities	Income statement	Has the historic level of business activity changed? Look at past years as well as quarter-to-quarter fluctuations. How do growth trends vary from season to season? How does growth compare to local competitors, to other co-ops, and to your goals?	At least 3% growth	Increasing	Decreasing	10%
Gross margin	Difference between cost of goods sold and sales. This money will pay for all expenses (labor, rent, supplies, etc.).	Income statement	Gross margin as a percentage of sales is one of the most important pieces of financial data that the board should monitor. Gross margin is the most difficult aspect of a retail food business to manage and control. A gross margin that is a few percentage points off its goal will have very negative effects on profitability.	Varies depending on the market and product mix— in general 34 to 38%	Consistently meets targets	Unplanned and/or unexplained decreasing margin	38% (36.5% in 2009)
Expenses	Total amount paid for operating expenses (wages, rent, utilities, insurance, supplies, advertising, cleaning, equipment, etc.)	Income statement	Percentages of various key expenses (personnel, marketing, etc.) should be monitored from period to period, as well as compared against industry standards.	At least 0.50% less than gross margin	At budget or less	Significantly over budget	37% (36.17% in 2009)
Net income (profit)	Difference between gross margin and total expenses	Income statement	This number will vary, depending on the co-op's goals. Are you trying to build some reserves to prepare for an expansion, or to lower prices and accept less profit to provide better value to members? Compare numbers to previous reporting periods to see if things are improving or not.	At least 0.50%	Meets budget or better	Losing money or in the red (unplanned)	0.85% (0.23% in 2009)
Cash and days of cash on hand	Money in the bank or readily available to pay operating expenses, including the purchase of goods for sale	Balance sheet	Compare cash balance to total purchases and expenses in a period to find the total days of cash. A week's worth of cash is workable. With more than two weeks' worth, cash should be invested rather than kept for immediate access.	10 or more days	Increasing, with more than 20 days	Decreasing, with less than 10 days	16.53 days
Current ratio	Ratio of current assets to current liabilities (divide current assets by current liabilities)	Balance sheet	Provides a comparison of assets available to cover short-term debt and financial obligations. Less than 1:1 can be trouble (not enough cash to meet current obligations).	1.25 (or $1.25 in current assets for each $1 in liabilities)	Steady at 1.25 or improving	Less than 1	3.0
Member shares	The percentage of total assets financed by member investment	Balance sheet	Answers the question, "How much of this co-op has been financed by member-owners?"	20–30%	Over 30%	Less than 20%	25%
Debt-to-equity ratio	Ratio showing the relationship between total debt and total equity (capital)	Balance sheet	Acceptable ratios vary depending on the situation. A range of 1:1 to 2:1 is realistic for most food co-ops. A ratio closer to 1:1 is advisable if the co-op is experiencing instability.	2:1	Decreasing and less than 2:1	Increasing and more than 2.5:1	1.25

Portions of this chart were adapted from *Reading and Utilizing Financial Statements* by Fred Stapenhorst.

Trust and Verify

Don't Monitor Alone

by Martha Whitman

When you think of audits and accountants, do Enron and Arthur Andersen come to mind? Bad things happened when auditors failed in their ethical responsibilities by giving Enron a clean bill of health when the company was really a house of cards. The Sarbanes-Oxley Act of 2002 was enacted in response to Arthur Andersen's unethical auditing practices, and now accountants are required to increase the scope of their services. Currently the rules of Sarbanes-Oxley apply only to publicly traded corporations. It may be that someday nonprofits and cooperatives will have to comply, but until then, we have a great deal of flexibility in contracting for external financial monitoring.

Even if accountants and audits aren't on your radar, as a board member it's good to know what they can and can't do for you and the role they play in the independent external monitoring of your financial statements. There may be excellent reasons why your board doesn't contract for financial auditing; below are reasons why you might consider it.

Have you ever questioned why your board might contract for a professional audit of the co-op's financial statements? They're pretty pricey, right? And aren't you sending a message of distrust to the general manager? The answers are yes—they can be expensive—and no, independent external monitoring is simply a smart business practice. Oftentimes general managers do benefit from information that comes out of an audit, but that's just a nice by-product. What's really happening is that one of the key responsibilities of a board, protecting the members' assets, is achieved. Contracting with someone from outside the co-op to examine the numbers is not a statement of a lack of trust but rather a prudent path to fulfilling the board's duty of care and diligence. And the professionalism can cut both ways; a new general manager might insist on an audit to establish the baseline for which he or she will be held accountable. Another reason your board might contract for an audit is to fulfill a lender's requirement, in which case there isn't a choice about the scope of external verification. In this case, the cost of the audit is essentially one cost of procuring a loan.

If you aren't required to do an audit but still want to verify through independent external monitoring, your board might consider engaging an accountant to perform a financial review. You and your board have to weigh the pros and cons of an audit versus a review—your decision will depend upon your particular circumstances. A financial review consists of the accountant verifying financial records using data provided by management. With a review, the accountant is not required to obtain any independent corroboration to substantiate the records. In contrast, as part

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Trust and Verify

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of an audit, the auditor must obtain independent evidence to verify account balances. (This accounts for much of the price difference between a review and an audit.) A review doesn't provide the auditor's statement of opinion, which is required under standard rules for an audit. This is a significant difference. An audit, through the statement of opinion, provides the co-op legal assurance, whether or not the financial statements are free of material misstatement. A review, on the other hand, due to its scope, offers what is technically referred to as limited assurance.

Some co-ops have an audit every year, while others decide an audit every three years is adequate. Another common approach is to have reviews during interim years between audits. Such was the case at La Montañita until our independent accountant presented us with another option. Since we don't have a loan covenant requiring an audit, our business has been stable, and our accountant understands the cooperative model, he suggested we switch to reviews, with the caveat that he would monitor year-end inventory, so if the need arose, we could switch back to an audit in any given year.

What has made this plan particularly appealing (beyond the obvious cost savings) is how we now tailor each year's review with an additional engagement for services known as agreed-upon procedures. It's a separate engagement to perform specific monitoring driven by what is happening at the co-op. So far we've identified four areas for additional focus to be covered under the agreed-upon-procedures engagement: fixed assets, cost of goods sold, sales, and human resources. In this engagement, a few accounts are randomly selected within the chosen area and are checked for accuracy and adequate internal controls. If the results of the random investigations are good, the agreed-upon procedures are done. If an irregularity appears, the auditor might dig deeper but will certainly make recommendations for changes. Keep in mind that your general manager might have good reasons for doing something a particular way and might not agree with a recommendation, in which case the GM must adequately defend his or her position so that the board can make an informed decision.

For any given year, circumstances drive the selection of areas for agreed-upon procedures engagement. We started with fixed assets because we had just completed a major store expansion. Last year the area was human resources because we were between years of management's own external monitoring. And this year we'll ask our auditors to review cost of goods sold. As there was a chance we were going with a new POS system, it didn't make sense to select sales because procedures would potentially change and render the engagement moot.

The discussion to determine each year's area of engagement occurs between the board's finance committee and an independent accountant; the committee then submits its recommendation for board approval. (As the auditor's work is part of the board's external monitoring, it isn't management's job to make the choice.) We are now in our third year using this approach for external monitoring, and we are pleased with the results. The cycle of particular focus into specific areas has provided prudent oversight and useful recommendations, along with cost efficiency. The system may not be for everyone, but it has served us well so far.

Under the umbrella of cooperative principles and values, co-ops are primed to enjoy a positive and trusting relationship between boards and

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Trust and Verify

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managers. The role of external monitoring is not to "catch" management doing something wrong. It's a function of trust and verification. An independent accountant contributes his or her professional expertise to help the board fulfill its duty of care and diligence. Along the way, positive outcomes can surface, to the benefit of both board and management, and can ultimately strengthen the co-op as a whole. Since most co-op board members aren't highly proficient with finances yet are still accountable for the performance of the co-op, independent external monitoring is worth your consideration, and it certainly offers the potential for a better night's sleep.

Try This: What If?

Take 15 minutes at each board meeting (or one board meeting per quarter) and have a "what if" discussion. For instance:

- *What if our co-op was given $500,000? What would we do with that windfall?*
- *What if it became apparent that our sales were declining at a slow but regular rate?*
- *What changes in consumer shopping have we observed in our store since October 2008 (the start of the current recession)? How do those changes match national trends? What should we be planning for the co-op's future if patterns hold or don't change?*
- *What would we be doing today if we knew we would have to relocate in three years?*
- *What would we be doing today if we knew a new competitor was going to open within a mile of the co-op in the next year?*

See You in Portland!

For the NCGA Western Corridor Regional Board Training

The next Western Corridor regional board training will be held on **Saturday, March 26, 2011,** in Portland. Like past regional training sessions, this year's session will offer a "Cooperative Board Leadership 101" seminar for new directors, led by CDS Consulting Co-op board trainers. In addition, we'll offer a concurrent board effectiveness seminar on strategic planning for consumer co-ops. The planning role is a critical one for co-op directors, and this session will explore the successful path to long-range and strategic planning, methods for engaging members in the process, and how to reflect member needs and interests. Details and registration are available through your co-op's NCGA designated representative. Join us for another day of group

By the Numbers

Board Decision Making Based on Financials

by Marcia Shaw

Financial decision making is based on a philosophy about how we should conserve and use our resources. It's likely that you both agree and disagree with other directors about the right time to make decisions that cost substantial amounts of money (building improvements, equipment upgrades) or involve risks. That said, as part of a board, all directors need to find a way to review financial reports, projections, and plans and build agreement on using that information as a basis for making decisions.

Before getting bogged down in a specific situation or proposal, it may be useful for your board to have a broader discussion about how those choices play out and the cost/benefit assumptions that we share. Focus on a discussion about the key assumptions that make up the budget and on the actual figures. You'll avoid wrangling over specific budget lines if you can agree on broader underlying principles and the implications over time.

Personal Financial Philosophy

It's also useful to recognize that you might handle your own personal budget and financial decisions very differently from other board members. From "Budget? What budget?" to "I can account for every penny of my monthly expenses," we all have different financial styles. Board members must understand that handling the co-op's financial and business decisions might be quite different from how individual directors handle their personal finances.

Most food co-ops are very conservative in their financial decisions. One could argue that that factor has been an important element in our longevity and success over the years. But in the business world, we need to use our resources wisely and to best business advantage. Operating debt-free is rarely viewed as a prudent way to go in business circles, as doing so can greatly limit a co-op's ability to leverage its resources to accomplish goals. Similarly, having a huge stash of cash isn't always the best business decision. Another factor that can be hard for directors to adjust to is the magnitude of financial decisions. Most of us aren't used to thinking about saving or spending a million dollars (or several million dollars); but this is likely the scale of the decisions facing many of our co-ops.

Budgets and Budget Variance

In addition to having some broad agreements about how conservative we'll be or what level of risk/benefit we're willing to accept with co-op money, directors also need to consider the budget itself. Some believe that a budget is a planning document and as such it will need to be modified as the year goes on and reality shows up on monthly statements. Others treat the budget as a yearlong reflection of the co-op's plans and note or track deviations from those plans as they occur. The board (with management) ought to have some understanding of what will happen if you generate windfall

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By the Numbers

Board Decision Making Based on Financials

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profits or just have a really great quarter or year. What if a truck takes out a bridge close to the store, and the driveway and parking are disrupted for months? It happened to us! Unforeseen circumstances can have a big impact on your bottom line.

How will the board view the budget in light of such unexpected factors? What is the board's expectation about how management should adapt to unexpected situations? How will the co-op's finances be affected by external factors, and how are your co-op's budget and financial philosophy affected by those factors—some of which you can predict and some of which are entirely unpredictable. All budgets should include a reserve or amounts that can be used by management when things don't go as expected. What parameters of deviation will the board accept? What are the board's expectations in terms of management reporting as these things are understood, revealed, or occur? There are no "right" answers to these questions, but it will be helpful (and calming) to have a prior discussion on what happens if assumptions change or are revealed to be wrong.

Monitoring Trends

Sometimes it's hard to make decisions based on a slowly moving target. Little changes from month to month may not mean much, but if some of your key indicators change steadily (and in the same direction) for six months to a year, that's a trend worth paying attention to. Just as it's important for directors to pay attention to the co-op's goals and how they translate into the co-op's finances, it's important to pay attention to what's going on in the business world beyond your doorstep.

Some directors find it useful for the GM to report regularly to the board about national natural food industry, local market, and environmental trends. How might the business climate in your city, county, or state impact the co-op? What do we know about changes that competitors might be making in the coming year? What changes in the organic foods industry should we be considering in planning for the coming and future years?

These trends can be subtle, but urban planning, traffic patterns, new housing developments, school placements, and family patterns can all change your shopper base, membership, and overall shopping patterns. Is the board tuned in? One reason we seek diversity in board members is to represent different constituents and areas of knowledge. Don't be surprised if directors have differing perspectives on ambiguous information.

Financial information is an important element in board decision making. The board needs accurate information presented cogently. It needs to understand what the numbers say and the limits of those messages. We need to be clear on what the subtle trends are and what management is doing to either curb those trends or capitalize on them. However, most difficult board decisions are matters of judgment that take into account all the variables that get brought to the table. Financial data is an important piece of the whole. Money talks and it often shouts, but decisions are still made by humans on the board. Make sure your board understands the language.

Check It Out!

For More Information

Additional articles that cover aspects of the board's financial monitoring role for further reading and consideration:

"Reading and Utilizing Financial Statements" by Fred Stapenhorst. From *Challenges to the Cooperative Board of Directors*. This article provides an overview of co-op financial statements, as well as a "10-point financial analysis" for directors. Available for purchase at: http://www.cgin.coop/toolbox/challenge_pub

"Balance Sheets: Getting the Picture of Your Co-op's Financial Position" by Mark Goehring. *Cooperative Grocer* magazine, September/October 2007. http://s.coop/6b6

"Economics 101—Sunk Costs and Opportunity Costs" by Scott Beers and Margaret Lund. *Cooperative Grocer* magazine, November/December 1998. http://s.coop/6b7

"Finance Committee Finesse" by Scott Beers and Margaret Lund. *Cooperative Grocer* magazine, March/April 1998. http://s.coop/6b8

"Financial Management and Ratio Analysis for Cooperative Enterprise" by the U.S. Department of Agriculture. This article is written for agricultural businesses, so some parts do not apply well to grocery and retail businesses. http://s.coop/69m

"Understanding Audits" by Randy Lee. *Cooperative Grocer* magazine, April/June 1989. http://s.coop/6b9

"Understanding Ratios" by Scott Beers and Margaret Lund. *Cooperative Grocer* magazine, January/February 1998. http://s.coop/6ba

Next Issue Focus on

General Manager Evaluation

Our next issue, which comes out in March 2011, will look at how boards can use the GM evaluation process to improve performance and clarify goals and expectations. We'll provide some guidelines, as well as some tools that can guide your board's annual evaluation process. Send your thoughts, questions, experiences, ideas, and tips on this topic to *askthebest@ncga.coop* or contact Karen Zimbelman *kz@ncga.coop*.

Thanks Michele!

Michele Adams is leaving First Alternative Co-op and the western corridor to enjoy other life pursuits and travel. Michele has served on the BEST since its inception and has been an invaluable contributor to our emerging *LEADer* publication and our regional board training sessions Thanks so much for all your contributions, Michele!

FINANCIAL REPORTS AND TRENDS

A LEADer STUDY GUIDE

MONITORING FINANCIAL TRENDS

It helps to see overall financial trends presented in a clear picture and over time. We offer the following template, covering the eight key financial indicators, for your regular financial review.

Your board may get its financial summary in this format already, or you could ask for it in the future. However, since many of us learn by doing, here are some steps to engage all directors in a hands-on learning experience with these indicators and this report format:

1. Decide who will coordinate the group's activity. This could be the board treasurer or any director willing to coordinate and lead the exercise.
2. Set aside about 30 minutes at a board meeting or set up a special finance review training meeting. In preparation, make copies of the following chart (or make your own) and get copies of your co-op's quarterly financial statements for the past eight quarters. (Feel free to adjust the dates on the chart to reflect the prior eight quarters.) Make sure that everyone participating has a calculator.
3. Start by calculating, as a group, all the indicators for the oldest financial period (first quarter 2009, in this example). As a group, identify which numbers you are using to calculate each ratio on the statements and calculate them. Make sure everyone gets the same ratio and understands how you got the result before moving on to the next calculation.
4. After you've completed the calculations for all eight indicators for the oldest period, decide how to continue. You can assign a different period to each person or have people work on calculating indicators in small groups.

In this issue, we offer tools to help directors better understand their co-op's financial trends and to identify whether the financial reports they're getting meet their needs.

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5. Once everyone has completed all calculations, compile one full chart of ratios for everyone and review it. Look at the trends and discuss them. Do you understand the changes in your current ratio? How did changes in your gross margin affect other ratios? How do your ratios compare to your co-op's goals? These are questions for the board to discuss with each quarterly financial review.

Later, consider having this data presented in an Excel format, with charts to accompany the numbers.

INDICATOR AND FORMULA	Indicator	Co-op's Target or Goal	1Q 09 (or oldest period)	2Q 09	3Q 09	4Q 09	1Q 10	2Q 10	3Q 10	4Q 10 (or most recent period)
Sales growth: difference in sales divided by sales in prior period	%									
Gross margin (% of sales): sales minus cost of goods sold, divided by total sales	%									
Total expenses (% of sales): total expenses divided by total sales	%									
Net Income (% of sales): net income divided by total sales	%									
Cash (days of cash on hand): total cost of goods plus total expenses divided by 90 (or number of days in period), then divided by current cash balance	#									
Current ratio: current assets divided by current liabilities	%									
Member equity (% of total assets): member equity divided by total assets	%									
Debt to equity: total liabilities (debt) divided by total equity	%									

ASSESSING FINANCIAL REPORTS AND MONITORING SYSTEMS

by Michele Adams

Here are some questions that can help you assess if your financial systems and the reports you're getting meet your needs as a board.

Indicate if you're:

✔ Happy with what you get

▲ Get something like this but would like some changes to presentation or formatting

✖ Don't get this or are not getting information that meets this need

FINANCIAL STATEMENTS AND REPORTS	✔▲✖
Do you receive simplified and clear quarterly financial statements, including an income statement (or "profit and loss" statement), balance sheet, and cash flow statements? Notes:	
Do financial statements show comparisons to the previous year, as well as comparisons to budget? Notes:	
Are financial statements accompanied by a management narrative that explains material deviations from budget or anomalies? Notes:	

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EFFECTIVE FINANCIAL MONITORING	✔▲✖
Does a finance committee keep the board up to date on financial matters that affect the board? **Notes:**	
Does the board have clear expectations about what it wants reports to cover (board policies, directives, or limitations statements)? **Notes:**	
Do you feel informed as to the financial condition of the store? Are the statements and reports presented in a way that gives you a clear picture of how things are going financially? **Notes:**	

BUDGETING	✔▲✖
Does the board review and approve budgets or projections for operations (income statement and balance sheet) before the start of each fiscal year, including core assumptions and goals for the coming year? **Notes:**	
Does the board review and approve a capital budget that identifies the total capital needed in the year, the priority for those investments, and a reasonable allowance for deviations? **Notes:**	
Does the co-op do financial planning derived from a multiyear plan? **Notes:**	

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FINANCIAL SYSTEMS AND COMPLIANCE	✔▲✖
Does the board ensure that the co-op follows generally accepted accounting principles in its financial systems and reporting through engagement with an outside financial expert? **Notes:**	
Does the board ensure adequate internal financial controls to safeguard the co-op's assets? **Notes:**	
Does the co-op settle its payroll, payroll taxes, and debts in a timely manner? **Notes:**	

FINANCIAL CONDITION AND POLICY	✔▲✖
Does your co-op budget and manage operations to meet goals and needs in terms of sales growth, margin, expenses, and net income? **Notes:**	
Does your co-op budget and maintain adequate ratios in key areas: current ratio, debt to equity, number of days cash, and member investment? **Notes:**	
Does the co-op maintain investments in institutions that are sound, financially prudent, and support the co-op's goals and values? **Notes:**	