Module 8: Cash Flow (Liquidity Ratio) and Debt Accumulation

Video time allowed 3:19 minutes

Facilitator Council president or other key council officer with assistance from the Scout executive

Learning objectives This module goes into detail on liquidity ratio and debt accumulation—from where to find these numbers on the monthly statement to the appropriate level of each for a financially sustainable council.

After completing this module, board members should

- Understand what a liquidity ratio is and how to calculate it.
- Know that the BSA national standard is a 1.33 liquidity ratio, or 45 days of cash on hand.
- Gain an understanding of what to do if the council liquidity ratio is too high or too low.
- Understand what is considered “manageable” debt and what is not.
- Know that the council needs written guidelines that serve as internal checks and balances, stating who on the board can authorize debt.

Materials needed

- Laptop, projector, and screen
- Council executive board handouts or binders—one for each participant—that can be printed in advance locally from the online appendix
- Whiteboard, flip chart, or overhead projector to facilitate discussion and presentation
- Local council statement of financial position and statement of operations

Introduction of Module 8

This module uses the video portion to explain liquidity ratio and debt accumulation in detail.

- First, you’ll review some of the key numbers; then, you’ll present a more in-depth scenario for discussion.
- The goal is to engage your audience, which enables them to apply logic to the formulas they’ve just learned. Make sure you ask participants why they chose a particular answer before you reveal all of the outcomes.

Show Module 8.

(Respectfully acknowledge any answer from participants. Discuss why they would have chosen that response.)

- Explain that this module will provide details on acceptable liquidity ratio and debt accumulation—and what to do if either is out of balance.
- Then, let them know they'll be participating in an interactive module after you review the information.
- Liquidity ratio
- Debt accumulation

Any questions?

- Ask if there are any questions and address them.

(Estimated discussion time will vary, based on the board level of experience and participation.)

Let's review.

- Debt should be manageable—or avoided.
- Liquidity ratio means your council can pay its bills.
- The council standard is 1.33 liquidity ratio, which equals 45 days cash on hand.

Cash Flow (Liquidity Ratio) and Debt Accumulation: Scenario

What would you do? This is a true scenario based on a situation that happened in a local council. I'll share the scenario and give you four options, then we'll follow each option to find out what the decision meant to the council in the long term.

A council needs to raise $2 million to build a new dining hall for its outdoor education environmental center. Its capital campaign brings in $1 million in pledges and cash donations, and they have verbal commitments for the additional $1 million from two other donors. Elated, the board decides to go ahead with the construction.

Cement is poured for the buildings, floors and walls installed, and about 40 percent of the construction is completed when the board learns the bad news—one of the donor companies is moving out of state, so they won't be making good on their $500,000 pledge. The other major contributor, a community foundation, was giving a matching gift, with approved specific time restrictions for 90 percent of the funds to be raised toward completion of the capital project.

Since the appropriate amount of funds had not been raised in the designated time frame, the council had to forfeit the money, and the foundation had no choice but to redesignate their matching gift to another charity.

What should the board do?

A. Take the money out of its operating fund and borrow from its endowment fund to restart construction.

B. Take out an immediate bank loan with low interest over five years.

C. Contact new donors and ask for $500,000.

D. Immediately stop construction until the money can be raised and in hand, and risk the price of completion going up some more.

Ask what your board members would do—and why. Then let participants know what happens next.

Option A: Take money out of its operating fund and borrow from their endowment fund to restart construction.

"Not the best option."

This council is now deep in debt and can't pay its day-to-day operating bills. So, they decide to borrow from the endowment fund to pay off the debt.

Explain the consequences . . . (add other thoughts)

- Borrowing from the endowment fund and spending the interest would have been a good solution if they had a plan to pay back the endowment fund.
- However, this board didn't.
- The council eventually had no long-term funds to continue their program and ended up selling their property to eliminate debt.

Option B: Take out an immediate bank loan with low interest.

"It's one option, but not recommended."

- This decision started an endless cycle of debt accumulation, to the point where it would take a miracle to correct.
- Explain the consequences . . .(add other thoughts)
- The council was in so much financial trouble that it had to merge with another council.

Option C: Contact New Donors and Ask For $500,000.

"Possible, but not likely."

- Most of the big donors who were contacted contributed. But they also wondered why the board was unaware of the council's financial dilemma. Although it is possible to raise a million dollars, that's usually the exception.
- Explain the consequences and add other thoughts.
- The council had to eliminate Scouting programs to lower the debt. And the dining hall was never completed.

Option D: Immediately Stop Construction Until the Money Becomes Available.

"This is your best option!"

- This makes sense. The council stopped spending money, re-evaluated where they were, and began identifying other sources of income. They involved the board and key volunteers to re-strategize and develop a short-term campaign to raise the needed funds.
- Explain the consequences and add other thoughts.
- They succeeded, without accumulating debt. Now, they have completed their environmental outdoor facility, and Scouting youth have benefited.
- This scenario is based on a real example.
- The BSA national Finance Impact Department is available to assist councils with developing their financial plans.