PARTICIPANT'S WORKBOOK

FINANCIAL ANALYSIS OF A SOCIAL ENTERPRISE

[Non-Profit Organizations and Co-operatives]

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FOREWORD

For several years, Chantier de l'économie sociale has contributed to a wide range of activities regarding the promotion and development of the social economy – throughout Québec, of course, and across Canada. Thus, over the years, solid partnerships have been created among organizations working in the social economy and community economic development.

In Québec, particularly since the Summit on the Economy and Employment in October 1996[1], all social economy players have worked on the creation of financial tools adapted to social economy enterprises. These tools have greatly favoured the startup and development of social economy enterprises, as they are called in Québec.

In 2007, a few partner organizations worked together to obtain access to Québec expertise in funding of social economy enterprises. This led to the idea of designing the project known as *Financing for social enterprises and the community sector: transferring the lessons of a decade of innovation in Québec.* Human Resources and Social Development Canada made a financial contribution to carry out the project over a one-year period.

The partner organizations in the project are: Canadian Centre for Community Renewal, Connections Clubhouse, Économie solidaire de l'Ontario, Edmonton Community Foundation, Enterprising Non-Profits and Canadian Community Economic Development Network, together with Chantier de l'économie sociale.

In spring 2008, Chantier de l'économie sociale began the project by constituting an Orientation Committee, with the role of participating in the adaptation of the existing financial tools and organizing consultation sessions and test sessions with social economy players. This process sought to understand the regional differences across Canada and design adapted training material.

This workbook is part of a set of themes related to the analysis and funding of social economy enterprises.

ACKNOWLEDGMENTS

Such a project could never have happened without the involvement and participation of many people. We especially thank the members of the Orientation Committee, Michelle Colussi, Éthel Côté, Martin Garber-Conrad, Norman Greenberg, David Lepage and Brendan Reimer, for their knowledge of Canadian regional realities and their expertise in the social economy and community economic development.

We also thank the participants in the different consultation sessions who contributed useful comments: Alain Keutcha, Anne Jamieson, Annie Dell, Bryn Sadownik, Carroll Murray, Catherine Ludgate, Cindy Coker, David Upton, Denyse Guy, Dolores Le Vangie, Eli Malinsky, Elizabeth L. Green, Garry Loewen, Jen Heneberry, Margot Smart, Marty Donkervoort, Matthew Thompson, Mike Hayes, Paul Chamberlain, Paul Crane, Penelope Rowe, Seth Asimakos, Stacey Corriveau, Tim Beachy, Tonya Surman.

Finally, we cannot fail to mention the work of Nancy Neamtan, President and Chief Executive Officer of Chantier de l'économie sociale, who was a guiding light in this project's design and implementation.

[1] Within the context of this Summit, the provincial government brought together the leaders from private enterprise, unions, education and associative, community and co-operative movements with the aim of finding solutions to restart the Québec economy.

INTRODUCTION

The work of adapting the financial tools was a major challenge, because Québec's experience is special, not only because of its language, but due to its social economy practices. Canadian realities also differ from one region to another.

For example, in Québec, the term *social economy enterprise* is used, while in the rest of Canada, *social enterprise* or *community enterprise* is preferred. Similarly, the concepts of third sector, solidarity economy and community economic development are in common usage when taking a different approach to production and/or the sale of goods and services for the benefit of the community.

Also, the project partners reached consensus on using the term *social enterprise* to name this form of community-based entrepreneurship. Making a choice has limits, however, because each region of Canada has developed according to its own geography, culture and history, and it is difficult for a single concept to illustrate all this wealth. To compensate for the deficiencies of a fragmented terminology, a glossary explains certain terms that can cause confusion.

To begin the study of the Financial analysis of a social enterprise, we thus suggest that you study the definition of social economy as developed by the leading players in the field in Québec, and the definition of a social enterprise.

Finally, the goal of the approach is to go beyond divergences, emphasize the points of convergence and make expertise accessible that can serve the interests of every player in the social economy field in Canada.

SOCIAL ECONOMY IN QUÉBEC DEFINITION[2]

The concept of the social economy combines two terms which are sometimes considered to be opposites:

- **"economy"** refers to the concrete production of goods and services; the enterprise as the organizational structure; and it contributes to a net increase in the collective wealth;

- **"social"** refers to the social and not just the economic benefits of these activities. The social benefits are assessed in terms of the contribution to democratic development, the support of an active citizenry, and the promotion of values and initiatives for individual and collective empowerment. The social benefits therefore contribute to enhancing the quality of life and well-being of the population, particularly by providing a greater number of services. As with the traditional public and private sectors, the social benefits can also be evaluated in terms of the number of jobs created.

In its entirety, the social economy field covers all activities and organizations built on a community based entrepreneurship and operating on the following principles and rules:

- the primary purpose is to serve its members or the community rather than simply to make profits and focus on financial performance;
- it is not government-controlled;
- it incorporates in its bylaws and operating procedures a process of democratic decision-making involving users and workers;
- it places people and the work first before capital in terms of the distribution of its profits and revenues;
- its activities are based on the principles of participation, empowerment and accountability of individuals and communities.

What is CED?

Community Economic Development (CED) is action by people locally to create economic opportunities and better social conditions, particularly for those who are most disadvantaged.

CED is an approach that recognizes that economic, environmental and social challenges are interdependent, complex and ever-changing. To be effective, solutions must be rooted in local knowledge and led by community members. CED promotes holistic approaches, addressing individual, community and regional levels, recognizing that these levels are interconnected.

Definition from **The Canadian Community Economic Development Network**

[2] *Excerpt from the report of the task force on the social economy,* "Taking On The Challenge Of Solidarity!", *from the Summit Conference* http://www.chantier.qc.ca/uploads/documents/categories_publications/rapport_synthese_final.pdf

A Social Enterprise is two entities in One

It is a **group of people**, brought together in a democratic framework, sharing values of solidarity and sustainable development in order to attain a common objective. This is the meaning of a social mission.

It also develops economic activities within the framework of a competitive market by producing and selling goods and/or services, but **with the aim of enabling the organization to carry out its mission.**

Two principal legal entities apply to the majority of social enterprises: co-operatives (CO-OP) and non-profit organizations (NPO).

This is the definition of a **social economy enterprise** as used in Québec. Within the context of the current project, the term social enterprise has been chosen. It is therefore used as the equivalent of "social economy enterprise" in the rest of the document.

Other definitions...

A social enterprise is a business with primarily social objectives where the surplus is reinvested in the business and/or used for community benefit.

Definition from **Building Community Wealth - A resource for social enterprises development** – Canadian Centre for Community Renewal – Centre for Community Enterprise – sept. 2006

"Social enterprises" refer to business ventures operated by non-profits, whether they are societies, charities, or co-operatives. These businesses sell goods or provide services in the market for the purpose of creating a blended return on investment, both financial and social. Their profits are returned to the business or to a social purpose, rather than maximizing profits to shareholders.

Definition from **Enterprising Non-Profits Program**
http://www.enterprisingnonprofits.ca

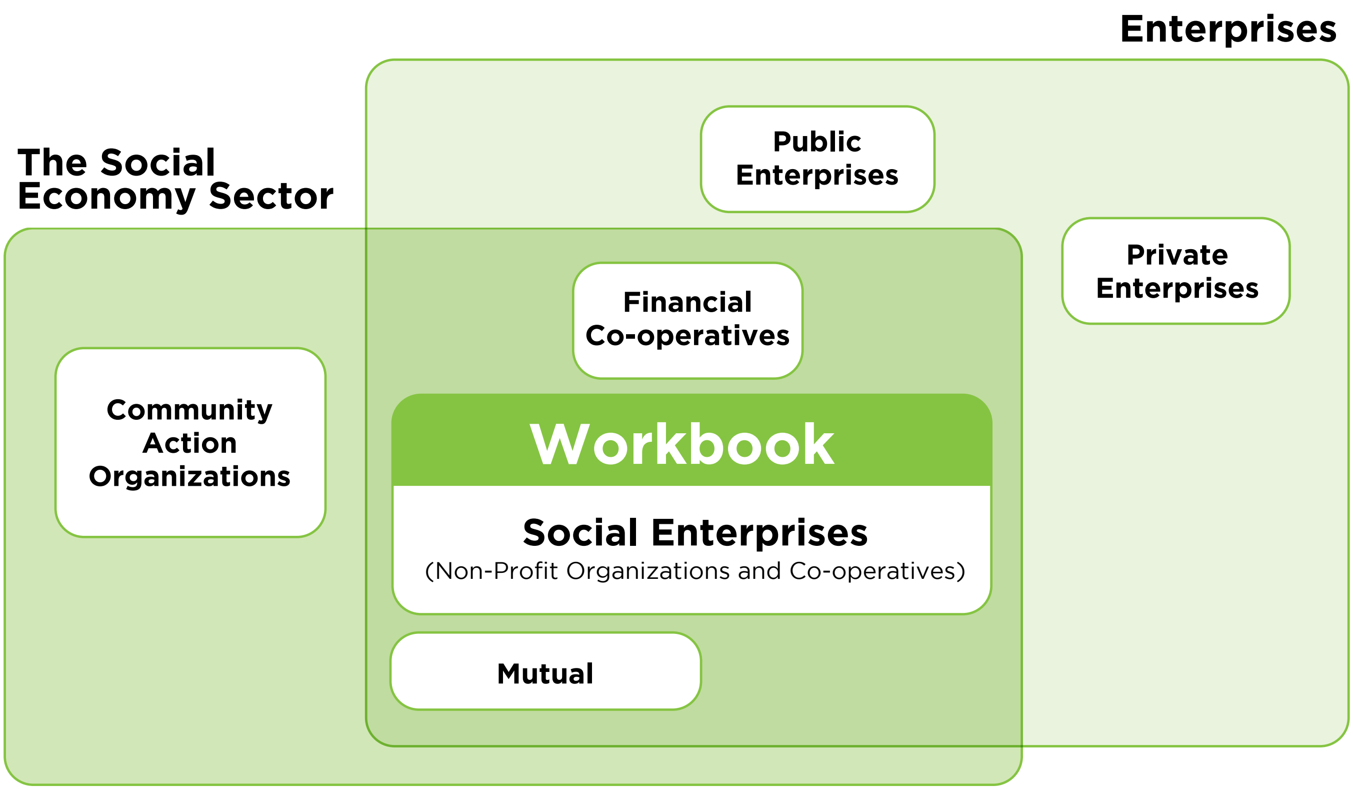
All social organizations, while their primary purpose may be to meet a social or community need, have economic value: they employ people, they produce or purchase goods and services, they own valuable assets and contribute to the economy in myriad ways.

Definition from **Social Innovation in Canada: How the non-profit sector serves Canadians ... and how it can serve them better.** Mark Goldberg, Canadian Policy Research Networks, 2004

Social enterprise *are revenue-generating business with primarily social objectives whose surpluses are reinvested for that purpose in the business or in the community, rather than being driven by the need to deliver profit to shareholders and owner. These can include enterprising non-profits or for-profit enterprises such as co-operatives and share capital corporations where all shares are held by non-profits.*

Definition in use in Manitoba.

In terms of application of this workbook, it is important to note at the outset that it has been designed to review projects undertaken by groups that are part of a formal collective entrepreneurial process. It specifically targets social enterprises (NPO – CO-OP) that generate revenue by invoicing their private and public users for goods and services.



It is suggested that you refer to the glossary for a definition of the terms used in this outline.

WORKBOOK'S GOALS

The theme of the "Financial Analysis of a Social Enterprise" workbook presents an analytical process specific to social enterprises (NPO and CO-OP) and is intended for financiers, analysts, coaches, consultants and fund managers who want to have a better understanding of the special features of these enterprises and thus make an informed decision on financing.

Goals

- Review the usefulness of conventional financial statements.
- Increase the chances of success of social enterprises and improve their access to financing.
- Learn the principle of adjustment of financial statements of social enterprises.

Prerequisite: the participant must have a proven knowledge of accounting logic and be able to understand the conventional financial statements of an NPO or a CO-OP.

This workbook is part of a series of three themes regarding the social economy:

Québec Social Economy Experience:
The Québec experience in the social economy and financing of social enterprises (NPO – CO-OP) / parallel to different regions in Canada.

Social Enterprises Analytical Model:
How to establish a profile to make an investment decision and assist in the development of a project, taking into consideration all the special features of a social enterprise.

Financial Analysis of a Social Enterprise:
How to restructure the financial statements of a social enterprise to increase its chances of success and improve access to financing.

All the training material has been designed in English and French.

THE FINANCIAL STATEMENTS OF A SOCIAL ENTERPRISE

4.1

IMPORTANCE OF THE FINANCIAL STATEMENTS

To be able to manage a social enterprise (NPO – CO-OP) effectively, the members of the board of directors and the management must have access to reports that give a general overview of the financial results, the financial position, and the source and utilization of funds. This financial information will help the directors and the enterprise's key resources to establish short-term plans, control current operations, formulate long-term plans and even facilitate decision-making.

In short

- Very revealing image of the enterprise's financial position.
- Makes it possible to establish short-term and long-term plans and control current operations.
- Serves for several external purposes: funders and government agencies for funding, employee representatives for union negotiations.

Understanding the financial statements is a basic condition for informed financial decision-making. The balance sheet, the income statement and the statement of cash flows are the most important financial reports: the balance sheet reflects the financial position as at a precise date, while the income statement summarizes what happened between two given periods and measures the general efficiency of management of the enterprise's operations. Finally, the statement of cash flows shows the changes in financial position from one period to another, and particularly the source and utilization of funds.

4.2

CAUTIONARY NOTE ON THE CONTENTS OF THE FINANCIAL STATEMENTS

Currently, the contents of the financial statements of social enterprises (NPO – CO-OP) only give a partial illustration of their actual economic and financial performance and little or practically no information on social performance. Indeed, the financial statements do not always disclose or value the specificities of social enterprises, namely the achievement of the objectives and the social mission. Here are the main problems encountered regarding the socioeconomic, financial and accounting aspects, which are hard to quantify and little reflected in the financial statements.

Socioeconomic aspects

The income statement does not offer alternative measures for achievement of objectives reflecting the specific missions of social enterprises and replacing maximization of the shareholders' wealth.

The balance sheet has difficulty presenting intangible assets, which generate wealth, in their entirety. In a recent document by the Canadian Institute of Chartered Accountants on identification of intangible assets, these assets are divided into four main classes[3]:

- Human capital: the competencies acquired by the management and the employees;
- Organizational capital: the competencies developed and safeguarded in the organization;
- Relational capital: the good or privileged relations the organization maintains with its environment, the synergies developed within a network;
- Contractual capital: this last class pertains to the advantages and opportunities from which an organization benefits, but which are presented only on the basis of the costs incurred in preparation of contracts.

The concept of research and development, recorded in the enterprise's assets, does not account for gains that are neither technical nor scientific but that contribute to the enterprise's value and solidity.

Financial and accounting aspects

- Difficulties presenting the fair value of the assets on the balance sheet, whether tangible or intangible.
  - Example 1: to protect the environment, a recreational organization improves a resort site, resulting in expenditures that are not necessarily recorded as assets in the balance sheet or, if they are, only show the reader the amount of the expenditure, without accounting for the actual increase in the value of the resort site.
  - Example 2: how to present an asset of an enterprise that negotiates an acquisition of property "at a discount", received as a donation or is totally subsidized.
- Difficulty of the income statement in presenting revenues from government contracts and confusing them with grants obtained by the enterprise.
- Difficulty standardizing representation of the investments.
- No balance sheet item allowing representation of investments in the form of quasi-equity.

[3] *As mentioned in the RISQ's* Guide for analysis of Social economy Enterprises, *Chapter 4, p. 2, 2004.*

IN SHORT

The financial statements do not value the specificities of social enterprises:

- No information on the enterprise's social performance—and thus only a partial illustration of performance.
- Difficulty presenting the non-monetary dimension, such as the fair value of the assets on the balance sheet, the involvement of volunteers, donations of fixed assets.
- Difficulty presenting the revenues coming from government contracts in the income statement (grant or current revenue).
- Difficulty standardizing the representation of investments.
- No balance sheet item allowing representation of the investments in the form of quasi-equity.

4.3

PRESENTATION OF THE FINANCIAL STATEMENTS

The enterprise's management is responsible for preparing the financial statements. Even if the assistance of a public accountant is sometimes required for this purpose, **the management always has the final say on the contents, in accordance with accounting standards.** The financial statements are subdivided into four reports:

- A balance sheet as at the last day of the financial year
- An income statement for financial year which has just ended
- A statement of net assets in the case of an NPO or a statement of the Reserve in the case of a co-operative
- and a statement of cash flows

The financial statements are usually established at the same date every year and are prepared on the basis of the general ledger account balance.

4.4

MANAGEMENT'S ANALYSIS REPORT: SOCIAL BALANCE SHEET

The presentation of the financial statements is disadvantageous to a social enterprise because of its specific mission and fundamental objective: achieving its social purpose and collective enrichment.

Many social enterprises have experienced difficulties obtaining financing from financial institutions. Indeed, the low profitability that appears in their financial statements, compared with the sectorial ratios, may seem to show a weakness in management, according to the traditional mode of assessment of a corporate financial file. Yet this simply reflects the social enterprise's fundamental objective.

To mitigate this disadvantage, some social enterprises have begun to attach something called a social balance sheet to their financial balance sheet. The social balance sheet is management's discussion and analysis of the financial statements, showing the enterprise's real social viability, among other information. This type of financial report by management offers the benefit of an image of its financial performance more suitable to the requirements of external institutions.

The social balance sheet can contain the following key points:

- information on the enterprise's specific mission and the achievement of its social objectives;
- certain terms of funding set by the funders that would not appear in the notes to the annual financial statements: this would allow a distinction to be made between debt and quasi-equity financing, indicating the principal repayment moratoriums, if applicable. This additional information will allow solidarity funders to consider their funding as a long-term debt and reclassify it as quasi-equity;
- the nature of any government contribution, which would explain its recurring character and its connection with the organization's mission, and its reclassification as recurring revenue;
- all relevant information involving an adjustment, such as non-recurring expenditures, exceptional revenue, etc.;
- indicate volunteer activity for a better assessment of the commitment of the members and the community in supporting the enterprise in its social mission.

INTERPRETATION AND ANALYSIS OF THE FINANCIAL POSITION OF A SOCIAL ENTERPRISE

5.1

BASIS OF FINANCIAL ANALYSIS

For various reasons, many people want to know an organization's financial position. Suppliers want to ensure that it is able to pay its bills. Funders have questions about its long-term capacity to repay principal and interest. Governments are concerned about management of public funds. The board of directors and the management are also concerned about its financial position, if only out of an interest in sound financial management or to negotiate with the funders. The analytical elements presented in this section seek to respond to these concerns.

One of the financial analysis methods used in this workbook is the ratio method. Based on a reading of several specialized textbooks in this matter, a financial ratio can have several terminologies and above all, different mathematical formulas. This means that some ratios are not really appropriate for social enterprises. To remedy this problem, this document has been designed in accordance with the approach and the ratios found in the RISQ's *Guide for Analysis of Social Economy Enterprises,* produced collectively by solidarity financial funders in Québec.

Thus, this workbook presents a financial analysis specially developed for social enterprises. In addition, for illustration purposes, two types of organizations that are part of the social economy, an non-profit organization (NPO) and a co-operative (CO-OP), have been used: CKOW Community Radio and the Manufacturing Plus Cooperative. These examples do not necessarily reflect the reality of all social enterprises in these sectors.

5.2

PRUDENT INTERPRETATION OF RATIOS

Before showing how to use the ratios, it is important to be clear about their nature: financial ratios commonly serve to establish relationships between the items of an enterprise's financial statements and study the changes in these relationships over time. They also allow financial analysts to make comparisons between companies at a given time (sector average). In other words, a ratio is only the relationship between two numbers, the reliability of which sometimes leaves something to be desired. One of these numbers (or both) sometimes represents realities that are difficult to discern, based on chosen accounting policies. For example, in calculating the working capital ratio of a food co-op or a co-operative school, the numerator particularly includes inventories. If the inventory item of the balance sheet were false (inventory appraisal error), this would be enough to inflate the working capital ratio unduly. This is why the financial analyst will prudently calculate a liquidity ratio that excludes inventories. In short, there is a risk that uncertain figures in the financial statements will produce misleading ratios. It is essential to be aware of this in advance to interpret the ratios with the relativity they deserve.

Moreover, this workbook is based on financial analysis geared to assessment of the social enterprise's financial performance, with little or practically no assessment of its social performance. The financial statements do not always disclose or value the specificities of social enterprises, that is, the achievement of the objectives and the social mission.

5.3

ADJUSTMENT OF THE FINANCIAL STATEMENTS

It is important to emphasize that the adjustment of the balance sheet and the income statement is only used for analytical purposes, because these adjustments do not conform to generally accepted accounting principles (GAAP).

5.3.1

BALANCE SHEET ADJUSTMENT: ASSESSMENT OF THE FINANCIAL STRUCTURE

For NPOs and co-operatives, certain balance sheet adjustments are necessary, particularly to determine the actual debt-equity structure (or the net worth) of the social enterprise, that is, the way the organization is funded in the long term. According to the Canadian Institute of Chartered Accountants Handbook (CICA), on the balance sheet, the enterprise's debt structure is represented as *long-term liabilities* under the following headings:

- **Long-term debt:** secured bank loans with financial institutions and loans granted by investment funds for "capitalization" purposes. In addition, in the case of co-operatives, long-term debt can sometimes include preference shares held by the members or third parties, and participating preference shares.

- **Long-term deferred contributions (NPO) or deferred grants (co-operative):** these are grants disbursed for acquisition of fixed assets.

Equity is represented by:

- **Net assets (NPO) or net equity (co-operative):** this is the enterprise's net worth, which represents the assets of the organization and its members, in the case of a co-operative.

The main reasons for reclassification of long-term liabilities:

- The deferred contributions or grants posted to long-term liabilities are not repayable debts and will have to be considered as equity.

- Several types of loans, currently posted to long-term debt, can be likened to patient capital or quasi-equity, depending on their characteristics. This type of patient loan serves for the enterprise's development and capitalization. Their characteristics are different from a term loan and a hypothec from a financial institution (loans secured by the financed assets) and will have to be reclassified as quasi-equity. This means that patient debt or quasi-equity has the following characteristics:

    - Generally it is unsecured (uncollateralized).

    - Principal repayment is often flexible (fixed portion, variable portion) and can be revised according to the enterprise's income statement. The return required can also be variable.

It is important to specify that only the long-term portion of the long-term debt (not counting the current portion) will be reclassified.

- According to the accounting standards (CICA), co-operatives have the obligation to account for the preference shares held by the members or third parties and the participating preference shares under long-term debt. However, Section 149 of the Canadian Co-operatives Act[4] states that the board of directors determines the amount of and the preferences, rights and restrictions attached to the shares and the conditions of redemption or repayment. The co-operative and its members thus have all the desired flexibility regarding redemption by the issuer, which allows them to consider the shares as equity.

[4] It is suggested that the concordance with the provincial co-operatives legislation of the region concerned be verified.

Special Feature of a Co-operative: Net Equity[5] and Reserve

Net equity

The accounts of this part of the balance sheet represent the balance between assets (what the co-operative owns) and liabilities (what the co-operative owes) and is divided into two categories.

- members' equity and
- co-operative equity.

Members' equity represents the social capital. In other words, it is the money paid by the members to buy qualifying membership shares and preference shares. Members' equity is variable and impermanent, because it fluctuates according to the inflows and outflows of funds by the members.

Co-operative equity can be constituted from three sources:

- the indivisible reserve is formed by the balance of the surpluses from the previous financial years which have not been paid to the members in the form of a rebate.
- the surpluses from the last financial year or overpayments; a portion of these surpluses will be paid subsequently to the Reserve, according to the decision made at the general meeting and based on the obligations of payment to the Reserve provided by law;
- the contributed surplus (for example, the amount of the shares assigned by a member to the co-operative upon departure).

To summarize, members' equity and co-operative equity fluctuate on the basis of:

- the issuance and repayment of membership shares and preference shares;
- the allocation of overpayments or surpluses to the surplus (deficit).

[5] *According to Québec's Co-operatives Legislation*

The Reserve

One special feature concerning co-operatives is the possibility of paying rebates to their members from a portion of the surpluses realized.

At the annual general meeting, after studying the recommendations of the Board of Directors, the members may allocate the surpluses or overpayments:

- for development of the co-operative to contribution of a *Reserve;*
- allocation of rebates in proportion to the transactions of each individual or corporate member in accordance with the co-operative's by-laws;
- allocation of rebates to the individual or corporate auxiliary members, in accordance with the co-operative's by-laws.

The statement of the Reserve of the co-operative indicates the amount of the surpluses that are retained by the enterprise from year to year. The previous years' surplus (or deficit) is added to (or subtracted from) the balance carried over from the previous year. Then the rebates and the taxes payable on the net surplus from the previous year are subtracted.

A new balance of the Reserve is obtained and posted to the co-operative equity section of the balance sheet.

Thus, it can be seen that the statement of the Reserve serves as the link between the balance sheet and the income statement.

Determination of equity or net assets

- The NPO's net assets or the co-operative's equity do not always reflect the fair value of their assets. It would be wise to examine the composition of the assets, in order to ensure that the balance sheet represents the enterprise's actual financial position. For example, does the enterprise have fixed assets (equipment, building, machinery, etc.) received as donations, which have not been accounted for? If this is the case, and the value of the property received in donations is significant, it is recommended that you have the market value validated by an appraisal report and account for it on your books.

In short, the purpose of reclassification of all these liabilities is to determine the enterprise's quasi-equity (or patient debt) and equity. Quasi-equity thus makes it possible to identify the safety and patient capital margin constituted in the enterprise's liabilities. This reclassification will have a major impact on all the financial stability ratios analyzed and interpreted in a section for this purpose. The table on the next page summarizes the characteristics of the capital structure of a social enterprise (debt, quasi-equity and equity). Certain liabilities may have to be reclassified to determine the fair value of the enterprise's equity and the debt structure, accounting for more flexible repayment commitments.

Reclassification of debt, quasi-equity and equity (net assets or net equity)

	DEBT	QUASI-EQUITY	EQUITY
Equivalent terms	Long-term liabilities	Patient debt	Capital Shareholders' equity Net worth Net assets (NPO) Co-operative equity
Characteristics	• Secured (or collateralized) loan • Represents a commitment to third parties, which must result in a future settlement • The commitment constitutes an obligation of repayment for the enterprise • Repayment of principal and interest in the form of a defined repayment schedule	• Unsecured (or uncollateralized) loan • Represents a commitment under which principal repayment can be patient (possibility of a principal repayment moratorium from a few months to several years) • Repayment is often flexible: fixed portion, variable portion, and their return may be variable, both linked to the amounts of the income statement, with maturity in the distant future. However, the principal still has to be repaid.	• No security required • Represents no obligation to repayment (future settlement is not time-limited)
Type of financing	Term loan Hypothec Commercial pledge Note payable Leasing Small business loan	Loan coming from a social economy investment fund for capitalization or development purposes	**NPO** Long-term deferred contributions (grants donations of fixed assets) Net assets **Co-operatives**[6] Long-term deferred grants (for acquisition of fixed assets) Preference shares held by third parties and participating preference shares Members' preference shares Co-operative equity
Type of creditors or investors	Financial institutions	Specialty social economy funds[7]. In Québec, there are RISQ, Fil*Action*, Investissement Québec, Community Loan Funds, etc.	Members Government agency Philanthropic investor

[6] *It is suggested that the concordance with the provincial co-operatives legislation of the region concerned be verified.*
[7] *It is recommended that you obtain information on the Funds and programs available in different regions of Canada.*

For example, the balance sheets of CKOW Community Radio and the Manufacturing Plus Co-operative will be adjusted.

Case 1: Example of balance sheet adjustment for CKOW Community Radio

CKOW Community Radio is an NPO that has been broadcasting for 15 years. Although it had been in financial difficulty for several years, an external diagnosis performed in 2001 validated that the programs' listenership is growing and that the local community strongly supports its alternative media. The support campaigns, which raise at least $60,000 each year, confirm this fact.

The audited balance sheet of the community radio station for the past two financial years as at August 31:

CKOW Community Radio
Balance sheet
As at August 31

ASSETS	**2002**	**2001**
Current assets		
Cash		2,772
Accounts receivable	25,324	22,581
Grants receivable	20,000	
Prepaid expenses	1,211	2,109
	46,535	27,462
Fixed assets (Note 1)	**81,568**	**30,480**
Intangible assets (Note 2)	**600**	**600**
Total assets	**128,703**	**58,542**
LIABILITIES		
Current liabilities		
Line of credit	2,424	
Accounts payable	37,915	40,742
Deferred contributions	33,000	58,990
Current portion of long-term debt	9,476	1,345
	82,815	**101,086**
Deferred contributions (Note 3)	**36,490**	**12,051**
Long-term debt (Note 4)	**32,468**	**1,944**
Total liabilities	**151,773**	**115,081**
NET ASSETS		
Invested in fixed assets	43,134	15,131
Unallocated surpluses	(66,204)	(71,670)
	(23,070)	**(56,539)**
Total liabilities and net assets	**128,703**	**58,542**

Here is the information regarding the adjustments to be made to the balance sheet:

Note	Details	Characteristics	Adjustments to be made
1	Fixed assets do not include a value of $25,000 of equipment received as donations and validated by an appraisal report.	According to accounting principles, fixed assets received as donations with a known market value must be accounted for.	To add to fixed assets in the amount of $25,000. To add to equity.
2	Intangible assets of $600 correspond to an old licence payment. These assets have no real value.	According to accounting principles, assets that that have no actual value must be written off.	To deduct from intangible assets of $600. To deduct from equity (unallocated surpluses).
3	Long-term deferred contributions correspond to grants received for acquisition of electronic equipment and to modernize the recording studio.	This is not a repayable debt.	To deduct from long-term debt. To add to equity.
4	Long-term debt represents a balance of a term loan of $468 (excluding the current portion) from the Caisse Desjardins[8] for acquisition of equipment. This loan is secured by a movable hypothec on certain equipment. The community radio station received a new loan contracted with RISQ[9] in the original amount of $40,000 without security, repayable over 5 years, to replenish its working capital and assist in development, following a diagnosis. The current portion of this loan represents $8,000. Term loan: $468 RISQ loan: $32,000 Total $32,468	The RISQ loan is patient capital for two reasons: • Unsecured loan. • The principal payment can be reviewed according to the enterprise's results.	RISQ loan to deduct from long-term debt ($32,000) To add to quasi-equity.

[8] *Financial co-operative in Québec.*
[9] *Réseau social d'investissement du Québec, an organization investing in the social economy in Québec.*

CKOW Community Radio
Interpretation of the balance sheet adjustment
as at August 31

	Note	2002 adjustment				2001 adjustment				
ASSETS		**Amount**	**To add**	**To deduct**	**Adjusted balance**	**Amount**	**To add**	**To deduct**	**Adjusted balance**	**Explanations**
Current assets										
Cash						2,772			2,772	
Accounts receivable		25,324			25,324	22,581			22,581	
Grants receivable		20,000			20,000					
Prepaid expenses		1,211			1,211	2,109			2,109	
		46,535			**46,535**	**27,462**			**27,462**	
Fixed assets	1	81,568	25,000		106,568	30,480			30,480	Add the equipment received as donations
Intangible assets	2	600		600	0	600		600	0	Deduct the licence, which has no book value
Total assets		**128,703**	**25,000**	**600**	**153,103**	**58,542**		**600**	**57,942**	
LIABILITIES										
Current liabilities										
Line of credit		2,424			2,424					
Accounts payable		37,915			37,915	40,742			40,742	
Deferred contributions		33,000			33,000	58,990			58,990	
Current portion of long-term debt		9,476			9,476	1,345			1,345	
		82,815			**82,815**	**101,086**			**101,086**	
Deferred contributions	3	36,490		36,490	0	12,051		12,051	0	Deduct the grant received for acquisition of fixed assets – no repayment
Long-term debt	4	32,468		32,000	468	1,944			1,944	Deduct the RISQ loan, which is considered as capitalization
Total liabilities		**151,773**		**68,490**	**83,283**	**115,081**		**12,051**	**103,030**	
Quasi-equity										
Capitalization loan	4		32,000		32,000				0	
NET ASSETS (Equity)										
Invested in fixed assets	1	43,134	25,000		68,134	15,131			15,131	Addition of equipment received as donations in 2002
Deferred contributions	3		36,490		36,490		12,051		12,051	Grant received for acquisition of net assets reclassified as net assets
Unallocated surpluses	2	(66,204)		600	(66,804)	(71,670)		600	(72,270)	Deduction of the licence, which has no book value
		(23,070)	**61,490**	**600**	**37,820**	**(56,539)**	**12,051**	**600**	**(45,088)**	
Total liabilities, quasi-equity and net assets		**128,703**	**93,490**	**69,090**	**153,103**	**58,542**	**12,051**	**12,651**	**57,942**	

After adjustments as at August 31, 2002:

- Total assets are shown at $153,103 instead of $128,703, after recognition of assets not accounted for and write-off of intangible assets.
- Adjusted liabilities are $82,283 instead of $151,773 after deducting deferred contributions (grant for acquisition of fixed assets) and the RISQ capitalization loan.
- The fair value of the enterprise's equity after adjustment is $37,820 instead of a negative amount of $23,070 (net assets).
- Equity and quasi-equity represent an amount of $69,820 instead of a negative amount of $23,070.

CKOW Community Radio
Adjusted Balance sheet
As at August 31

ASSETS	**2002**	**2001**
Current assets		
Cash		2,772
Accounts receivable	25,324	22,581
Grants receivable	20,000	
Prepaid expenses	1,211	2,109
	46,535	**27,462**
Fixed assets (Note 1)	106,568	30,480
Intangible assets (Note 2)		
Total assets	**153,103**	**57,942**
LIABILITIES		
Current liabilities		
Line of credit	2,424	
Accounts payable	37,915	40,742
Deferred contributions	33,000	58,990
Current portion of long-term debt	9,476	1,345
	82,815	**101,086**
Long-term debt (Note 4)	468	1,944
Total liabilities	**83,283**	**103,030**
Quasi-equity		
Capitalization loan	32,000	
NET ASSETS (Equity)		
Invested in fixed assets	68,134	15,131
Deferred contributions	36,490	12,051
Unallocated surpluses	(66,804)	(71,670)
	37,820	**(45,088)**
Total liabilities, quasi-equity and net assets	**153,103**	**57,942**

Case 2: Example of balance sheet adjustment for Manufacturing Plus Cooperative

Manufacturing Plus Cooperative is a worker co-operative in the manufacturing sector. It generated a net surplus of $39,599 in its year ended December 31, 2002. This surplus is recorded in the audited year-end financial statements (income statement and equity in the balance sheet), which are presented at the annual general meeting.

Having a sufficient reserve in 2002, the board will recommend, at the April 2003 annual meeting, that the members vote a $5,000 cash rebate. Consequently, 87% of the surplus will increase the reserve posted in the balance sheet as at December 31, 2003. We should remember that the $5,000 cash rebate will reduce the amount to be allocated to the reserve.

Here is the audited balance sheet of Manufacturing Plus Cooperative for the last two financial years as at December 31:

Manufacturing Plus Cooperative
Balance sheet
As at December 31

ASSETS	**2002**	**2001**
Current assets		
Cash	21,573	10,560
Investment	20,042	
Accounts receivable	13,004	20,408
Inventories	20,429	23,833
Prepaid expenses	4,490	5,344
	79,538	**60,145**
Fixed assets	**186,563**	**213,268**
Total assets	**266,101**	**273,413**
LIABILITIES		
Current liabilities		
Loan		25,000
Accounts payable	20,325	25,188
Deferred revenue	2,000	
Current portion of long-term debt	31,568	27,250
	53,893	**77,438**
Deferred grants (Note 1)	**10,465**	**14,645**
Long-term debt (Note 2)	**134,646**	**162,423**
Total liabilities	**199,004**	**254,512**
NET EQUITY		
Members’ equity	33,641	25,044
Co-operative equity		
Net surplus (deficit)	39,599	(10,120)
Reserve	(6,143)	3,977
	67,097	**18,901**
Total liabilities and equity	**266,101**	**273,413**

Manufacturing Plus Cooperative
Adjustments to be made to the balance sheet:

<table>
<tr><th>Note</th><th>Details</th><th>Characteristics</th><th>Adjustments to be made</th></tr>
<tr><td>1</td><td>Long-term deferred grants correspond to amounts received for acquisition of machinery.</td><td>This is not a repayable debt.</td><td>Deduct from long-term debt.

Add to equity.</td></tr>
<tr><td>2</td><td>Long-term debt (after deducting the current portion) breaks down as follows:

<table>
<tr><th></th><th><u>2002</u></th><th><u>2001</u></th></tr>
<tr><td>Bank loans (1)</td><td>69,236</td><td>92,853</td></tr>
<tr><td>RISQ loan (2)</td><td>23,855</td><td>31,806</td></tr>
<tr><td>Preference shares paid by the members</td><td>36,555</td><td>32,764</td></tr>
<tr><td>Participating preference shares</td><td>5,000</td><td>5,000</td></tr>
<tr><td></td><td>134,646</td><td>162,423</td></tr>
</table>

(1) Bank loans: equipment loans over 5 years, fixed rate, secured by a hypothec on the universality of property.

(2) RISQ loan: the RISQ loans was considered to be patient capital, because it is uncollateralized. Moreover, although its repayment is fixed, it was granted to capitalize the co-operative and provide it with the means for its development. Finally, the terms of repayment can be revised according to the organization's income statement. RISQ is an organization investing in the social economy in Québec.</td><td>The RISQ loan is patient capital for two reasons:

• Unsecured loan

• The principal repayment can be revised according to the enterprise's income statement – RISQ loan.

Concerning preference shares, under Section 46 of the Co-operatives Act, the co-operative and its members have all the desired flexibility regarding redemption by the issuer, which allows them to consider the shares as equity.</td><td>Deduct the RISQ loan from long-term debt.

Add the RISQ loan to quasi-equity.

Deduct the preference shares from long-term debt.

Add the preference shares to equity.</td></tr>
</table>

Manufacturing Plus Cooperative
Interpretation of the balance sheet adjustment
As at December 31

	Note	Adjustment 2002				Adjustment 2001				
ASSETS		**Amount**	**To add**	**To deduct**	**Adjusted balance**	**Amount**	**To add**	**To deduct**	**Adjusted balance**	**Explanations**
Current assets										
Cash		21,573			21,573	10,560			10,560	
Investment		20,042			20,042					
Accounts receivable		13,004			13,004	20,408			20,408	
Inventory		20,429			20,429	23,833			23,833	
Prepaid expenses		4,490			4,490	5,344			5,344	
		79,538			**79,538**	**60,145**			**60,145**	
Fixed assets		**186,563**			**186,563**	**213,268**			**213,268**	
Total assets		**266,101**			**266,101**	**273,413**			**273,413**	
LIABILITIES										
Current liabilities										
Loan						25,000			25,000	
Accounts payable		20,325			20,325	25,188			25,188	
Deferred revenues		2,000			2,000					
Current portion of long-term debt		31,568			31,568	27,250			27,250	
		53,893			**53,893**	**77,438**			**77,438**	
Deferred grants	1	**10,465**		10,465	**0**	**14,651**		14,651	**0**	Deduct the non-repayable grants received for acquisition of fixed assets
Long-term debt	2	**134,646**		23,855	**69,236**	**162,423**		31,806	**92,853**	Deduct the RISQ capitalization loan
	2			36,555				32,764		Deduct members' preference shares
	2			5,000				5,000		Deduct participating preference shares
Total liabilities		**199,004**	**0**	**75,875**	**123,129**	**254,512**	**0**	**84,221**	**170,291**	
Quasi-equity										
Capitalization loan	2		23,855		23,855		31,806		31,806	RISQ loan reclassified as quasi-equity
Net equity (Equity)										
Participating preference shares	2		5,000		5,000		5,000		5,000	Reclassification of participating preference shares
Members' preference shares	2		36,555		36,555		32,764		32,764	Reclassification of members' preference shares
Members' equity		33,641			33,641	25,044			25,044	
Deferred grants	1		10,465		10,465		14,651		14,651	Reclassification of deferred grants for acquisition of fixed assets
Net surplus (deficit)		39,599			39,599	(10,120)			(10,120)	
Reserve		(6,143)			(6,143)	3,977			3,977	
Total net equity		**67,097**	**52,020**	**0**	**119,117**	**18 ,901**	**52,415**	**0**	**71,316**	
Total debt, quasi-equity and equity		**266,101**	**75,875**	**75,875**	**266,101**	**273,413**	**84,221**	**84,221**	**273,413**	

After adjustments as at December 31, 2002:

- Adjusted liabilities are $123,129 instead of $199,004.
- The fair value of co-operative equity after adjustment is $119,117 instead of an amount of $67,097 (net equity).
- Equity and quasi-equity represent an amount of $142,972 instead of an amount of $67,097 (net equity).

Here, after adjustments, is the adjusted balance of Manufacturing Plus Cooperative:

Manufacturing Plus Cooperative
Adjusted Balance Sheet
As at December 31

ASSETS	**2002**	**2001**
Current assets		
Cash	21,573	10,560
Investment	20,042	
Accounts receivable	13,004	20,408
Inventories	20,429	23,833
Prepaid expenses	4,490	5,344
	79,538	**60,145**
Fixed assets (Note 1)	**186,563**	**213,268**
Total assets	**266,101**	**273,413**
LIABILITIES		
Current liabilities		
Loan		25,000
Accounts payable	20,325	25,188
Deferred revenues	2,000	
Current portion of long-term debt	31,568	27,250
	53,893	**77,438**
Long-term debt (Note 2)	**69,236**	**92,853**
Total liabilities	**123,129**	**170,291**
Quasi-equity (Note 2)		
Capitalization loan	**23,855**	**31,806**
NET EQUITY (Equity)		
Participating preference shares	5,000	5,000
Members' preference shares	36,555	32,764
Members' equity	33,641	25,044
Deferred grants	10,465	14,651
Net surplus (deficit)	39,599	(10,120)
Reserve	(6,143)	3,977
	119,117	**71,316**
Total liabilities, quasi-equity and net assets	**266,101**	**273,413**

5.3.2

INCOME STATEMENT ADJUSTMENT: APPRAISAL OF THE CURRENT AND EXCEPTIONAL SURPLUS (DEFICIT)

The income statement adjustments are mainly to revenue sources. The social enterprise's revenue sources are examined in detail to determine whether they are progressing and, above all, whether they are recurring. Social enterprises mainly have three types of revenue:

- Sale of goods or services (which, in principle, are posted in the same way as for business corporations);
- Revenues from government contributions. According to the accounting principles (CICA), these revenues are posted as a contribution (NPO) or a grant (CO-OP).
- Other revenues not obtained directly from operations. For example, donations, interest income on investments, rental income, and sometimes a profit realized on the sale of fixed assets.

Concerning revenues from government contributions, the following question must be asked: are these revenues obtained from grants or programs for access to client services, or are they recurring revenues?

According to the Canadian Institute of Chartered Accountants (CICA) Handbook, financing of services offered to the public by the government is considered to be a contribution (for an NPO) or a grant (for a co-operative), and thus not current revenue in the strict sense of the term. Government revenues of domestic help enterprises, adapted work centres (AWC) and social insertion enterprises[10] are examples of revenue from services offered to the public and treated as a grant or a contribution in the financial statements.

It is important to mention that the government provides for the modes of presentation of revenue sources for the enterprises it is heavily involved in funding.

Revenues or grants

According to the RISQ's *Guide for analysis of social economy enterprises*, government assistance to social enterprises must be considered as recurring revenue, considered in turn as remuneration for a contract for services, if it fulfills the following conditions:

- The government assistance is tied to the organization's fundamental mission.
- The good or services are delivered at the market price.
- The assistance is recurring in nature.

[10] *These examples may vary in different Canadian provinces.*

In other words, government revenue sources will be reclassified, either as a grant (non-recurring) or as recurring revenue. This reclassification will have an impact on the ratio that determines the enterprise's self-financing and the appraisal of the operating surplus (deficit).

After reclassification, we can group the revenue sources as follows:

- Recurring revenues: obtained from the sale of goods or the provision of services, government revenues related to the mission, support campaign recurring each year in the same proportion, operating grants.
- "Exceptional" (non-recurring) revenues: grants obtained from external contributions, namely salary grants, social economy funds, etc.
- Other revenues: not obtained directly from operations. Example: interest income on investments, donations, rental income, and sometimes the profit realized on the sale of fixed assets.

In addition to evaluating the recurrence of revenue sources, the composition of the expenditures will also be determined in order to evaluate their degree of recurrence. Thus, the income statement, after adjustment, presents actual current operating revenues and expenditures, from which the social economy funders can deduce medium-term and long-term economic viability as the basis for their funding decision.

When the amount of funds generated is used to determine the capacity to meet financial commitments, it thus will be prudent to determine the current funds generated and calculate the coverage ratio of the debt to recurring operating items.

Adjustment of revenues and expenditures allows recognition of two levels of annual results:

- **After adjustment:** the current surplus (deficit), normally comparable from year to year.
- **Before adjustment:** the "exceptional" or final surplus (deficit), including non-recurring revenue and expenditure items, which cannot serve as a basis for analysis of future results.

For example, the income statement will be adjusted to determine the two types of surpluses (current and final) of CKOW Community Radio and Manufacturing Plus Cooperative.

Case 1: Example based on the income statement of CKOW Community Radio

CKOW Community Radio
INCOME STATEMENT
Year ended August 31

	2002	2001
REVENUES		
Sales and other revenues (Note 1)		
Advertising revenues	180,306	167,183
Support campaign	62,773	71,190
Dues	24,955	23,545
Antenna leasing	15,824	13,160
	283,858	275,078
Contributions and grants		
Ministère Culture et Communications (Note 2)	87,570	75,810
Ministère Culture et Communications (Note 3)	5,600	
Salary grants (Note 4)	12,466	26,886
Cultural Stabilization Fund (Note 5)	23,288	
Amortization – deferred contributions (Note 6)	2,073	2,073
	130,997	104,769
Total revenues	**414,855**	**379,847**
Production expenses		
Salaries and employer contributions	133,634	123,512
Technical material and supplies	14,360	20,270
Equipment maintenance and repair	2,891	2,499
Leasing of transmission lines	2,174	1,570
Copyrights	4,253	3,893
	157,312	151,744
Promotion expenses		
Salaries and employer contributions	69,083	71,229
Promotion and advertising	15,018	24,758
Related to the support campaign	30,886	22,924
Other	3,641	2,759
	118,628	121,670
Administration expenses		
Salaries and employer contributions	49,981	42,035
Rent	24,254	23,752
Professional fees (Note 7)	2,300	8,040
Electricity and heating	3,167	5,456
Office maintenance and repair	3,805	3,470
Office expenses	11,845	12,425
Amortization	6,947	10,622
	102,299	105,800
Financial expenses		
Bank charges and current interest	2,805	2,373
Interest on long-term debt	342	1,556
	3,147	3,929
	381,386	383,143
Net surplus (deficit)	**33,469**	**(3,296)**

The additional information in the community radio income statement and the adjustments to make are as follows:

Note	Details	Characteristic	Adjustment to be made
1	Sales are composed of recurring revenues, including the support campaign, recurring each year in the same proportion.	Revenues used for market activity.	Recurring revenue
2	An annual operating grant from the Ministère de la Culture et des Communications du Québec.	Recurring and related to the mission.	Recurring revenue
3	A grant from the Ministère de la Culture et des Communications du Québec for a special project of $5,600, which resulted in $4,900 of salary (temporary contract).	Related to the mission. Non-recurring.	Exceptional revenue and reduction of salary expenses.
4	A grant for employment unrelated to the organization's mission, but granted and renewed each year for an adapted promotion position for an amount of $12,466 in 2002 and $17,083 in 2001. In 2001, the organization received a job voucher of $9,803.	Not related to the mission. Not considered revenue.	Reduction of salary expenses. 2002: $12,466 2001: $17,083 Exceptional revenue of $9,803 (job voucher)
5	A non-recurring grant from the Québec Cultural Stabilization Fund intended to reduce previous deficits.	Related to the mission but not recurring.	Exceptional revenue, which should have been applied directly to net assets because of its nature.
6	Portion of the grant received for acquisition of equipment that appears under liabilities under long-term "Deferred contributions".	Not considered revenue. Not related to the mission.	Reduction of amortization expenditure.
7	In 2001, the enterprise hired a consultant for professional fees of $5,740 to produce a diagnosis of listenership and community support for alternative media.	Non-recurring expenditure.	To deduct from the professional fees expenditure.

CKOW Community Radio
Interpretation of the Adjustment of the Income Statement
As at August 31

	Note	2002 adjustment				2001 adjustment				
REVENUES		**Amount**	**To add**	**To deduct**	**Adjusted balance**	**Amount**	**To add**	**To deduct**	**Adjusted balance**	**Explications**
Recurring revenues										
Advertising revenues		180,306			180,306	167,183			167,183	
Support campaigns		62,773			62,773	71,190			71,190	
Dues		24,955			24,955	23,545			23,545	
Antenna leasing		15,824			15,824	13,160			13,160	
Ministère Culture et communications	2		87,570		87,570		75,810		75,810	Reclassification of the operating grant (recurring and related to the mission)
		283,858			**371,428**	**275,078**	**75,810**	**0**	**350,888**	
Grants										
Ministère Culture et communications	2	87,570		87,570	0	75,810		75,810	0	Reclassification of the grant as current revenue
Ministère Culture et communications	3	5,600		5,600	0				0	Reclassification as exceptional revenue
Salary grants	4	12,466		12,466	0	26,886		26,886	0	Reclassification as exceptional revenue
Stabilization Fund	5	23,288		23,288	0				0	Reclassification as exceptional revenue
Amortization – deferred contributions	6	2,073		2,073	0	2,073		2,073	0	Reduction of amortization
		130,997			**0**	**104,769**	**0**	**104,769**	**0**	
Total revenues		**414,855**	**87,570**	**130,997**	**371,428**	**379,847**	**75,810**	**104,769**	**350,888**	
EXPENDITURES										
Production expenses										
Salaries and employer contributions	3	133,634		4,900	128,734	123,512			123,512	Non-recurring expenditures
Material and supplies		14,360			14,360	20,270			20,270	
Maintenance and repair		2,891			2,891	2,499			2,499	
Line leasing		2,174			2,174	1,570			1,570	
Copyrights		4,253			4,253	3,893			3,893	
		157,312			**152,412**	**151,744**			**151,744**	
Promotion expenses										
Salaries and employer contributions	4	69,083		12,466	56,617	71,229		17,083	54,146	Salary grant reduction
Promotion and advertising		15,018			15,018	24,758			24,758	
Related to the campaign		30,886			30,886	22,924			22,924	
Other		3, 641			3,641	2,759			2,759	
		118,628			**106,162**	**121,670**			**104,587**	
Administration expenses										
Salaries and employer contributions		49,981			49,981	42,035			42,035	
Rent		24,254			24,254	23,752			23,752	
Professional fees	7	2,300			2,300	8,040		5,740	2,300	Non-recurring expenditures
Electricity and heating		3,167			3,167	5,456			5,456	
Maintenance		3,805			3,805	3,470			3,470	
Office expenses		11,845			11,845	12,425			12,425	
Amortization	6	6,947		2,073	4,874	10,622		2,073	8,549	Recurring grant reduction not related to the mission
		102,299			100,226	105,800			97,987	
Financial expenses										
Bank charges		2,805			2,805	2,373			2,373	
Interest on long-term debt		342			342	1,556			1,556	
		3,147			**3,147**	**3,929**			**3,929**	
Total expenditures		**381,386**	**0**	**19,439**	**361,947**	**383,143**	**0**	**24,896**	**358,247**	
Current surplus (deficit)		**33,469**	**87,570**	**111,558**	**9,481**	**(3,296)**	**75 810**	**79,873**	**(7,359)**	
Exceptional revenues (non-recurring grants)	3		5,600		5,600					Reclassification of non-recurring grant revenues
	5		23,288		23,288					
	4						9,803		9,803	
Non-recurring expenditures	3			4,900	(4,900)			5,740	(5,740)	Reclassification of non-recurring expenditures
Exceptional surplus (deficit)					**33,469**				**(3,296)**	

After adjustment as at August 31, 2002, the Community Radio recognizes two surplus or deficit levels:

- After adjustment: a current surplus (deficit) of $9,481.
- Before adjustment: an "exceptional" or final surplus (deficit) of $33,469, which must not be taken into account to assess the enterprise's future capacity to repay its debts.

CKOW Community Radio
ADJUSTED INCOME STATEMENT
Year ended August 31

	2002	2001
REVENUES		
Sales and other revenues		
Advertising revenues	180,306	167,183
Support campaigns	62,773	71,190
Dues	24,955	23,545
Antenna leasing	15,824	13,160
Ministère de la Culture et des Communications	87,570	75,810
Total revenues	**371,428**	**350,888**
EXPENDITURES		
Production expenses		
Salaries and employer contributions	128,734	123,512
Technical material and supplies	14,360	20,270
Equipment maintenance and repair	2,891	2,499
Leasing of transmission lines	2,174	1,570
Copyrights	4,253	3,893
	152,412	151,744
Promotion expenses		
Salaries and employer contributions	56,617	54,146
Promotion and advertising	15,018	24,758
Related to the support campaign	30,886	22,924
Other	3,641	2,759
	106,162	104,587
Administration expenses		
Salaries and employer contributions	49,981	42,035
Rent	24,254	23,752
Professional fees	2,300	2,300
Electricity and heating	3,167	5,456
Office maintenance and repair	3,805	3,470
Office expenses	11,845	12,425
Amortization	4,874	8,549
	100,226	97,987
Financial expenses		
Bank charges and current interest	2,805	2,373
Interest on long-term debt	342	1,556
	3,147	3,929
	361,947	358,247
Current net surplus (deficit)	**9,481**	**(7,359)**
Exceptional (non-recurring) revenues		
Ministère de la Culture et des Communications	5,600	
Salary grants		9,803
Stabilization Fund	23,288	
Non-recurring expenditures		
Salaries and employer contributions (promotion)	4,900	
Professional fees		5,740
"Exceptional" or final surplus (deficit)	**33,469**	**(3,296)**

Case 2: Example based on the income statement of Manufacturing Plus Cooperative

Based on the example of Manufacturing Plus Cooperative, the income statement will be adjusted to determine the two types of surpluses (current and final).

Manufacturing Plus Cooperative
INCOME STATEMENT
Year ended December 31

	2002	2001
REVENUES		
Sales and other revenues (Note 1)		
Grants	377,829	297,086
Salary grants (Note 2)	38,279	84,233
CLD grant (Note 3)		30,000
Amortization of deferred grants (Note 4)	4,186	4,186
Total revenues	**420,294**	**415,505**
Cost of goods sold		
Salaries and employer contributions	120,651	158,864
Purchases	98,920	78,560
Energy	5,682	5,498
Taxes and permits	4,235	3,283
	229,488	246,205
Gross earnings	**190,806**	**169,300**
EXPENDITURES		
Selling expenses		
Promotion and advertising (Note 3)	11,660	30,896
Travel and entertainment	5,620	4,616
Delivery expenses	2,772	2,560
	20,052	38,072
Administration expenses		
Salaries and employer contributions	23,200	22,440
Rent	22,291	19,716
Professional fees (Note 3)	5,605	9,554
Electricity and heating	9,738	8,747
Office maintenance and repair	5,665	9,604
Office expenses	13,345	14,597
Amortization	37,336	39,375
	117,180	124,033
Financial expenses		
Bank charges and short-term interest	3,086	5,269
Interest on long-term debt	10,889	12,046
	13,975	17,315
	151,207	179,420
Net surplus (deficit)	**39,599**	**(10,120)**

The additional information to the income statement of Manufacturing Plus Cooperative and the reclassifications and adjustments to be made are as follows:

Note	Details	Characteristic	Adjustment to be made
1	Sales are composed of revenues from commercial activities.	Recurring revenues from the organization's market activities.	Recurring revenue.
2	Salary grants to favour hiring of young workers and thus temporarily support the training time necessary for their full adaptation to the workstation.	Not related to the mission.	Reduction of employer contributions.
3	In 2001, the co-operative received a $30,000 grant from the CLD (the Centres locaux de développement in Québec, or Local Development Centres, are intermediate coaching organizations in entrepreneurship), one portion of which ($15,000) made it possible to implement a major promotional operation and another portion ($5,000) to pay an external resource person to establish the communication plan.	Non-recurring grant. Non-recurring expenditures.	Exceptional revenue of $30,000 and decrease in promotional expenditures ($15,000) and professional fees ($5,000).
4	Part of the grant received for acquisition of equipment, which appears under liabilities under the "Long-term deferred grants" heading.	Not considered a revenue. Not related to the mission.	Reduction of the amortization expenditure.

Manufacturing Plus Cooperative
Interpretation of the Adjustment of the Income Statement
As at December 31

	Note	Adjustment 2002				Adjustment 2001				
REVENUES		**Amount**	**To add**	**To deduct**	**Adjusted balance**	**Amount**	**To add**	**To deduct**		**Explanations**
Reccuring revenues Grants		377,829			377,829	297,086			297,086	
Salary grants	2	38,279		38,279	0	84,233		84,233	0	Reclassification as exceptional revenue
CLD grant	3				0	30,000		30,000	0	Reclassification as exceptional revenue
Amortization of deferred grants	4	4,186		4,186	0	4,186		4,186	0	Reduction of amortization expenditure
		420,294		**42,465**	**377,829**	**415,505**			**297,086**	
Cost of goods sold										
Salaries and benefits	2	120,651		38,279	82,372	158,864		84,233	74,631	Reduction of salary grant
Purchases		98,920			98,920	78,560			78,560	
Energy		5,682			5,682	5,498			5,498	
Taxes and permits		4,235			4,235	3,283			3,283	
		229,488			191,209	246,205			161,972	
Gross earnings		**190,806**		**38,279**	**186,620**	**169,300**		**84,233**	**135,114**	
Selling expenses										
Promotion and advertising	3	11,660			11,660	30,896		15,000	15,896	Non-recurring expenditure
Travel and entertainment		5,620			5,620	4,616			4,616	
Delivery expenses		2,772			2,772	2,560			2,560	
		20,052			**20,052**	**38,072**		**15,000**	**23,072**	
Administration expenses										
Salaries and benefits		23,200			23,200	22,440			22,440	
Rent		22,291			22,291	19,716			19,716	
Professional fees	3	5,605			5,605	9,554		5,000	4,554	Non-recurring expenditure
Electricity and heating		9,738			9,738	8,747			8,747	
Office maintenance and repair		5,665			5,665	9,604			9,604	
Office expenses		13,345			13,345	14,597			14,597	
Amortization	4	37,336		4,186	33,150	39,375		4,186	35,189	Reduction of recurring grant not related to the mission
		117,180			**112,994**	**124,033**			**114,847**	
Financial expenses										
Interest on long-term debt		3,086			3,086	5,269			5,269	
		10,889			10,889	12,046			12,046	
		13,975			**13,975**	**17,315**			**17,315**	
Total expenditures		**151,207**		**4,186**	**147,021**	**179,420**		**24,186**	**155,234**	
Current surplus (deficit)		**39,599**		**0**	**39,599**	**(10,120)**			**(20,120)**	
Non-recurring grants	3						30,000		30,000	Reclassification of non-recurring grant revenues
Non-recurring expenditures	3							20,000	(20,000)	Reclassification of non-recurring expenditures
Exceptional or final surplus (deficit)					39,599				(10,120)	

After adjustment as at December 31 2001, Manufacturing Plus Cooperative recognizes revenues and expenditures on the following basis:

- After adjustment: a current deficit of $20,120.
- Before adjustment: an "exceptional" deficit of $10,120.

Manufacturing Plus Cooperative
ADJUSTED INCOME STATEMENT
Year ended December 31

	2002	2001
REVENUES		
Sales and other revenues	377,829	297,086
Total revenues	**377,829**	**297,086**
Cost of goods sold		
Salaries and employer contributions	82,372	74,631
Purchases	98,920	78,560
Energy	5,682	5,498
Taxes and permits	4,235	3,283
	191,209	161,972
Gross earnings	**186,620**	**135,114**
EXPENDITURES		
Selling expenses		
Promotion and advertising	11,660	15,896
Travel and entertainment	5,620	4,616
Delivery expenses	2,772	2,560
	20,052	23,072
Administration expenses		
Salaries and employer contributions	23,200	22,440
Rent	22,291	19,716
Professional fees	5,605	9,554
Electricity and heating	9,738	8,747
Office maintenance and repair	5,665	4,554
Office expenses	13,345	14,597
Amortization	33,150	35,189
	112,994	114,847
Financial expenses		
Bank charges and short-term interest	3,086	5,269
Interest on long-term debt	10,889	12,046
	13,975	17,315
	147,021	155,234
Net surplus (deficit)	**39,599**	**(20,120)**
Exceptional (non-recurring) revenues		
CLD grant		30,000
Non-recurring expenditures		
Promotion and advertising		15,000
Professional fees		5,000
"Exceptional" surplus (deficit)	**39,599**	**(10,120)**

5.4

ANALYSIS OF THE ADJUSTED FINANCIAL STATEMENTS BY KEY RATIOS

There are about fifteen financial ratios that can be used for financial analysis. The purpose of the next exercise is to calculate and interpret the best-known ratios. However, it is important to examine the following points:

- The ratios can be grouped in three main categories:
  - Liquidity indicators: measure the enterprise's capacity to honour its financial commitments in the short term.
  - Financial stability (or debt) indicators: measure the share of borrowed capital in the financing of the enterprise and the financial burden weighing on the organization and determining its long-term solvency.
  - Management indicators: measure the efficiency with which the enterprise manages its resources, in view of its policies.
- Certain ratios are expressed in percentage terms, others in days, and still others represent a simple proportion.
- Since the ratios vary according to the time when they are calculated, the ratios must be used very prudently, especially when there are major fluctuations in sales that can influence the interpretation of certain ratios.
- The ratios are only indicators to find out the fundamental reasons for a favourable or adverse ratio. There must be a detailed analysis of the activities in question.
- A ratio inherently means nothing. To begin to mean something, this ratio must be placed in context and in perspective. For this purpose, it is necessary to produce a historical analysis of the balance sheet and the income statement, in order to compare the ratios obtained with what they were one year, two years and five years ago. A ratio is very useful to analyze the changes in the situation and see whether it is progressing or regressing. However, it does not indicate whether you are doing better or worse than other enterprises.
- You can also compare the ratios with similar enterprises. Certain sectors of the social economy, which are essential to a good diagnosis, have financial indicators.

5.4.1

INTERPRETATION OF THE BALANCE SHEET

Reading the adjusted balance sheet gives the answers to three questions:

- Does the organization have enough (CURRENT ASSETS MUST EXCEED CURRENT LIABILITIES)?
- How are the assets financed? By external funds (DEBT and QUASI-EQUITY) or by funds from the organization and its members, in the case of a co-operative (NET ASSETS)?
- What asset does the organization hold (NET ASSETS)?

Analyzing the liquidity ratios and the financial stability will let us answer these questions.

Liquidity indicators

Liquidity indicators show an enterprise's capacity to meet its current financial obligations. The following ratios are complementary indications of the organization's solvency, such as net working capital, working capital ratio, immediate liquidity ratio.

1 – Net working capital

Liquidity indicator

Net working capital is the most commonly used method to determine the status of an enterprise's liquidity (or solvency). It reveals the extent to which part or all of the enterprise's current assets is sufficient to cover its current liabilities, and even its daily operating expenditures. It is calculated by subtracting current liabilities from current assets.

It should be noted that current assets include assets that will be converted into cash within one year. Current liabilities include debts repayable within one year.

Net working capital is not necessarily a solvency indicator, as the following example shows:

	Enterprise A	Enterprise B
Current assets	\$100,000	\$20,000
Minus: current liabilities	\$90,000	\$10,000
Equals: Working capital	\$10,000	\$10,000

The current assets of enterprise A are five times higher than those of enterprise B, even though both organizations have \$10,000 of working capital. However, the current assets of enterprise B are twice as high as its current liabilities, while the current assets of enterprise A barely exceed its current liabilities. Enterprise B would be able to pay its debts, even if its current assets decreased by 50%. On the other hand, enterprise A would not have enough funds to pay its short-term debts if its current assets decreased by more than 10%.

To obtain a better measurement of the enterprise's solvency, it is preferable to calculate the working capital coefficient or working capital ratio.

Example: CKOW Community Radio

	In August 2002	In August 2001
Current assets	$46,535	$27,462
Minus: current liabilities	– 82,815	– 101,086
Negative working capital	(36,280)	(73,624)

The community radio station is in a position of current insolvency. In other words, it is unable to fulfill its current obligations. The radio station will have to replenish its working capital over the next few years, first with its generated funds or by calling on patient capital, to the extent that it shows its capacity to repay its new debts.

Example: Manufacturing Plus Cooperative

	In December 2002	In December 2001
Current assets	$79,538	$60,145
Minus: current liabilities	– 53,893	– 77,438
Net working capital	$25,645	$(17,293)

The co-operative's net working capital improved between 2001 and 2002. The analysis of the next two indicators (working capital and immediate liquidity) will allow a better assessment of the co-operative's solvency.

Key ratio	2 – Working capital ratio	Liquidity indicator

Equivalent terms

- Working capital coefficient
- General liquidity ratio
- Current solvency ratio
- Short-term debt ratio

This indicator establishes the ratio between current assets and current liabilities. This ratio is a better measurement of the enterprise's solvency than the net working capital expressed dollars.

If current assets exceed current liabilities, this means that the enterprise will generate liquid cash during the coming year to deal with its financial obligations. In this case, the working capital ratio will be greater than 1 and the enterprise will be solvent.

The higher the ratio, the higher the liquidity and consequently it is easier to settle the enterprise's obligations when due. However, too high a ratio may mean that the enterprise has too much inventory or that the accounts receivable collection period is too long.

Otherwise, the financial analysts estimated that current assets should be at least double current liabilities, but this interpretation was abandoned a few years ago when they found that such a ratio would not allow correct assessment of the enterprise's current financial position. The estimate of the working capital required may vary from one enterprise to another. It is necessary to account for the nature of its operations, the composition of its current assets and the rotation of some of its assets.

The nature of an enterprise's operations influences its working capital. For example, a cultural enterprise has no inventory and grants little credit to its customers, so sales revenue is collected faster and the enterprise has easier access to funds for payment of its short-term debts. This enterprise can operate with more modest working capital and could be in an excellent financial position, even though its working capital ratio is only 1. On the other hand, a ratio of 2 could be insufficient for a manufacturing co-operative that makes products with a relatively long production period, which means a long delay between purchasing of raw materials, production, sales of finished goods and, finally, cash inflows from sales. Consequently, this enterprise needs high working capital to finance its operations until it sells its finished goods.

The composition of the enterprise's current assets should also be considered. Normally, an enterprise with a considerable amount of cash, compared to its accounts receivable, inventory and grants receivable, can fulfill its obligations more easily when due than an enterprise with current assets composed mainly of accounts receivable, grants receivable or inventory. It must be realized that these accounts receivable and inventories must be converted into cash before the enterprise can settle its obligations.

Formula

$$\frac{\textbf{Current assets}}{\textbf{Current liabilities}}$$

Example: CKOW Community Radio

In August 2002	In August 2001
$\frac{46,535}{82,815}$ = 0.56 times	$\frac{27,462}{101,086}$ = 0,27 times

According to the Community Radio Station's balance sheet, it is recognized that the enterprise will have difficulty fulfilling its current obligations (ratio less than 1). However, the immediate liquidity ratio will give us a better solvency index.

Example: Manufacturing Plus Cooperative

In December 2002	In December 2001
$\frac{79,538}{53,893}$ = 1.48 times	$\frac{60,145}{77,438}$ = 0.78 times

Looking at the balance sheet of Manufacturing Plus Cooperative, we recognize a clear improvement of the working capital ratio at 1.5 to 1 (or 1.5:1). This means that each dollar of short-term debt is supported by $1.50 of current assets.

Key ratio	3 – Immediate liquidity ratio	Liquidity indicator

Equivalent terms

- Cash flow coefficient
- Liquidity index

This ratio is a more rigorous measurement of the enterprise's liquidity. Various components of current assets, particularly inventories and prepaid expenses, are less liquid or have little liquidity. Inventories can take several months before they are converted into finished goods and sold, and can sometimes be subject to loss of value and obsolescence. Moreover, the inventory appraisal may vary over time. Prepaid expenses are not future liquidity.

Also, you must not account for deferred revenues (or grants) of current liabilities, which are not future payments.

This is why it is necessary not to account for these items in determining the enterprise's actual current solvency.

Formula

$$\frac{\textbf{Current assets – inventories – prepaid expenses}}{\textbf{Current liabilities – current deferred revenues (or grants)}}$$

Example: CKOW Community Radio

In August 2002	In August 2001
$\dfrac{46{,}535 - 1{,}211}{82{,}815 - 33{,}000} = 0.91$ times	$\dfrac{27{,}462 - 2{,}109}{101{,}086 - 58{,}990} = 0.61$ times

It is recognized that the immediate liquidity ratio approaches 1 in 2002, mainly due to the deferred contributions item, which is not a debt that the enterprise must pay in the short term. A ratio of 1 is considered satisfactory.

Example: Manufacturing Plus Cooperative

In December 2002	In December 2001
$\dfrac{79{,}538 - 20{,}429 - 4{,}490}{53{,}893 - 2{,}000} = 1.05$ times	$\dfrac{60{,}145 - 23{,}833 - 5{,}344}{77{,}438} = 0.40$ times

Using only the co-operative's liquidity, that is, the items that can be converted into cash as quickly possible (cash, investments and accounts receivable), we find that the immediate liquidity ratio is 1.05, a very great improvement compared to 2001. A ratio of 1 is considered satisfactory.

Financial stability indicators

The financial stability indicators essentially seek to measure the materiality of the debt to the enterprise's financing. To some extent, they measure the financial risk incurred by the solidarity financial funders. Among these indicators, the debt ratio and debt coverage are the most popular.

Key ratio	4 – DEBT RATIO	Financial stability indicator

Equivalent terms

- Financing ratio
- Leverage

This tool is used extensively by funders to measure an enterprise's degree of long-term debt. It is necessary to adjust the enterprise's debt to consider patient capital or quasi-equity, in order to obtain a more accurate picture of this ratio.

It will be more used by social enterprises that have fixed assets and long-term debt.

Formula

$$\frac{\textbf{Long-term debt (adjusted)}}{\textbf{Equity (or net assets)}}$$

Example: CKOW Community Radio

In August 2002	In August 2001
$\frac{468}{37,820} = 1\%$	$\frac{1,944}{-45,088} = -4\%$

After the adjusted balance sheet, the radio station has practically no long-term debt.

Cautionary note!
Some investors or funders may consider "patient capital" loans different, so substantial differences may exist in the calculation of this ratio. It is very important that you always keep the same method for comparison.

Example: Manufacturing Plus Cooperative

In December 2002	In December 2001
$\frac{69,236}{119,117} = 58\%$	$\frac{92,853}{71,316} = 130\%$

The debt ratio greatly improved in 2002 and the enterprise shows better long-term solvency.

Key ratio	5 – EQUITY / (EQUITY + QUASI-EQUITY) RATIO	Financial stability indicator

This ratio allows assessment of patient capital as a share of the total “capital” available to the enterprise for its development. The greater the equity share, the more leeway the enterprise will have in looking for external “patient capital” to finance its development project.

Conversely, the smaller than equity share, the heavier the debt, even the patient debt, will weigh on the expenditures in terms of the company’s financial interest charges.

A ratio close to 50% allows a good balance between internal and external resources. However, it must be weighted according to the enterprise’s beneficiary capacity, as well as its stage of evolution (startup, consolidation, development, etc.).

Formula

$$\frac{\textbf{Equity}}{\textbf{Equity + Quasi-equity}}$$

Example: CKOW Community Radio

In August 2002

$$\frac{37{,}820}{37{,}820 + 32{,}000} = 54\%$$

In August 2001

$$\frac{(45{,}088)}{(45{,}088) + 0} = 100\%$$

In 2002, equity represents over 54% of the total of equity + quasi-equity, which is a good ratio.

Example: Manufacturing Plus Cooperative

In December 2002

$$\frac{119{,}117}{119{,}117 + 23{,}855} = 83\%$$

In December 2001

$$\frac{71{,}316}{71{,}316 + 31{,}806} = 69\%$$

In 2002, equity represents over 83% of the total of equity + quasi-equity, which is a very good ratio.

Key ratio	6 – FINANCIAL RATIO STRUCTURE	Financial stability indicator

This indicator determines the enterprise's financial structure according to the share of the assets provided by the creditors and the share provided by the enterprise's quasi-equity or by equity or self-financing.

Formula

Debt share: $\dfrac{\textbf{Adjusted total liabilities}}{\textbf{Adjusted total assets}}$

Quasi-equity (patient capital) share: $\dfrac{\textbf{Quasi-equity}}{\textbf{Adjusted total assets}}$

Equity or asset self-financing share: $\dfrac{\textbf{Equity}}{\textbf{Adjusted total assets}}$

In case of financial difficulties, the creditors prefer that the portion of the funds provided by equity and quasi-equity be high, because they will have to absorb the losses. The higher the equity, the higher the deficits can be before the creditors and the quasi-equity funders are exposed to losing their investment.

The Community Radio Station greatly improved its financial structure in 2002, presenting a better financial stability, the debt share accounts for 54% of total assets, the equity share 25% and the quasi-equity share 21%. In 2001, by comparison, the creditors completely funded the assets and accumulated deficits and the enterprise showed no long-term solvency.

The total assets of Manufacturing Plus Cooperative are financed 46% by the creditors, 9% by quasi-equity and 45% by equity, and show an improvement of the financial structure compared to 2001.

Example: CKOW Community Radio

	In 2002			In 2001		
Debt share:	83,283 / 153,103	=	54%	103,030 / 57,942	=	179%
Quasi-equity (patient capital) share:	32,000 / 153,103	=	21%	0 / 57,942	=	0%
Equity or asset self-financing share:	37,820 / 153,103	=	25%	(45,088) / 57,942	=	– 79%
Total			100%			100%

Example: Manufacturing Plus Cooperative

	In 2002			In 2001		
Debt share:	123,129 / 266,101	=	46%	170,291 / 273,413	=	62%
Quasi-equity (patient capital) share:	23,855 / 266,101	=	9%	31,806 / 273,413	=	12%
Equity or asset self-financing share:	119,171 / 266,101	=	45%	71,316 / 273,413	=	26%
Total			100%			100%

Key ratio	7 – DEBT COVERAGE	Financial stability indicator

Equivalent terms

- Debt service coverage ratio

This indicator assesses the sufficiency of the generated funds to repay the principal and interest on the long-term debt. This debt coverage ratio indicates the extent to which surpluses can decrease without putting the enterprise in an embarrassing financial position (with its financial institution, for example) as a result of its inability to pay its annual debts.

Formula

$$\frac{\textbf{Generated funds}}{\textbf{Annual principal repayable on the long-term debt}}$$

An enterprise's available generated funds include the surplus (deficit) for the year, adjusted to account for items involving no cash inflows or outflows, such as amortization. By adding the following items, we will obtain the funds generated for the year:

- Surplus (deficit) for the year.
- Plus: expenditures not involving cash outflows. Example: amortization of fixed assets.
- Minus: revenues not involving cash inflows. Example: amortization of deferred contributions on acquisition of fixed assets (grant received for acquisition of fixed assets amortized on the income statement over the useful life of the fixed asset).

The ratios are calculated based on the current or final (non-recurring) surplus (deficit). The Community Radio Station shows a debt coverage ratio, before adjustment, of 28.3 in 2002. In reality, it is 10.6, which is still excellent. It will be able to assume the new RISQ loan.

In the example of Manufacturing Plus Cooperative, in 2002, the debt service is covered 2.7 times, which is very good. In 2001, however, we find that the ratio was 1.02 before adjustment, whereas when calculated on the adjusted generated funds, it was really 0.6. This was a sign of serious problems, and the cooperative probably would have had some difficulty obtaining additional debt financing if it had not improved its generated funds in 2002.

Example: CKOW Community Radio

Calculation of generated funds	In 2002		In 2001	
	Year	Current (adjusted)	Year	Current (adjusted)
Net surplus (deficit)	33,469	9,481	(3,296)	(7,359)
Plus: amortization	6,947	4,874	10,622	8,549
Minus: amortization of grants (deferred contributions)	2,073	0	2,073	0
Generated funds	38,343	14,355	5,253	1,190
Debt coverage ratio	38,343 / 1,354 = 28.3	14,355 / 1,354 = 10.6	5,253 / 1,550 = 3.4	1,190 / 1,550 = 0.8

Example: Manufacturing Plus Cooperative

Calculation of generated funds	In 2002		In 2001	
	Year	Current (adjusted)	Year	Current (adjusted)
Net surplus (deficit)	39,599	39,599	(10,120)	(20,120)
Plus: amortization	37,336	33,150	39,375	35,189
Minus: amortization of grants (deferred contributions)	4,186	0	4,186	0
Generated funds	72,749	72,749	25,069	15,069
Debt coverage ratio	72,749 / 27,250 = 2.7	72,749 / 27,250 = 2.7	25,069 / 24,613 = 1.02	15,069 / 24,613 = 0.6

5.4.2

INTERPRETATION OF THE INCOME STATEMENT

The analysis of the income statement is particularly based on the following points:

- The revenues and expenditures for the financial year must be reasonable in relation to the organization's objectives and activities.
- The comparisons between the current year and the previous year make it possible to pinpoint trends and forecast changes in finances.
- The comparison of actual data and budget forecasts allows the organization to avoid straying too far from the initial budget. The variances require in-depth analysis to determine the causes and take corrective action or restore the situation.

The income statement expressed in percentages is useful to the enterprise's management because it shows the changes that have occurred that are not simply due to the positive or negative growth of recurring revenues. The income statement expressed in percentages allows horizontal and vertical analysis of the financial data, which shows the favourable or adverse trends. Horizontal analysis serves to examine the changes in various items over several periods (month, quarter, year). Vertical analysis expresses an item in terms of sales.

It is to the advantage of an enterprise's management to present a three-column income statement to the board of directors: one year back, the current year and the budget. A fourth column could also be added, the variance between the actual amount for the current year and the budget.

Obviously, the role of the directors of the social enterprise will be to know how to ask the treasurer or the management relevant questions to fuel decision-making. The presentation of these comparative statements risks raising more questions by the members of the board of directors if they contain major changes, differences or variances.

For the Community Radio Station, the enterprise's general performance improved between 2001 and 2002. The analysis allows better recognition of operations and highlights the following points:

- The radio station obtained a 5.9% revenue increase between 2001 and 2002, mainly coming from advertising sales. This radio station has existed for more than 15 years and has always been supported by the Ministère de la Culture et des Communications and by the community, as alternative media, which strengthens its position and allows the corresponding revenues to be considered as recurring.
- The increase in sales revenues explains the improvement of the income statements in 2002, and thus of generated funds.
- By adjusting the exceptional items, such as the temporary contract of employment in 2002 and the professional fees in 2001 (non-recurring expenditures), the Community Radio Station presents more consistent and comparable operating ratios. We can recognize that operating expenditures were well controlled. It even slightly reduced production expenditures (2.2%) and promotion expenses (1.2%) in relation to generated revenue in 2002.
- There was little variation of administration expenditures in relation to revenue in 2001 and 2002.

CKOW Community Radio
Analysis of the income statement by percentage

ADJUSTED INCOME STATEMENT			Horizontal analysis		Vertical analysis	
	2002	2001	Increase or (decrease)	% increase or (decrease)	2002	2001
REVENUES						
Sales and other revenues						
Advertising revenues	180,306	167,183	13,123	7.8%		
Support campaign	62,773	71,190	(8,417)	-11.8%		
Dues	24,955	23,545	1,410	6.0%		
Antenna leasing	15,824	13,160	2,664	20.2%		
Ministère Culture et Communications	87,570	75,810	11,760	15.5%		
Total revenues	**371,428**	**350,888**	20,540	5.9%	100.0%	100.0%
EXPENDITURES						
Production expenses						
Salaries and employer contributions	128,734	123,512	5,222	4.2%	34.7%	35.2%
Technical material and supplies	14,360	20,270	(5,910)	-29.2%	3.9%	5.8%
Equipment maintenance and repair	2,891	2,499	392	15.7%	0.8%	0.7%
Leasing of transmission lines	2,174	1,570	604	38.5%	0.6%	0.4%
Copyrights	4,253	3,893	360	9.2%	1.1%	1.1%
	152,412	151,744	668	0.4%	41.0%	43.2%
Promotion expenses						
Salaries and employer contributions	56,617	54,146	2,471	4.6%	15.2%	15.4%
Promotion and advertising	15,018	24,758	(9,740)	-39.3%	4.0%	7.1%
Related to the support campaign	30,886	22,924	7,962	34.7%	8.3%	6.5%
Other	3,641	2,759	882	32.0%	1.0%	0.8%
	106,162	104,587	1,575	1.5%	28.6%	29.8%
Administration expenses						
Salaries and employer contributions	49,981	42,035	7,946	18.9%	13.5%	12.0%
Rent	24,254	23,752	502	2.1%	6.5%	6.8%
Professional fees (Note 13)	2,300	2,300	0	0.0%	0.6%	0.7%
Electricity and heating	3,167	5,456	(2,289)	-42.0%	0.9%	1.6%
Office maintenance and repair	3,805	3,470	335	9.7%	1.0%	1.0%
Office expenses	11,845	12,425	(580)	-4.7%	3.2%	3.5%
Amortization	4,874	8,549	(3,675)	-43.0%	1.3%	2.4%
	100,226	97,987	2,239	2.3%	27.0%	27.9%
Financial expenses						
Bank charges and interest	2,805	2,373	432	18.2%	0.8%	0.7%
Interest on long-term debt	342	1,556	(1,214)	-78.0%	0.1%	0.4%
	3,147	3,929	(782)	-19.9%	0.8%	1.1%
	361,947	358,247	3,700	1.0%	97.4%	102.1%
Current net surplus (deficit)	9,481	(7,359)	16,840	228.8%	2.6%	-2.1%
Plus amortization	4,874	8,549				
Current generated funds	**14,355**	**1,190**				
Plus non-recurring grants	28,888	9,803				
Minus non-recurring expenditures	(4,900)	(5,740)				
Non-recurring surplus (deficit)	23,988	4,063				
Generated funds for the year	**38,343**	**5,253**				

Concerning Manufacturing Plus Cooperative, the analysis shows a substantial adjustment, essentially linked to the following factors:

- A 27% increase in sales between 2001 and 2002, due to the effective promotion operation launched in 2001 with the assistance of the CLD, among other reasons.
- Better employee productivity, after training of young workers, which should be maintained, if not improved, for the years ahead.
- Good control of expenditures by reduction of selling and administration expenses in relation to sales volume in 2002.
- The increase in sales and the reduction of administration and selling expenses allowed the co-operative to improve its results considerably in 2002, and thus its generated funds.

Manufacturing Plus Cooperative
Analysis of the income statement by percentage

ADJUSTED INCOME STATEMENT			Horizontal analysis		Vertical analysis	
	2002	**2001**	**Increase or (decrease)**	**increase or (decrease)**	**2002**	**2001**
REVENUES						
Total revenues	377,829	297 086	80,743	27.2%	100.0%	100.0%
Cost of goods sold						
Purchases	98,920	78,560	20,360	25.9%	26.2%	26.4%
Salaries & employer contributions	82,372	74,631	7,741	10.4%	21.8%	25.1%
Energy	5,682	5,498	184	3.3%	1.5%	1.9%
Taxes and permits	4,235	3,283	952	29.0%	1.1%	1.1%
	191,209	161,972	29,237	18.1%	50.6%	54.5%
Gross earnings	**186,620**	**135,114**	51,506	38.1%	49.4%	45.5%
EXPENDITURES						
Selling expenses						
Promotion and advertising	11,660	15,896	(4,236)	-26.6%	3.1%	5.4%
Travel and entertainment	5,620	4,616	1,004	21,8%	1.5%	1.6%
Delivery expenses	2,772	2,560	212	8.3%	0.7%	0.9%
	20,052	23,072	(3,020)	-13.1%	5.3%	7.8%
Administration expenses						
Salaries & employer contributions	23,200	22,440	760	3.4%	6.1%	7.6%
Rent	22,291	19,716	2,575	13.1%	5.9%	6.6%
Professional fees	5,605	4,554	1,051	23.1%	1.5%	1.5%
Electricity and heating	9,738	8,747	991	11.3%	2.6%	2.9%
Office maintenance and repair	5,665	9,604	(3,939)	-41.0%	1.5%	3.2%
Office expenses	13,345	14,597	(1,252)	-8.6%	3.5%	4.9%
Amortization	33,150	35,189	(2,039)	-5.8%	8.8%	11.8%
	112,994	114,847	(1,853)	-1.6%	29.9%	38.7%
Financial expenses						
Bank charges and interest	3,086	5,269	(2,183)	-41.4%	0.8%	1.8%
Interest on long-term debt	10,889	12,046	(1,157)	-9.6%	2.9%	4.1%
	13,975	17,315	(3,340)	-19.3%	3.7%	5.8%
	147,021	155,234	(8,213)	-5.3%	38.9%	52.3%
Current net surplus (deficit)	39,599	(20,120)	59,719	-296.8%	10.5%	-6.8%
Plus amortization	33,150	35,189				
Current generated funds	**72,749**	**15,069**				
Plus non-recurring grants		30,000				
Minus non-recurring expenditures		(20,000)				
Non-recurring surplus (deficit)	0	10,000				
Generated funds for the year	**72,749**	**25,069**				

5.5

ASSESSMENT OF CAPACITY TO MEET ITS FINANCIAL COMMITMENTS

The funds generated from the enterprise's operations determine your capacity to meet your financial commitments. The enterprise's capacity to honour its future obligations is the main financial factor analyzed for an investment project.

Thus, the generated funds must not only cover repayment of the current and future debt, but must also be sufficient to cover all of the following items:

- Repayment of the current and future principal of the debt.
- Replacement of the current assets.
- Purchase of new fixed assets.
- Redemption of co-operative shares and preference shares.
- Need for working capital necessary for development.

The enterprise will have internal or external financial resources to develop, ensure its sustainability and honour its financial obligations:

- Funds generated from operations (internal financing).
- Grants for acquisition of fixed assets (external funding).
- New term loans (external funding).
- New capitalization loans (external funding).
- Co-operative share and preference share issues (internal funding).

The combination of the above items will determine the enterprise's capacity to meet its financial obligations.

The following tables, still based on the examples of CKOW Community Radio and Manufacturing Plus Cooperative, illustrate how to analyze the financial structure in order to assess the changes in its liquidity, and whether the enterprise has leeway.

What is the meaning of changes in liquidity?

It is important to know the source of the funds and how they are utilized. For example, an enterprise that goes into debt 100% to pay for its equipment risks not being able to fulfill its obligations in the long term. However, an enterprise that pays down its financial commitments by using its internal financial resources (generated funds and financial participation of the members in the case of a co-operative) can obtain balanced financing.

A company's available generated funds include the surplus (deficit) for the year to account for items not involving any cash inflow or outflow, such as amortization, minus repayment of the current long-term loans and replacement of the current assets (e.g., replacement of computer equipment).

This table shows that the radio station used its generated funds and the grant to acquire new fixed assets. The radio station's working capital is clearly insufficient. To replenish its working capital, the enterprise called on patient capital through a new RISQ loan.

However, its remaining liquidity is still insufficient, because working capital is still negative. The radio station will have to replenish it in the next few years, first with its generated funds or by calling on patient capital, to the extent that it shows its capacity to repay its new debts.

CKOW Community Radio
Changes in liquidity

Calculation of generated funds	**2002**	**2003**
		Forecast
Surplus (deficit) for the year	33,469	
Plus: Amortization	6,947	
Minus: Amortization of deferred grants	(2,073)	
Plus: Gain on disposal of fixed assets	0	
Minus: Loss on disposal of fixed assets	0	
Generated funds	**38,343**	
Minus: Repayment of long-term debt	(1,354)	
Minus: Replacement of current assets	0	
Available generated funds	**36,989**	
Other resources from external funds		
Grants received related to acquisition of fixed assets	24,439	
RISQ loan	40,000	
TOTAL FINANCIAL RESOURCES (A)	**101,428**	
Investing activity		
Acquisition of new fixed assets	55,962	
TOTAL NEEDS (B)	**55, 962**	
Improvement (deterioration) of working capital (A minus B)	**45,466**	

In the case of Manufacturing Plus Cooperative, the funds generated in 2002 allowed it to repay its financial commitments (debts) and replace existing assets.

We saw previously that the co-operative needed $25,645 in additional working capital to deal with its current obligations. With the addition of financial resources from the members by issuing co-operative shares and preferred shares, the liquidity improved by $47,316, resulting in an acceptable working capital ratio.

Manufacturing Plus Cooperative
Changes in liquidity

Calculation of generated funds	**2002**	**2003**
		Forecast
Surplus (deficit) for the year	39,599	
Plus: Amortization	37,336	
Minus: Amortization of deferred grants	(4,186)	
Plus: Gain on disposal of fixed assets	0	
Minus: Loss on disposal of fixed assets	0	
Generated funds	**72,749**	
Repayment of long-term debt:		
Repayment of the RISQ loan	(7,951)	
Repayment of bank loan	(19,299)	
Forecast rebates		
Redemption of membership shares		
Redemption of preference shares		
Asset replacement	(10,641)	
Available generated funds	**34,928**	
Other resources from internal funds		
Issue of membership shares	8,597	
Issue of preference shares	3,791	
External		
New bank loan	0	
TOTAL FINANCIAL RESOURCES (A)	**47,316**	
Investing activity		
Acquisition of new fixed assets	0	
TOTAL NEEDS (B)	**0**	
Improvement (deterioration) of working capital (A minus B)	**47,316**	

Other factors are also analyzed, more specifically when assessing the repayment capacity of social enterprises. Here are some factors:

- degree of diversity of the clientele (not depend on only 2 or 3 customers);
- possibility that a grant, although non-recurring, can be repeated in a few years;
- level and evolution of gross margin (when applicable);
- payroll analysis and quality of conditions of employment;
- changes in workforce productivity;
- actual impact of an investment on the income statement;
- personality and competence of the executives;
- strength of the enterprise's roots in its community;
- comparison of results with enterprises in the same sector;
- capacity of the enterprise not only to cover its expenses but to create a reserve.

5.6

SUMMARY OF THE FINANCIAL ANALYSIS

The different ratios grouped in the tables on the following pages give CKOW Community Radio and Manufacturing Plus Cooperative a fairly good idea of their main strengths and weaknesses.

CKOW Community Radio

Concerning liquidity, the Community Radio Station is in a fair position and close to a satisfactory ratio, thus improving its current solvency in 2002 compared to 2001. Regarding debt, the radio station has strongly improved its financial structure thanks to the RISQ capitalization loan, which also explains the improvement of its current liquidity. Revenue growth, combined with control of production and promotion expenditures, has allowed the radio station to release satisfactory generated funds, thus reassuring RISQ about compliance with its long-term financial obligations.

While the above analysis by ratio gives a fairly good overview of the radio station's operations, it is nonetheless incomplete, in the sense that it does not account for one major factor: the time dimension. The ratios give an instant image of the enterprise at a specific point in time, but there may be trends. The radio station has been in operation for 15 years, and how have its ratios fluctuated over time? For example, have sales increased constantly over the years?

Summary of the financial performance of CKOW COMMUNITY RADIO

Financial indicators	Formulas	Definition	2002	2001	Interpretation
LIQUIDITY					
Net working capital:	Current assets minus current liabilities	Measures the enterprise's capacity to honour its current financial commitments (current solvency)	($36,280)	($73,624)	Unsatisfactory
Working capital ratio:	Current assets / Current liabilities		0.6 times	0.3 times	Unsatisfactory
Immediate liquidity ratio:	Current assets – inventories – prepaid expenses / Current liabilities – current deferred revenues (or grants)		0.9 times	0.6 times	Fair
FINANCIAL STABILITY					
Debt ratio:	Long-term debt / Equity (or net assets)	Measures the size of the debt in relation to quasi-equity (patient capital) and equity, debt service and long-term solvency	1%	-4%	Satisfactory
Equity/ (equity + quasi-equity) ratio:	Equity / (equity + quasi-equity)		54%	100%	Satisfactory
Financial structure Debt share	Adjusted total liabilities / Adjusted total assets		54%	179%	Satisfactory
Quasi-equity (patient capital) share:	Quasi-equity / Adjusted total assets		21%	0	Satisfactory
Equity share	Equity / Adjusted total assets		25%	-79%	Satisfactory
Debt coverage ratio by generated funds	Current generated funds (adjusted) / Annual principal repayable on the long-term debt		10.6 times	0.8 times	Satisfactory

Manufacturing Plus Cooperative

The co-operative's cash flow is in a very satisfactory position. The working capital and immediate liquidity ratios show us a very substantial improvement over 2001. The enterprise's financial structure is very well balanced, showing a good ratio between debt, quasi-equity and equity. All these factors reflect good financial health.

Summary of the financial performance of MANUFACTURING PLUS COOPERATIVE

Financial indicators	Formulas	Definition	2002	2001	Interpretation
LIQUIDITY					
Net working capital:	Current assets minus current liabilities	Measures the enterprise's capacity to honour its current financial commitments (current solvency)	$25,645	($17,293)	Satisfactory
Working capital ratio:	Current assets / Current liabilities		1.5 times	0.8 times	Satisfactory
Immediate liquidity ratio:	Current assets – inventories – prepaid expenses / Current liabilities – current deferred revenues (or grants)		1.05 times	0.4 times	Satisfactory
FINANCIAL STABILITY					
Debt ratio:	Long-term debt / Equity (or net assets)	Measures the size of the debt in relation to quasi-equity (patient capital) and equity, debt service and long-term solvency	58%	130%	Satisfactory
Equity/ (equity + quasi-equity) ratio:	Equity / (equity + quasi-equity)		83%	69%	Satisfactory
Financial structure Debt share	Adjusted total liabilities / Adjusted total assets		46%	62%	Satisfactory
Quasi-equity (patient capital) share:	Quasi-equity / Adjusted total assets		9%	12%	Satisfactory
Equity share	Equity / Adjusted total assets		45%	26%	Satisfactory
Debt coverage ratio by generated funds	Current generated funds (adjusted) / Annual principal repayable on the long-term debt		2.7 times	0.6 times	Fair

FINANCIAL PLANNING AND APPROPRIATE FINANCING

6.1

MAIN FUNDING SOURCES

In general, social enterprises do not like to use debt as a means of funding. To develop their business, the directors prefer self-financing to external funding.

In practice, given the directors' objectives (geared to the social profitability and sustainability of their activity), enterprises do not like long-term debt and instead resort to short-term debt. Regardless of their motivations, managers consider that the uncertainty regarding future profitability is the dominant factor in the decision to use short-term debt as a means of financing.

How do social enterprises use funding sources?

During startup, the social economy resorts to the following funding sources: first the community contribution, the funds invested by a co-operative's members (in membership shares and preference shares), social economy funds, grants, funds specific to the social economy and reinvested surpluses, if applicable. Regarding debt, the manager can benefit from expenditures payable, accounts payable and a line of credit secured by accounts receivable and inventories, to which a guarantee by a social economy investor can be added. Subsequently, external funding sources can be used, such as hypothecary loans, term loans secured by equipment and unsecured loans. When the enterprise is more stabilized, that is, when it generates surpluses, long-term loans from social economy investment funds or venture capital funds will come into play, particularly patient capital loans. However, sometimes social economy investors will get involved during startup.

Table 1 illustrates the different stages of development of enterprises, with the associated funding.

Table 1
Stage of an enterprise's development, with associated funding

Stage of development of a social enterprise	Financial structure	Proportion
1. Startup	Short-term debt: specially accounts payable	+ +
	Long-term debt: almost nonexistent	
	Quasi-equity: almost nonexistent	
	Equity: Community investment, Membership share issue (co-op)	+ + +
2. Enterprise	Short-term debt: accounts payable and bank loan (line of credit)	+ + +
	Long-term debt: secured term loan (3 to 5 years)	+ +
	Quasi-equity: almost nonexistent	
	Equity: accumulated surplus, Membership share issue (co-op) Preference share issue (co-op)	+ + - ++
3. Growth phase	Short-term debt: accounts payable and bank loan (line of credit)	- +
	Long-term debt: secured term loan (3 to 5 years)	+
	Quasi-equity: unsecured loan (5 to 10 years)	+ +
	Equity: accumulated surplus, Preference share issue (co-op)	+ + +
4. Mature enterprise	Short-term debt: accounts payable and bank loan (line of credit)	- -
	Long-term debt: secured term loan (3 to 5 years)	-
	Quasi-equity: unsecured loan (5 to 10 years)	+ +
	Equity: accumulated surplus, Preference share issue (co-op)	+ + +

Proportion: + + Growing, + Stable, - Decreasing

6.1.1

THE KEY TO SUCCESS: APPROPRIATE FUNDING

Social enterprises need funds to startup, expand, diversify their activities and modernize their facilities. Funding strategies exist to meet these asset needs and approach the various funding sources (lenders and investors).

The money that finances the enterprise is called capital. The bank loans authorized for an enterprise's day-to-day operations (working capital) have characteristics that distinguish them from the bank loans authorized for equipment purchases (fixed assets). There are also social economy investment funds for capitalization or development purposes. Their characteristics are also different from a term loan and a hypothec from a financial institution. A social economy development agent of a development support agency[11] can often help you find an effective combination of different types of capital. The figure below shows three different methods of financing an enterprise's assets.

Matched Scenario

The first scenario consists of synchronizing the funding sources with the financing needs, both short term (working capital) and long term (fixed assets). In other words, the term of the funding sources corresponds to the term of the financial needs.

High-Risk Scenario

The Achilles heel of enterprises is often their lack of liquidity. Social enterprises are often short of liquidity and thus are financially fragile. This shortage is often due to poor working capital management. It is caused in part by the desire of managers and directors for autonomy, meaning that they don't like to go into debt for the long term. Another reason is that financial intermediaries are prudent and grant few or no long-term loans. The shortage of permanent capital available for social enterprises and sales growth that requires a large quantity of available funds are some of the explanations for this situation. The enterprise thus finds itself in the following situation: long-term assets financed by current liabilities and low working capital that includes very little cash on hand and a high cost of financing. This increases the enterprise's financial risk. Indeed, fixed financial expenses increase because the cost of short-term financing via a line of credit is greater than the cost of long-term financing, given the underlying security of each mode of financing.

Sometimes enterprises that have growth at a fast and sustained pace for several years end up in a situation where a portion of their fixed assets is financed by a line of credit. They then are exposed to a clear risk related to renegotiation of financing agreements. Also, the line of credit loses its meaning and purpose, because no margin remains! The figure on the next page presents undercapitalized enterprises. The only remedy is new capitalization and refinancing.

Risky Scenario on the long term

Another scenario is to finance all funding needs on a long-term basis to avoid resorting to short-term financing. This strategy obviously requires long-term loans, quasi-equity and reinvestment of liquidity surpluses. This scenario can be risky, especially if the enterprise has little equity (equity or net assets) and a lot of long-term debt, because the organization can end up in long-term insolvency.

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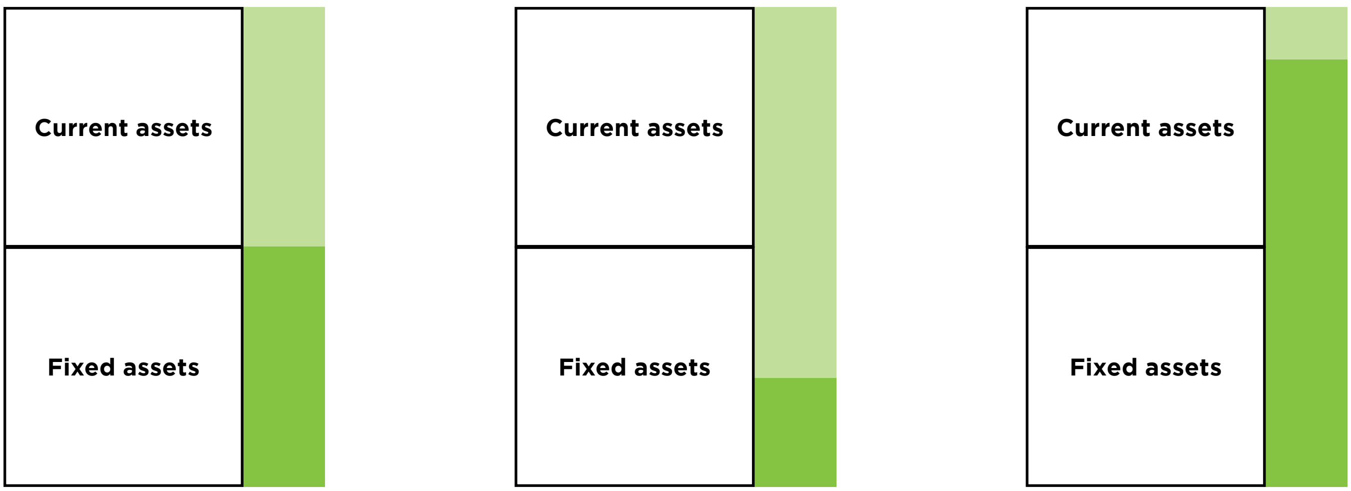
[11] In Québec: Local Development Centres (CLD), Corporation de développement économique et communautaire (CDEC), les sociétés d'aide au développement économique (SADC)

Figure 3
Different asset financing scenarios

Matched Scenario | **High-Risk Scenario** | **Risky Scenario on the long term**



Matching the life span of financing sources

Short-term financing is used for short-term needs

Long-term financing pays for fixed assets

Undercapitalized enterprise

This scenario is "mis-matched" because a large portion of long-term needs is funded by short-term financing

Highly capitalized enterprise

Long-term financing is used for working capital needs

This scenario is "mis-matched" because short-term needs are funded by long-term financing

Short-term debt financing (accounts payable, salaries payable, line of credit, short-term bank loan)

Long-term debt financing and equity or net assets (term loan, hypothecs, quasi-equity loan and accumulated surplus, membership share and preference share issues by co-operatives)

Source: Industry Canada, Strategis, "Where Buyers and Sellers Connect": http://www.strategis.gc.ca

6.1.2

EQUITY FUNDING

Equity funding is equivalent to the permanent capital an enterprise obtains, also known as equity (for a co-operative) or net assets (for an NPO). It is mainly obtained from members of a co-operative (preference shares held by the members or third parties), government agencies (capital grant), philanthropic investors and funders. No security is required and there is no obligation to repay the principal (future settlement is not time limited). There may be a capital cost (interest or rebate). An enterprise's accumulated surpluses also increase its equity.

The more equity the enterprise has, the more leverage it obtains to finance its development and growth through borrowing.

6.1.3

LONG-TERM PATIENT CAPITAL (QUASI-EQUITY) FUNDING

Quasi-equity funds, also known as patient capital, come from social economy investment funds for capitalization and development purposes.

These funds usually are unsecured and involve no special right to any assets of the enterprise. This frees up assets that must be used as collateral for loans (financing by a financial institution). Principal repayment is often flexible (fixed portion, variable portion) and its return may be variable, since both are tied to results, with a long-term maturity. There is a possibility of a principal repayment moratorium ranging from a few months to several years. However, the principal will have to be repaid.

The enterprise must submit a business plan, financial forecasts and a financial set-up to these funders. This often serves as leverage to obtain other types of financing (by borrowing).

6.1.4

LONG-TERM DEBT FINANCING

A long-term debt represents a loan with a projected repayment schedule and useful life of acquired property exceeding one year (e.g., building, computer equipment, machinery, office equipment, tooling, etc.). Long-term loans normally are secured first by the new property acquired (up to 65%), then by other uncommitted physical assets (for the remaining 35%), or failing this, by obtaining a loan guarantee. The lenders (generally financial institutions) grant loans to enterprises that show strong management capacity. A business plan must be submitted (including financial forecasts and a monthly cash budget), which shows the enterprise's capacity to repay its debts according to the loan repayment schedule. The financial institution expects the enterprise to have appropriate insurance to protect the assets.

The types of long-term loans are:

- Immovable hypothec: a loan (hypothec) for which the financing applies to the purchase or refinancing of land and buildings. A first hypothec is applied to the title of acquisition.
- Movable hypothec: a loan on assets other than land and buildings. A prior claim to the title is registered.
- Commercial pledge: this is an agreement similar to the movable hypothec, except that the property is transferred to the lender and the title remains in the borrower's hands, as in the case of bonds held by the bank.
- Note payable: This is a written promise to pay a sum of money specified to the lender, either on demand or on a given date.

In addition, some financial institutions recognize the specificities of social enterprises and collective entrepreneurship in their orientations or financial products.

6.1.5

SHORT-TERM DEBT FINANCING

Short-term loans are usually made in the form of term loans (less than one year) and renewable lines of credit. Lines of credit are mainly secured by accounts receivable (up to 75% of accounts receivable) and grants (up to 90% of grants receivable). Inventories can also be pledged as security. They finance the enterprise's working capital for its day-to-day activities, particularly employee salaries, inventory purchases and supplies.

6.1.6

LEVERAGE

Financial leverage reflects the enterprise's capacity to obtain other loans and investments. This is the ratio between debt financing, quasi-equity, and equity. A proportion of $6,000 of debt to $2,000 of equity (net assets) is known as a 3 to 1 debt ratio. In general, financial institutions prefer that a startup have a ratio of 2 to 1, and even 1 to 1.

6.1.7

FUNDING OF TECHNICAL SUPPORT

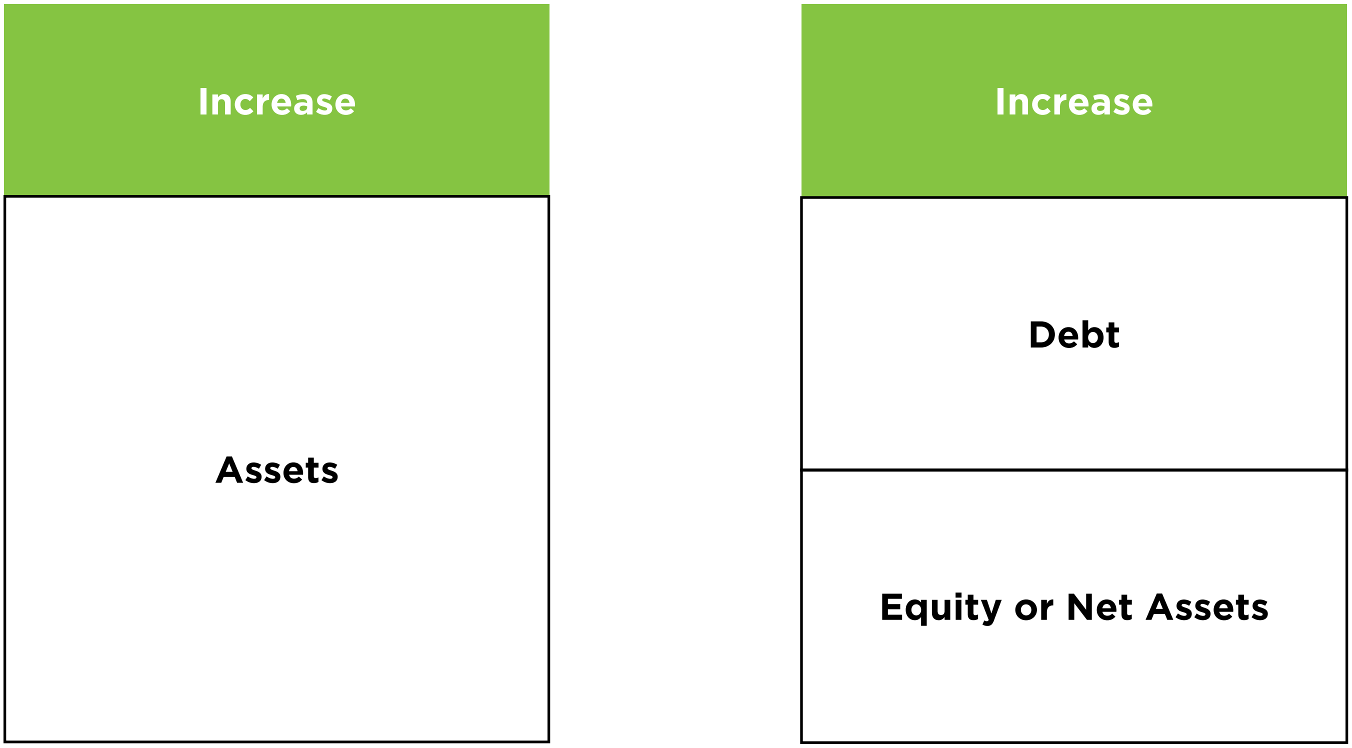
Technical support to conduct a specialized study (market study, feasibility plan) or prepare a business plan is often covered by specific funding. However, it can be noted that some organizations may offer funding through loans or non-repayable contributions of consulting services.

6.1.8

BALANCE BETWEEN DEBT AND INTERNAL FUNDING

Figure 4 on the next page shows an enterprise's typical balance sheet. This typical balance sheet shows that an enterprise's assets are financed by two main sources of funds: borrowing and equity (net assets).

Figure 4
Typical balance sheet



The increase in an enterprise's assets must be funded either by debt or by equity (generated funds and share issue in the case of a co-operative). Obviously, the left side of the balance sheet cannot grow faster than the right side.

Assuming that the enterprise is currently at a maximum (or desired) debt level, an increase in assets will require debt and quasi-equity (patient capital) to rise in proportion to equity or net assets to prevent the enterprise from becoming insolvent.

In the long term, the enterprise's growth is therefore directly related to the growth of its equity and quasi-equity. This equity can increase in two ways: by reinvesting surpluses or excess funds and by issuing new shares (in the case of a co-operative).

Quasi-equity (or patient capital) comes from social economy investment funds for capitalization or development purposes.

Any growth of the enterprise necessarily means that it is faced with financing needs that cannot be completely covered by internal sources and it necessarily will have to resort to external funding. The higher the growth, the greater the needs for negotiated funds. For social enterprises, this reality conditions all of their development, because they have less access than business corporations to the capital market. This is the source of the main justifications for governments to institute various assistance programs to fund social enterprises, through funds to assist capitalization of enterprises, co-operative investment legislation (provincial and federal), etc.

6.2

HOW TO ASSESS FINANCIAL NEEDS

Based on financial planning – that is, revenue and expenditure budgets, the capital budget and the monthly cash budget – the financial needs for funding growth can be estimated. The following are the four key factors to assess your financial needs:

- Working capital
- Acquisition of fixed assets (asset replacement, purchase of new fixed assets, etc).
- Marketing activities (advertising, promotion, development agent, etc.).
- Safety cushion

You must not neglect the safety cushion. Even if the necessary working capital and the fixed asset and marketing expenditures have been estimated carefully, the forecasts are never perfect. Your estimates may be too high or too low. It would be interesting to establish a realistic scenario and a pessimistic scenario, to set the level of the safety cushion that would be necessary if the baseline scenario does not materialize. The safety cushion makes it possible to avoid unpleasant surprises and you will tell the funders that additional capital contributions may be necessary.

Practical example: Development project

The development project consists of diversifying the activities to increase the clientele, and thus the revenue volume, and ensure the enterprise's long-term sustainability. For this purpose, the enterprise will have to be relocated and will need to expand its premises. An immovable property is acquired at a cost of $200,000, a communications officer is hired at an annual salary of $25,000, computer equipment is acquired for $5,000, and an advertising campaign is run, including design and printing of promotional material, at a cost of $15,000.

Moreover, according to the financial forecasts, $15,000 in working capital is needed, plus a $5,000 safety cushion.

Thus, the total cost of the development project is $265,000.

Capital to be mobilized

The challenge for the enterprise is to determine what portion of this $265,000 amount will come from:

- Internal sources (i.e., funds generated from operations, credit from suppliers)
- Government sources (salary grant, social economy development fund, etc.)
- External sources of conventional financing (i.e., line of credit, term loan and hypothecary loan from a financial institution)
- External sources from a social economy capitalization fund or unconventional funding (i.e., unsecured patient capital).

Project cost		**Project funding**		
		Short-term financing	**Long-term financing**	
		Generated funds, line of credit, grants	Traditional financing (term loan, hypothecary loan, leasing)	Capitalization fund (patient capital)
Fixed assets • Computer equipment • Acquisition of immovable	$5,000 $200,000		$114,000 (4)	$91,000 (5)
Marketing expenses	$40,000	$15,000 (1)		$25,000 (6)
Working capital	$15,000	$15,000 (2)		
Safety cushion	$5,000	$5,000 (3)		
Total	$265,000	$35,000	$114,000	$116,000
		(1) Investment (2) (3) Social economy fund	(4) Financial institution secured by the social economy lender	(5) (6) Social economy investors

MONITORING CHART

7.1

DEFINITION OF A MONITORING CHART

A monitoring chart is a system for measuring the enterprise's performance. It is a measurement information and summary document, oriented to control and decision-making. It must allow the person responsible, the manager and the directors to track the sensitive points of economic and social profitability, analyze situations, anticipate changes and react as quickly as possible. It is also a privileged communication tool for the organization's decision-making bodies and stakeholders. This tool must provide a summary but representative view of the enterprise and its operations.

The enterprise could also establish a slightly more forward-looking monitoring chart by seeking to determine not only past performances but the key factors of future performance. It is important to find coherence between the different axes to be targeted.

The monitoring chart thus is a management tracking tool that periodically displays a succinct set of indicators, covering the social enterprise's main functions.

Essentially, the monitoring chart has a limited number of financial and non-financial indicators, grouped around dimensions on which a social enterprise's sustainability and viability are based – for example, the financial aspect, operations, social purpose, human resources, democratic vitality, etc. For each dimension, the managers develop the most appropriate indicators to track the progress of performance according to the enterprise's strategic development.

The monitoring chart validates whether operations and the critical factors that influence them stand up to forecasts or objectives.

The monitoring chart is also an opportunity to illustrate the cause-and-effect relationships between social purpose and operational performance indicators and the financial results. It thus becomes a tool for an enterprise's stakeholders to understand its overall operations and an opportunity for training and transparency.

7.2

USEFULNESS OF THE MONITORING CHART FOR THE ENTERPRISE

The monitoring chart has proved its usefulness for all groups involved in the enterprise's success.

For employees and management: the monitoring chart as a management tool

If it contains relevant information for a given enterprise, the monitoring chart can allow:

- Observation of results;
- Control of expenditures;
- Compliance with budgets;
- Analysis of trends;
- Measurement of variances from forecasts;
- Assessment of risks;
- Tracking of the progress of a project or an activity;
- Triggering of various actions (meetings, audits, etc.).

Like an automobile monitoring chart, a business monitoring chart, if it is well documented and structured, has the following functions:

- Anticipate obstacles (alert, flashing lights);
- Guide the enterprise onto the right road with the best possible visibility (management indicators);
- Get to the right destination (compliance with objectives).

For the board of directors: the monitoring chart as a strategic tool

The monitoring chart has the advantage of being a tool that synthetically and visually represents the enterprise's position. Management thus can illustrate its presentation to the board of directors with this document and the directors can use it to make decisions with a better knowledge of the organization's strategic development.

For the enterprise's partners: the monitoring chart as a tracking tool

For funders and mentors, the monitoring chart is primarily a tool for tracking the enterprise. According to RISQ's *Guide for Analysis of Social Economy Enterprises*, "the purpose of the tracking function is to support the developer group in adjusting its project's parameters to the shocks of reality". Tracking therefore is performed primarily within a logic of prevention, support "for the entrepreneurial capabilities of the individuals and the group". In no case is it meant to be a means of control or a form of interference in the enterprise.

The real objective pursued by the technical and financial partners is to be able to detect the enterprise's difficulties in time, to be able to intervene before it is too late. The monitoring chart thus allows the enterprise to provide its partners with a better accounting of its situation, by drawing on their assistance more rapidly in case of a problem.

7.3

IMPORTANCE OF OVERALL TRACKING

The sustainability and success of social enterprises thus depend on a set of complex factors that influence each other. Beyond this complexity, the mission requires more than maximization of surpluses – it requires a demonstration of performance that goes beyond financial results as tracking tools.

Overall tracking thus is important to have a precise understanding of the enterprise's evolution and thus be better equipped to assess its situation and make adjustments, if required. This type of tracking can be of invaluable assistance in risk management and crisis prevention, as well as in the enterprise's decision-making process.

Tracking that focuses exclusively on economic and financial performance rarely makes it possible to prevent or eliminate a crisis. This analytical perspective alone does not account for other dimensions that are the basis of a social enterprise's sustainability and viability.

Indeed:

- Problems of democratic functioning (problems of cohesion, demobilization, conflict management, integration of new members, etc.) have repercussions on the enterprise's economic activities and social mission. On the other hand, an enterprise with strong democratic vitality and greater mobilization capacity can rely on this collective strength to overcome certain difficulties.
- In another vein, financial difficulties often are only the result of problems of management or operational efficiency.
- Moreover, governance of a social enterprise is a work in progress that involves constant learning, since democracy and its practice do not come any more naturally than managing a business. Just as a social enterprise must maintain and strengthen its entrepreneurial skills and competencies, it must also lay the foundations of its democratic functioning and develop its democratic culture.

7.4

IMPLEMENTING A MONITORING CHART

Implementing a monitoring chart is a unique opportunity for an enterprise. It is an ideal time to:

- Identify its critical success factors;
- Share its strategic vision with its partners;
- Adopt a training, awareness and motivation approach for its human resources.

This is an opportunity for analysis and pooling of knowledge that requires time-consuming and rigorous effort in its development to facilitate its use and maximize its usefulness. This design approach should be streamlined and carried out over a short period (about one month).

Monitoring Chart Construction Approach

1| Identify the enterprise's strategic dimensions or axes

Dimension
Dimension
Dimension
Dimension
Financial dimension

List the activities for each axis and establish the priorities

2| Choose the objectives

For each activity, determine the objectives to be achieved

3| Select the indicators

Determine the possible indices/indicators representative of the chosen activity status

Choose a limited number of indicators

Define the units of measure (data) attached to the indicator

4| Define the control indicators

Define the tolerance range for each indicator

5| Choose the modes of obtaining data

Choose the information sources

Formalize a manual or a dictionary of indicators

6| Format the monitoring chart

Construct the monitoring chart in an Excel spreadsheet (flag page, results page and graphic presentation page)

7| Use and maintain the monitoring chart

Collect data

Interpret the summary results

Define the corrective actions

Upgrade the monitoring chart

APPENDICES

CKOW Community Radio

BALANCE SHEET
As at August 31

	2002	2001
ASSETS		
Current assets		
Cash		2 772
Accounts receivable (Note 1)	25 324	22 581
Grants receivable	20 000	
Prepaid expenses	1 211	2 109
	46 535	27 462
Fixed assets (Note 2)	81 568	30 480
Intangible assets (Note 3)	600	600
	128 703	**58 542**
LIABILITIES		
Current liabilities		
Line of credit	2 424	
Accounts payable	37 915	40 742
Deferred contributions (Note 4)	33 000	58 990
Current portion of long-term debt	9 476	1 354
	82 815	101 086
Deferred contributions (Note 5)	36 490	12 051
Long-term debt (Note 6)	32 468	1 944
	151 773	**115 081**
Net assets		
Invested in fixed assets (Note 7)	43 134	15 131
Unallocated surpluses	(66 204)	(71 670)
	(23 070)	(56 539)
	128 703	**58 542**

CKOW Community Radio
CHANGES IN NET ASSETS
Year ended August 31

	Invested in fixed assets	Unallocated	2002	2001
Opening balance	**15 131**	**(71 670)**	**(56 539)**	**(53 243)**
Surplus (deficit) of revenues over expenses		33 469	33 469	(3 296)
Acquisition of fixed assets for the year	55 962	(55 962)	0	0
Grants received for acquisition of fixed assets for the year	(24 439)	24 439	0	0
Amortization of deferred contributions	(2 073)	2 073	0	
Principal payment of capital debt	(1 354)	1 354	0	0
Closing balance	**43 134**	**(66 204)**	**(23 070)**	**(56 539)**

CKOW Community Radio
INCOME STATEMENT
Year ended August 31

REVENUES	**2002**	**2001**
Sales and other revenues		
Advertising revenues	180 306	167 183
Support campaign	62 773	71 190
Dues	24 955	23 545
Antenna leasing	15 824	13 160
	283 858	275 078
Contributions and grants		
Ministère Culture et Communications (Note 8)	87 570	75 810
Ministère Culture et Communications (Note 9)	5 600	
Salary grants (Note 10)	12 466	26 886
Cultural stabilization fund (Note 11)	23 288	
Amortization - deferred contributions (Note 12)	2 073	2 073
	130 997	104 769
Total revenues	**414 855**	**379 847**
EXPENSES		
Production expenses		
Salaries and employer contributions	133 634	123 512
Material and technical supplies	14 360	20 270
Equipment maintenance and repair	2 891	2 499
Leasing of transmission lines	2 174	1 570
Copyrights	4 253	3 893
	157 312	151 744
Promotion expenses		
Salaries and employer contributions	69 083	71 229
Promotion and advertising	15 018	24 758
Related to the support campaign	30 886	22 924
Other	3 641	2 759
	118 628	121 670
Administration expenses		
Salaries and employer contributions	49 981	42 035
Rent	24 254	23 752
Professionals fees (Note 13)	2 300	8 040
Electricity and heating	3 167	5 456
Maintenance and repair of the premises	3 805	3 470
Office expenses	11 845	12 425
Amortization	6 947	10 622
	102 299	105 800
Financial expenses		
Bank charges and current interest	2 805	2 373
Interest on long-term debt	342	1 556
	3 147	3 929
	381 386	383 143
Net surplus (deficit)	**33 469**	**(3 296)**

	2002	2001
OPERATING ACTIVITIES		
Net surplus (deficit) for the year	33 469	(3 296)
Plus: amortization of fixed assets	6 947	10 622
Minus: amortization of deferred contributions	(2 073)	(2 073)
	38 343	5 253
Variation of non-working capital items	(50 662)	(2 461)
INVESTING ACTIVITIES		
Acquisition of fixed assets	(55 962)	
FINANCING ACTIVITIES		
RISQ loan	40 000	
Grants received for acquisition of fixed assets	24 439	
RISQ loan payment		
Term loan payment	(1 354)	(1 250)
	63 085	(1 250)
Cash at opening	2 772	1 230
Cash at closing	(2 424)	2 772

ADDITIONAL INFORMATION ON THE BALANCE SHEET

CKOW Community Radio is a non-profit organization, which has broadcast radio programs for the past 15 years. It was constituted according to Part III of the Québec Companies Act on March 2, 1978. The organization has the following mission:

Offer radio close to the community, with alternative cultural and information content, complementary to the commercial media and close to the neighbourhood's needs while enriching local cultural development.

Note 1- Accounts Receivable

Accounts receivable are composed of accounts receivable (advertising sales).

Note 2- Fixed Assets

Fixed assets do not include the value of $25,000 of equipment received as donations and validated by an appraisal report. It should be noted that according to accounting principles, an organization must account for all fixed assets received as donations, for which the market value is known.

Note 3- Intangible Assets

Intangible assets represent the acquisition of a licence for which the right to use has expired.

Note 4- Deferred Contributions (Current)

Deferred contributions correspond to an annual grant from the Ministère de la Culture et des Communications collected in advance of the next financial year, namely 4/12 for the period from September 1 to December 31, 2002.

Note 5- Deferred Contributions (Long-Term)

These are grants received for acquisition of fixed assets. At the end of August 2002, the organization received a new grant of $24,439, for the acquisition of transmitter equipment, which was added to the 2001 balance. Deferred contributions are amortized on the same basis as the annual fixed assets to which they apply are depreciated.

Note 6- Long-Term Debt

Long-term debt represents a balance of a term loan with the Caisse Desjardins for acquisition of equipment. This loan is secured by a movable hypothec on certain equipment. A new loan was contracted with the RISQ for the original amount of $40,000 without any guarantee (security interest), repayable over 5 years, in order to replenish the working capital and assist in development, following a diagnosis.

	2002	2001
Term loan (equipment purchase)	1 944	3 298
RISQ loan (working capital)	40 000	
	41 944	3 298
Current portion		
Term loan	1 476	1 354
RISQ loan	8 000	
	9 476	1 354
Long-term debt	32 468	1 944

Note 7- Net Assets Invested in Fixed Assets

The following table gives the composition of the net assets invested in fixed asset according to accounting standards.

	2002	2001
Fixed assets	81 568	30 480
Minus: Long-term debt for fixed assets	(1 944)	(3 298)
Grants deferred for fixed assets	(36 490)	(12 051)
	43 134	15 131

ADDITIONAL INFORMATION ON THE INCOME STATEMENT

Note 8- Grant from the Ministère de la Culture et des communications
An annual operating grant.

Note 9- Grant from the Ministère de la Culture et des communications
A $5,600 grant for a special project, which resulted in $4,900 of salaries (temporary contract).

Note 10- Salary Grants
This is a salary grant for an adapted position, renewed each year, but unrelated to the organization's mission. It should be noted that in 2001, the organization had also obtained a Bon d'emploi (job voucher) for a person employed in administration, which represented $9,803.

Note 11- Stabilization Fund
A non-recurring grant intended to reduce previous deficits.

Note 12- Amortization of Deferred Grants
This is the amortized portion of the grant received for acquisition of equipment, which appears in liabilities under "Deferred contributions" (long-term) (see Note 5).

Note 13- Non-Recurring Expenditures
Professionals fees:

In 2001, the organization engaged a consultant to produce a diagnosis of the listenership and community support for alternative media.

Cost of professional fees	$5 740

Manufacturing Plus Cooperative
BALANCE SHEET
As at December 31

	2002	2001
ASSETS		
Current assets		
Cash	21 573	10 560
Investment	20 042	
Accounts receivable	13 004	20 408
Inventories (Note 1)	20 429	23 833
Prepaid expenses	4 490	5 344
	79 538	60 145
Fixed assets	186 563	213 268
	266 101	**273 413**
LIABILITIES		
Current liabilities		
Loan		25 000
Accounts payable	20 325	25 188
Deferred revenues	2 000	
Current portion of long-term debt	31 568	27 250
	53 893	77 438
Deferred grants (Note 2)	10 465	14 651
Long-term debt (Note 3)	134 646	162 423
	199 004	**254 512**
Net equity		
Members' equity	33 641	25 044
Co-operative equity		
Net surplus (deficit)	39 599	(10 120)
Reserve	(6 143)	3 977
	67 097	**18 901**
	266 101	**273 413**

Manufacturing Plus Cooperative
Reserve
Year ended December 31

	2003	**2002**	**2001**
	Estimated		
Surplus (deficit) of revenues over expenditures for the previous year	39 599	(10 120)	(15 140)
Minus: Rebate	(5 000)		
Surplus (deficit) paid to the reserve	34 599	(10 120)	(15 140)
Deferred income taxes			
	34 599	(10 120)	(15 140)
Opening balance	(6 143)	3 977	19 117
Closing balance	**28 456**	**(6 143)**	**3 977**

Manufacturing Plus Cooperative
INCOME STATEMENT
Year ended December 31

	2002	2001
REVENUES		
Sales and other revenues	377 829	297 086
Grants		
Salary grants (Note 4)	38 279	84 233
CLD grant (Note 5)		30 000
Amortization – deferred grants (Note 2)	4 186	4 186
Total revenues	**420 294**	**415 505**
Cost of good sold		
Purchases	98 920	78 560
Production salaries and employer contributions	120 651	158 864
Energy	5 682	5 498
Taxes and permits	4 235	3 283
	229 488	246 205
Gross earnings	**190 806**	**169 300**
EXPENDITURES		
Selling expenses		
Promotion and advertising (Note 5)	11 660	30 896
Travel and entertainment	5 620	4 616
Delivery expenses	2 772	2 560
	20 052	38 072
Administration expenses		
Salaries and employer contributions	23 200	22 440
Rent	22 291	19 716
Professionals fees (Note 5)	5 605	9 554
Electricity and heating	9 738	8 747
Maintenance and repair of the premises	5 665	9 604
Office expenses	13 345	14 597
Amortization	37 336	39 375
	117 180	124 033
Financial expenses		
Bank charges and current interest	3 086	5 269
Interest on long-term debt	10 889	12 046
	13 975	17 315
	151 207	179 420
Net surplus (deficit)	39 599	(10 120)

Manufacturing Plus Cooperative
CASH FLOWS
Year ended December 31

	2002	2001
OPERATING ACTIVITIES		
Net surplus (deficit) for the year	39 599	(10 120)
Plus: Amortization of fixed assets	37 336	39 375
Minus: amortization of deferred contributions	(4 186)	(4 186)
	72 749	25 069
Variation of non-working capital items	(11 243)	(9 583)
INVESTING ACTIVITIES		
Acquisition of fixed assets	(10 631)	(6 763)
FINANCING ACTIVITIES		
Net variation of the current bank loan	(25 000)	25 000
Bank loan	0	
Issue of preference shares paid by the members	3 791	
Issue of membership shares	8 597	
Principal payment of the RISQ loan	(7 951)	(7 951)
Principal payment of the bank loans	(19 299)	(16 662)
	(39 862)	387
Cash variation	11 013	9 110
Cash at opening	10 560	1 450
Cash at closing	21 573	10 560

ADDITIONAL INFORMATION ON THE BALANCE SHEET

Manufacturing Plus Cooperative is a worker co-operative in the manufacturing sector. It was constituted under the Québec Co-operatives Act. Its purpose is to provide work to its members in the manufacturing field.

Note 1- Inventories

Inventories are composed of raw materials, finished goods, spare parts and supplies. Raw materials and finished goods are appraised according to the first in, first out method, while spare parts and supplies are appraised according to the average cost method.

Note 2- Deferred Grants

These are grants received for acquisition of fixed assets. The deferred grants are amortized on the same basis as the fixed assets to which they apply are depreciated. The amortization thus calculated becomes a revenue in the income statement for each financial year.

Note 3- Long-Term Debt

	2002	**2001**
1. Caisse Desjardins, movable hypothec 2000	92 853	112 152
2. Caisse Desjardins, movable hypothec 2002		
3. RISQ loan (capitalization)	31 806	39 757
4. Preference shares paid by the members	36 555	32 764
5. Participating preference shares	5 000	5 000
	166 214	189 673
Current portion		
Bank loan 1	23 617	19 299
Bank loan 2		
RISQ loan	7 951	7 951
	31 568	27 250
Total long-term debt	134 646	162 423

1. Bank loan: equipment loan over 5 years, fixed rate, secured by a hypothec on the universality of property.

2. RISQ loan: the RISQ loan was considered patient capital, because it has no security interest. Moreover, although its repayment is fixed, it was granted to capitalize the co-operative and provide it with the means for its development. Finally, the terms of repayment may be reviewed on the basis of the organization's results.

ADDITIONAL INFORMATION ON THE INCOME STATEMENT

Note 4- Salary Grants

Non-recurring salary grants were received in 2001 and 2002 to favour hiring of young workers and thus temporarily support the training time necessary to adapt fully to their new workstation.

Note 5- CLD Grant (Centre local de développement au Québec)

In 2001, a non-recurring CLD grant of $30,000 was received, one portion of which ($15,000) allowed the implementation of a major promotion campaign, which another portion ($5,000) served to pay an external resource to establish the communications plan.

GLOSSARY

The definitions in the glossary are derived from *Une économie à valeurs ajoutées – Compréhension des états financiers d'une entreprise d'économie sociale,* produced by Chantier de l'économie sociale.

Accounts payable
Common definition: expenses which must be charged to the current financial year, but which will be paid during the next financial year.

Accounts receivable
Common definition: revenues that must be applied to the current financial year, but that will only be received in the next financial year. Note: the services were rendered in the current financial year.

Anchoring
See Grounded in the community

Annual budget
The budget, prepared annually, serves to illustrate the enterprise's revenue and expenditure forecast for the coming financial year.

Assets
Assets represent all of the financial resources used by the organization to achieve its own ends, namely all the securities and all the goods owned.

Audited financial statements
The audited financial statements have been reviewed by an independent public accountant, who certifies that they are faithful and that the users can accept their figures without danger. The audit is conducted according to the auditing standards dictated by the Ordre des comptables agréés du Québec.

Auditors' report
The auditors' report certifies that the financial statements present faithfully: the position of the organization (by the balance sheet), the result of its operations (by the statement of revenues and expenditures) and the changes in financial position (by the statement of cash flows). The audit is conducted according to generally accepted auditing standards.

Balance sheet
The balance sheet is a financial statement which sets out the financial position of an enterprise as at a given date, and in which are presented the assets and liabilities and the difference between these items, which corresponds to equity.

Capital
Finance: means of financing used by the enterprise to acquire its long-term assets. Permanent capital essentially includes equity, long-term deferred contributions (or grants) and long and medium-term borrowing.

General accounting: capital means the excess of assets over liabilities.

Capital structure
Financing of the enterprise represented by long-term debt, preferred shares (for a co-operative), deferred contributions, grants or subsidies, and equity (net assets or the co-operative's equity).

Chartered accountant (CA)
The chartered accountant mainly specializes in the following fields of expertise: financial and administrative accounting, auditing, taxation, business law, insolvency, etc. The audit function is performed by independent chartered accountants, meaning that they deal at arm's length with the enterprise. They are not all in-house, given the existence of many public accounting firms.

Chartered general accountant (CGA)
The CGA's main areas of expertise are management, finance, marketing, economics, personnel management, organizational behaviour, etc. The CGA often acts as an advisor in an enterprise.

Chartered management accountant (CMA)
Most CMAs carry on their activities in the private or public sector. They offer guidance in management accounting and have a mission to research the needs of internal users of financial data.

Collective
This term refers to a community-based group of persons and, by extension: collective approach, collective initiative, collective entrepreneurship. The group is the decision-making body.

Contributions
Transfer WITHOUT CASH OR OTHER CONSIDERATION to an NPO (the funds provided to an NPO by an administration are considered to be contributions. Usually all grants and subsidies are classified in these contributions, regardless of whether or not they are conditional on an activity or a service.

Community action organizations (community action agencies)
(associations, charitable organizations, non-governmental organizations)
The services and products offered are not part of a market economy because they are not priced or impossible to price. These organizations are not required to apply the entrepreneurial philosophy in their management mode: self-financing or user-pay are not necessarily part of the organizations' strategies and orientations. "Community action" organizations, whose mission has a priority focus on social and political action (social change, defence of rights, helping people, etc.) are part of this group.

Co-operative
A co-operative (a mutual) is an autonomous association of persons, voluntarily joined together to satisfy their common economic, social and cultural aspirations and needs, by means of a collectively owned enterprise in which power is exercised democratically.
(source: http://www.coopquebec.coop/site.asp?page=element&nIDElement=2259)

Disbursement
A disbursement is a cash outflow that must not be confused with operating expenses or expenditures. For example, a principal repayment on a loan is a disbursement but not an operating expenditure.

Endowment
Type of contribution encumbered with a restriction of external origin whereby the organization is bound to maintain the allocated resources permanently (example: a foundation).

Equity
General accounting: Participation of the members (of a co-operative), government bodies (infrastructure grant, capital grant), philanthropic investors and/or donors of a social economy enterprise in that enterprise's assets.

Expenditures (expenses)
Expenditures are the sums paid or payable by the corporation for the current financial period. They may involve a sum committed but not yet disbursed.

Financial services co-operative
A financial services co-operative is a legal person bringing together persons who have common economic needs and who, in order to satisfy these needs, associate to form a deposit and financial services institution
(source: http://www2.publicationsduquebec.gouv.qc.ca/dynamicSearch/telecharge.php?type=2&file=/C_67_3/C67_3.htm)

Financial year
Generally, the financial year or accounting year is a one-year period. It should be chosen according to the enterprise's calendar of operations. The financial statements are presented according to this financial year.

Government corporations (public enterprises or Crown corporations)
Entity wholly owned, directly or indirectly, by the Government, providing a commercial service (goods or services) considered to be in the general interest and whose management pursues a general objective of profitability. Sometimes called "public enterprises" in Québec, or Crown corporations in the rest of Canada, government corporations or Crown corporations are public structures and their organizational and operational modalities are governed by a specific constituting act.
(source: http://www.etatquebecois.enap.ca/fr/index.aspx?sortcode=1.3#S)

Grounded in the community (community mobilization – strategic networking)
It is defined by the ties between the organization and its environment, its community, its territory, its sector of activity.

Income statement
See "Statement of revenues and expenditures"

Internal profitability
The enterprise generates more revenues than expenditures.

Liabilities
Liabilities can be defined simply as all of the sums owed by the enterprise to third parties.

Mutual
Voluntary collective insurance enterprise based on a system of reciprocal commitments whereby the members of a group combine their efforts and, in consideration of periodic dues, insure themselves against certain risks (illness, accidents, etc.) by guaranteeing themselves the same benefits and excluding any idea of profit.
(source: http://www.coopquebec.coop/site.asp?page=element&nIDElement=2286)

Net assets (non-profit equity)
In an enterprise, owners' equity is defined as the sums that the owners invest in the enterprise (initial investment), plus the earnings realized and not distributed to these owners. In the vast majority of NPOs, net assets, formerly known as "non-profit equity", only consist of the amounts invested in the organization and the total of the accumulated surpluses (or cumulative losses) annually since its constitution. Equity corresponds to the difference between assets and liabilities. On the financial balance sheet, equity plus liabilities equals total assets.

New accounting standing applies to NPOs since April 1, 1997 (see the Canadian Institute of Chartered Accountants Handbook). According to one of these standards, the balance sheet must present:

Net assets invested in capital assets;
Net assets which, due to restrictions, must be retained permanently (i.e. endowments);
Other restricted net assets;
Unrestricted net assets.

Net earnings (excess of revenues over expenditures)
Net earnings for a financial year is defined as the excess of total revenues over total expenditures. If the expenditures are greater than the revenues, the difference is then called a "deficit" or insufficiency of revenues over expenditures.

Non-profit organizations (non-for-profit agencies)
They are considered to be one of the vectors of local development, particularly for their impacts on the employment situation in their community. They sometimes choose activities with limited financial profitability or profitable sectors that they manage with different redistribution modes. The State may intervene in these organizations on an ad hoc or recurring basis as a "client" of the service provided to the community.

Notice to reader
The notice to reader is prepared by the public accountant who compiles the data provided by the organization. This work is characterized by the absence of audit and review of the financial statements.

Patient capital in the social economy
Finance: Venture capital invested for the long term. These funds are usually unsecured and do not included any particular right to any assets of the enterprise (no security). Principal repayment is often flexible and the return on capital may be variable, since both are linked to the bottom line.

Private enterprise
One of the forms of private enterprise is defined as a legal person with an autonomous existence distinct from its shareholders. Its purpose is to generate earnings and distribute them among the shareholders (business corporation).

An enterprise may also be individual, with the purpose of generating profits for the sole proprietor who owns the assets (sole proprietorship).
(source: http://www2.gouv.qc.ca/entreprises/portail/quebec/creer?lang=fr&g=creer&sg=&t=s&e=3733407055

Public enterprises
See Government corporations

Proceeds
See "revenues"

Quasi-equity
See "patient capital in the social economy"

Receipts
A receipt is an inflow in cash or cheques. Receipts and revenues must not be confused, because in many cases, receipts are all the payments received, which are not always proceeds or revenues. For example, the receipt of a bank loan is not considered to be a revenue and does not constitute enrichment.

Restriction
An obligation imposed on an organization to use resources in a prescribed manner.

Retained earnings
The term "retained earnings" means retained earnings in the form of dividends or earnings invested in the company.

Revenues (proceeds)
Revenues are the sums received by the organization in compensation for services rendered. They may be a sum receivable with certainty but not yet received. For example, a sum promised by a sponsor, for three years, under a contract or remuneration for the sale by the enterprise of its products and services to individuals or corporations or the government.

Social enterprise (social economy enterprise)
This is an **association of persons**, joined together in a democratic framework, sharing values of solidarity and sustainable develop to achieve this common objective together. This is the meaning of the social mission. It is also **an enterprise**, which develops economic activities within the context of a competitive market by producing and selling goods and services, but **with the rationale of enabling the association to accomplish its mission**.

Social profitability or social usefulness
The enterprise's activities have an impact and positive effects on the community, which do not necessarily translate into monetary terms on its books, nor into a quantifiable monetary impact on the national, regional or local economy.

Statement of cash flows
The objective of the statement of cash flows is to provide information on the origin of the organization's funds and how it uses these funds to carry on its operating, financing and investing activities. The statement of cash flows helps the users of the financial statements assess the organizations' capacity to obtain funds from internal and external sources in order to provide its services and fulfill its obligations. The information provided in this statement also helps the users of the financial statements assess the manner in which the resources were entrusted to it. The statement of cash flows can also be called the "statement of source and use of funds" or the "statement of changes in financial position".

Statement of changes in net assets
The statement of changes in net assets must present the variations that have occurred in the following net assets:

a) net assets invested in capital assets;
b) net assets which, due to restrictions, must be retained permanent as endowments;
c) other restricted net assets;
d) unrestricted net assets;
e) total net assets.

The statement of changes in net assets indicates the measure by which the organization's activities have resulted in an increase or a decrease in the net assets presented in the balance sheet.

The statement of changes in net assets may be combined with the income statement.

Statement of receipts and disbursements
The statement of receipts and disbursements considers only the sums actually received and disbursed and disregards the expenses payable and amounts receivable. It indicates the funds available at the beginning of the period, the receipts and disbursements for the period, and the balance available at the end of the period.

Statement of revenues and expenditures
The statement of income and expenditures (income statement, or statement of income and expenditures) serves to show the results of the enterprise's operations during a given period, generally one year. It indicates the revenue sources, how these revenues are spent and the excess (insufficiency) of revenues over expenditures.

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