

# [Non-profit organization finances and pricing](https://assignbuster.com/non-profit-organization-finances-and-pricing/)

The Global Alliance for TB Drug Development (TB Alliance) is a non-profit organization which uses its revenues to develop new, simpler, faster-acting TB drug regimens [1] rather than distributing those profits to its shareholders and board of directors. [2] It is also a PDP (product development partnership) that operates like a biotechnology firm creating collaborations between the private, public, academic, and philanthropic sectors to drive the development of new TB drugs for developing countries using various licensing and partnership agreements. In this way risk and incentives are shared between the partners. TB Alliance manages the various projects although the laboratory experiments and clinical studies are performed by external partners. Donors include private foundations, governments, multilateral donors including the Bill & Melinda Gates Foundation, the European Commission, the Global Health Innovative Technology Fund, Irish Fund, National Institute of Allergy and Infectious Disease, UK AID, UNIT AID, United States Agency for International Development, and the US Food and Drug Administration. [3] As a corporation, TB Alliance has to maintain legal status and reporting functions by filing reports with federal, state and local authorities. However, they have to demonstrate “ no profit” and show how the money was utilized by submitting a Form 990 to the Internal Revenue Service (IRS) to keep their tax-exempt status. [4] The financial position for non-profit research based organization is important because it is funded by various donors. The board of directors and management of TB Alliance are accountable for how the money is spent for research, administrative activities, and production of new, faster-acting and affordable TB drugs.

Ratios to Measure the Financial Position of an Organization: An efficient measure which could analyse the trends and financial position of the organization over a period of time is the ratio analysis. Ratio analysis is a gauge which indicates the organizational financial performance.[5]Management of a non-profit organization uses ratio analysis in order to highlight the flaws and strengths of various strategies on the basis of which plans could be shaped. Funders or private donors of the organization can use the ratio analysis to measure the efficiency and effectiveness of the projects and make decision about management’s performance.[6]

The assessment of financial condition of non-profit organization starts with the evaluation of financial reports.[7]Various ratios are there to analyse the financial position of organization but a ratio is more useful if it is consistent in nature over time and measure the precise financial information.[8]We normally look at the published annual reportshttp://www. tballiance. org/annualreport/and review their financial position and look for any red flags. We make sure their cash position is good relative to the annual operating income, and their equity / net assets are reasonably positive. We also make sure that any grant or investment we give is not a huge percentage of their annual budget. [9]

There are eleven ratios identified by Non Profit Assistance Fund which could be used by a non-profit research based organization which is funded by private donors.[10]

There are 5 Balance sheet ratios which could be used by a non-profit organization:

1. Debt ratio: It is used to examine how much organization is relying on other people debts and how much cushion there is for the company. It is calculated by dividing total debt to total net assets.[11]
2. Current ratio: Current ratio is current assets to current liabilities and it identifies the ability of the organization to pay its debts on time. It is a measure which tells about the cash flow in near future.[12]
3. Days cash on hand: It is cash and current investments to daily cash requirement and helps to identify the amount of operating cast required by organization. It is helpful as it tells about the unrestricted cash available to the organization.[13]
4. Accounts receivable aging: Account receivable aging ratio is important because it helps to identify all those bills which have become older and are aberrant. This ratio identifies the cash flow problems of the non profit organization. It consists of all the accounts payable overdue for more than 90 days to total accounts receivable.[14]
5. Accounts payable aging: It is all the accounts payable over due for more than 90 days to total accounts payable. It specifies the cash flows problems related to payments and serve as a tool for several financial problems.[15]

There are 3 expense ratios which are important for a non-profit organization as donors will need to examine the expense incurred and these are:

1. Personnel costs ratio: It indicates the expense incurred on the human resource of the organization and tells how much budget is allocated for staff. It is the total wages to total expense.[16]
2. Administration cost ratio: It is the total general and administrative expense to total expense. It is very helpful for the donors who regularly examine the expenses of company over time.[17]
3. Fundraising efficiency: It is the income contributed to fundraising expense. As the organization raise funds from private donors it’s important to know each dollar which is being raised from the contribution by incurring expense on fundraising . [18]

There is 1 ratio related to income statement: Reliance ratio . This ratio helps to identify the major source of income which is utilized by the organization for income. It highlights major activities which help to increase organizations income and it is the largest income source to total income.[19]

Contracts and Its Affect on Provider Behaviour: Private donors can use Donor Advice Funds which is a written agreement between the donor and the non profit organization.[20]It is the fastest growing technique for non profit organization funded mainly by private donors. In this contract a special fund is created by the private donor to donate as charity or for well being of society. In this type of contract there is an agreement between the organization and the donor which states that the non profit organization will respect the donor’s wishes while using funds. But the agreement is non-binding and the ultimate decision and control is in the hands of non profit organization. The nature of provider in the contract is advisory and can only give suggestions to the board of non profit research company and the ultimate decision lies with management.[21]

Contracts can be: (1) Fixed price contract when there is no uncertainty in the scope of work. The contractor is bound to complete the task within the agreed amount of money and time and is required to finish the task within a fixed amount. In this type of contract, the contractor bears the risk and the scope needs to be as detailed as possible[22]; (2) Cost reimbursable contract where the contractor is reimbursed for completed work and paid a certain amount representing the profit. In this type of contract, the buyer bears the risk since the buyer pays for all (allowable and reasonable) costs incurred by the contractor[23]; (3) Time and Materials contract when a contractor is paid on the basis of cost of labor specified hourly, actual cost of materials and equipment used, and an agreed upon amount to cover the contractor’s overhead with instructions not to exceed a certain limit. Here the risk is distributed between both buyer and seller[24].

Pricing Policy and Costing Methods: Price is the value charged for a product and pricing policy is the strategy by which the wholesale or retail price of the product is decided.[25]In developed countries the price of product is high due to high cost of R&D as compared to underdeveloped countries.[26]Various costing methods which could be used by organization are cost based, competition based and value based pricing. Cost based pricing is the price of product decided according to the cost plus a profit margin. Cost based pricing consider both the fixed plus variable cost of the product and adds a margin over it.[27]Competition based pricing is a pricing technique that considers the industry in which the firm is operating and the competition.[28]Finally, Value based pricing is the customer based pricing technique which is based on customers’ needs, habits and attitudes.[29]The pricing structure for a non-profit pharmaceutical company providing inexpensive drugs is cost based pricing method which includes the fixed and variable cost plus an addition of suitable profit margin to cover the expenses for instance Howard Hugh medical institute uses cost based pricing.[30]The company can also use three tiered pricing policy in which it could make the pricing strategies by dividing countries into groups. The drugs could be sold at marginal cost in those countries where there is hard strike of disease and can be sold at a higher price with profit margin to middle income countries for instance Abbott uses three tiered pricing policy.[31]GlaxoSmithKline was one of the first vaccine companies to adopt this approach – higher prices for high income countries; low prices in GAVI eligible countries; and intermediate prices in middle income countries.[32]

## References

Allen, S. ‘ Pricing Methods’. 2015. http://entrepreneurs. about. com/od/salesmarketing/a/pricingstrategy\_2. htm(Accessed 2015-3-9)

B. Barkin, TB Finance Manager, Bill & Melinda Gates Foundation (personal communication, March 13, 2015)

Basu, C.‘ Four Basic Types of Financial Ratios Used to Measure a Company’s Performance’. 2015. http://smallbusiness. chron. com/four-basic-types-financial-ratios-used-measure-companys-performance-25299. html(Accessed 2015-3-9)

Bate, R. & Boateng, K. ‘ Drug Pricing and Its Discontents’. 2007. http://www. aei. org/publication/drug-pricing-and-its-discontents/(Accessed 2015-3-10)

Business Dictionary. Cost reimbursable contract. http://www. businessdictionary. com/definition/cost-reimbursement-contract. html(Accessed 2015-3-10)

Business Dictionary. Time and materials contract. http://www. businessdictionary. com/definition/time-and-materials-T-M-contract. html(Accessed 2015-3-10)

Chabotar, k., J., “ Financial ratio analysis comes to nonprofits.” The Journal of Higher Education , 1989. pp. 188-208.

Chuang, J., and Marvin, S. “ Pricing multicast communication: A cost-based approach.” Telecommunication Systems, 2001, vol. 17, no. 3, pp. 281-297.

DCU. ‘ Charitable Planning: Donor Advised Funds vs. Private Foundations’. 2015. http://dcufinancial. org/new/dcufinancial/content. asp? contentid= 2017940795(Accessed 2015-3-10)

FRA. ‘ Financial Ratio Analysis’ 2013. http://www. demonstratingvalue. org/resources/financial-ratio-analysis(Accessed 2015-3-9)

Global Alliance for TB Drug Development. (2015)http://www. tballiance. org/about/operating-model. php(Accessed 2015-3-9).

GSK – Tiered pricing and vaccines. (2014)http://www. gsk. com/media/280905/tiered-pricing-for-vaccines-policy. pdf(Accessed 2015-3-13)

Herman, R. D., & Renz, D. O. ‘ Theses on nonprofit organizational effectiveness’. Nonprofit and voluntary sector quarterly , 1999, vol. 28 , no. 2, pp. 107-126.

Investorwords. Fixed Price Contract. http://www. investorwords. com/19291/fixed\_price\_contract. html(Accessed 2015-3-10)

Joskow, P. & Alvin, K. “ A framework for analyzing predatory pricing policy.” Yale Law Journal , 1979, pp. 213-270.

Kanter, R. M., & Summers, D. V. ‘ Doing well while doing good: Dilemmas of performance measurement in nonprofit organizations and the need for a multiple-constituency approach’. Sage publication, 1994, pp. 220-236.

Kaplan, R. “ Strategic performance measurement and management in nonprofit organizations.” Nonprofit management and Leadership, 2001, vol. 11, no. 3, pp. 353-370.

Mckeever, M.‘ Family Foundations: Donor Advised Funds and Supporting Organizations as Alternatives to Private Foundations’ . 1999. http://www. pgdc. com/pgdc/family-foundations-donor-advised-funds-and-supporting-organizations-alternatives-private-foundations(Accessed 2015-3-10).

NAF. “ Analyzing Financial Information Using Ratios”. 2014. https://nonprofitsassistancefund. org/sites/default/files/publications/nonprofit\_financial\_ratios\_2013. pdf(Accessed 2015-3-10).

Nagle, T., T., and Reed K., H., Strategy and tactics of pricing . Pearson Education Limited, 2013.

Salamon, L., M., “ The rise of the nonprofit sector.” Foreign Affairs , 1994, pp. 109-122.

Tuckman, H., P., and Cyril F. C., “ A methodology for measuring the financial vulnerability of charitable nonprofit organizations.” Nonprofit and Voluntary Sector Quarterly, 1991, vol. 20, no. 4, pp. 445-460.

Zall, M., ‘ The Pricing Puzzle’. 2006. http://pubs. acs. org/subscribe/archive/mdd/v04/i03/html/03zall. html(Accessed 2015-3-10).

Z, J., ‘ Nonprofit financial objectives and financial responses to a tough economy’. Journal of Corporate Treasury Management , 2010, vol. 3, no. 3, pp. 238-248.

[1] Global Alliance for TB Drug Development. (2015)http://www. tballiance. org/about/operating-model. php(Accessed 2015-3-9).

[2] R. M. Kanter, & D. V. Summers. ‘ Doing well while doing good: Dilemmas of performance measurement in nonprofit organizations and the need for a multiple-constituency approach’. Sage publication, 1994, pp. 220-236.

[3] Global Alliance for TB Drug Development. (2015)http://www. tballiance. org/about/operating-model. php(Accessed 2015-3-9).

[4] B. Barkin, TB Finance Manager, Bill & Melinda Gates Foundation (personal communication, March 13, 2015)

[5]R. D. Herman, & D. O. Renz. (1999). ‘ Theses on nonprofit organizational effectiveness’. Nonprofit and voluntary sector quarterly , 1999, vol. 28 , no. 2, pp. 107-126.

[6]FRA. ‘ Financial Ratio Analysis’. 2013. http://www. demonstratingvalue. org/resources/financial-ratio-analysis(Accessed 2015-3-9).

[7]R, Kaplan. ‘ Strategic performance measurement and management in nonprofit organizations’. Nonprofit management and Leadership, 2001, vol. 11, no. 3, pp. 353-370.

[8]FRA. ‘ Financial Ratio Analysis’. 2013. http://www. demonstratingvalue. org/resources/financial-ratio-analysis(Accessed 2015-3-9)

[9] B. Barkin, TB Finance Manager, Bill & Melinda Gates Foundation (personal communication, March 13, 2015)

[10]C, Basu. ‘ Four Basic Types of Financial Ratios Used to Measure a Company’s Performance’. 2015. http://smallbusiness. chron. com/four-basic-types-financial-ratios-used-measure-companys-performance-25299. html(Accessed 2015-3-9)

[11]J. K., Chabotar, ‘ Financial ratio analysis comes to nonprofits’. The Journal of Higher Education , 1989. pp. 188-208

[12]H, Tuckman, and C, Cyril. ‘ A methodology for measuring the financial vulnerability of charitable nonprofit organizations’. Nonprofit and Voluntary Sector Quarterly 20. 4 (1991): 445-460

[13]J. Zietlow, ‘ Nonprofit financial objectives and financial responses to a tough economy’. Journal of Corporate Treasury Management , 2010, vol. 3, no. 3, pp. 238-248.

[14]R, Kaplan. ‘ Strategic performance measurement and management in nonprofit organizations’. Nonprofit management and Leadership, 2001, vol. 11, no. 3, pp. 353-370.

[15]NAF. ‘ Analyzing Financial Information Using Ratios’. 2014. https://nonprofitsassistancefund. org/sites/default/files/publications/nonprofit\_financial\_ratios\_2013. pdf(Accessed 2015-3-10)

[16]H, Tuckman, and C, Cyril. ‘ A methodology for measuring the financial vulnerability of charitable nonprofit organizations’. Nonprofit and Voluntary Sector Quarterly 20. 4 (1991): 445-460

[17]J,, K.,. Chabotar, ‘ Financial ratio analysis comes to nonprofits’. The Journal of Higher Education , 1989. pp. 188-208

[18]NAF. ‘ Analyzing Financial Information Using Ratios’. 2014. https://nonprofitsassistancefund. org/sites/default/files/publications/nonprofit\_financial\_ratios\_2013. pdf(Accessed 2015-3-10)

[19]L., M. Salamon. ‘ The rise of the nonprofit sector’. Foreign Affairs , 1994, pp. 109-122.

[20]M. Mckeever.‘ Family Foundations: Donor Advised Funds and Supporting Organizations as Alternatives to Private Foundations’ . 1999. http://www. pgdc. com/pgdc/family-foundations-donor-advised-funds-and-supporting-organizations-alternatives-private-foundations(Accessed 2015-3-10).

[21]DCU. ‘ Charitable Planning: Donor Advised Funds vs. Private Foundations’. 2015. http://dcufinancial. org/new/dcufinancial/content. asp? contentid= 2017940795(Accessed 2015-3-10)

[22]Investorwords. Fixed Price Contract. http://www. investorwords. com/19291/fixed\_price\_contract. html(Accessed 2015-3-10)

[23]Business Dictionary. Cost reimbursable contract. http://www. businessdictionary. com/definition/cost-reimbursement-contract. html(Accessed 2015-3-10)

[24]Business Dictionary. Time and materials contract. http://www. businessdictionary. com/definition/time-and-materials-T-M-contract. html(Accessed 2015-3-10)

[25]P, Joskow & K, Alvin. ‘ A framework for analyzing predatory pricing policy’. Yale Law Journal , 1979, pp. 213-270.

[26]R. Bate, & K. Boateng.‘ Drug Pricing and Its Discontents’. 2007. http://www. aei. org/publication/drug-pricing-and-its-discontents/(Accessed 2015-3-10)

[27]John, Chuang & Sirbu, Marvin. ‘ Pricing multicast communication: A cost-based approach’. Telecommunication Systems, 2001, vol. 17, no. 3, pp. 281-297.

[28]T, T. Nagle, & H.,, K., Reed.‘ Strategy and tactics of pricing’ . Pearson Education Limited, 2013.

[29]S. Allen, ‘ Pricing Methods’. 2015. http://entrepreneurs. about. com/od/salesmarketing/a/pricingstrategy\_2. htm(Accessed 2015-3-9)

[30]M., Zall.. ‘ The Pricing Puzzle’. 2006. http://pubs. acs. org/subscribe/archive/mdd/v04/i03/html/03zall. html(Accessed 2015-3-10).

[31]R. Bate, & K. Boateng.‘ Drug Pricing and Its Discontents’. 2007. http://www. aei. org/publication/drug-pricing-and-its-discontents/(Accessed 2015-3-10)

[32]GSK – Tiered pricing and vaccines. (2014)http://www. gsk. com/media/280905/tiered-pricing-for-vaccines-policy. pdf(Accessed 2015-3-13)